SECURITIES AND EXCHANGE COMMISSION

FORM 10-K

Annual report pursuant to section 13 and 15(d)

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FILER

FMS FINANCIAL CORP
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SIC: **6036** Savings institutions, not federally chartered

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SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

FORM 10-K

(Mark One) ANNUAL REPORT PURSUANT TO SECTION 13 OR 15 (d) OF THE SECURITIES
|X| EXCHANGE ACT OF 1934

For the Fiscal Year Ended December 31, 1998

|_| TRANSITIONAL REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

For the transition period from ____________________ to _________________________

Commission File Number: 0-17353

FMS FINANCIAL CORPORATION

(Exact name of registrant as specified in its charter)

New Jersey	22-2916440
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)
3 Sunset Road, Burlington, New Jersey	08016
(Address of principal executive offices)	(Zip Code)

Registrant's telephone number, including area code: (609) 386-2400

Securities registered pursuant to Section 12(b) of the Act: None

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

Common Stock, par value $.10 per share

(Title of Class)

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

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

Based on the closing sales price of $9.00 per share of the registrant's common stock on March 1, 1999, as reported on the Nasdaq National Market System the aggregate market value of voting stock held by non-affiliates of the registrant was approximately $65.1 million. On such date, 7,231,767 shares of the registrant's Common Stock were outstanding.

DOCUMENTS INCORPORATED BY REFERENCE

1. Portions of 1998 Annual Report to Stockholders (Parts II and IV)
2. Portions of Proxy Statement for the 1999 Annual Meeting of Stockholders. (Part III)

PART I

Forward-Looking Statements

FMS Financial Corporation (the "Corporation") may from time to time make written or oral "forward-looking statements," including statements contained in the Corporation's filings with the Securities and Exchange Commission (including this Annual Report on Form 10-K and the exhibits thereto), in its reports to stockholders and in other communications by the Corporation, which are made in good faith by the Corporation pursuant to the "safe harbor" provisions of the private securities litigation reform act of 1995.

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These forward-looking statements involve risks and uncertainties, such as statements of the Corporation's plans, objectives, expectations, estimates and intentions, that are subject to change based on various important factors (some of which are beyond the Corporation's control). The following factors, among others, could cause the Corporation's financial performance to differ materially from the plans, objectives, expectations, estimates and intentions 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 Corporation conducts operations; the effects of, and changes in, trade, monetary and fiscal policies and laws, including interest rate policies of the board of governors of the federal reserve system, inflation, interest rate, market and monetary fluctuations; the timely development of and acceptance of new products and services of the Corporation and the perceived overall value of these products and services by users, including the features, pricing and quality compared to competitors' products and services; the willingness of users to substitute competitors' products and services for the Corporation's products and services; the success of the Corporation in gaining regulatory approval of its products and services, when required; the impact of changes in financial services' laws and regulations (including laws concerning taxes, banking, securities and insurance); technological changes, acquisitions; changes in consumer spending and saving habits; and the success of the Corporation at managing the risks involved in the foregoing.

The Corporation cautions that the foregoing list of important factors is not exclusive. The Corporation 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 Corporation.

Item 1. Business

General

FMS Financial Corporation, a New Jersey corporation, headquartered in Burlington, New Jersey, is the holding company for Farmers and Mechanics Bank (the "Bank"). The Bank principally operates through its twenty-three branch offices located throughout Burlington County, New Jersey.

The Bank is primarily engaged in the business of attracting deposits from the general public and originating loans which are secured by residential real estate. To a lesser extent, the Bank also originates consumer, commercial business loans and construction loans and invests in U.S. government securities and mortgage-related securities. The Bank has several subsidiaries which are currently either inactive or not material to the operations of the Bank.

Competition

The Bank's primary market area consists of Burlington County, New Jersey, and is one of many financial institutions serving this market area. The competition for deposit products comes from other insured financial institutions such as commercial banks, thrift institutions and credit unions in the Bank's market area. Deposit competition also includes a number of insurance products sold by local agents and investment products such as mutual funds and other securities sold by local and regional brokers. Loan competition comes from other insured financial institutions such as commercial banks, thrift institutions and credit unions.

Lending Activities

Analysis of Loan Portfolio

The following table sets forth the composition of the Bank's loan portfolio in dollar amounts and in percentages of the respective portfolios at the dates indicated.
<TABLE>
<CAPTION>

	December 31,									
	1998		1997		1996		1995		1994	
	Carrying Value	Percent of Total	Carrying Value	Percent of Total	Carrying Value	Percent of Total	Carrying Value	Percent of Total	Carrying Value	Percent of Total
	(In thousands)									
Mortgage loans:										
<S>	<C>	<C>	<C>	<C>	<C>	<C>	<C>	<C>	<C>	<C>
One-to-four family........	$246,072	81.11%	$253,001	82.43%	$257,451	82.89%	$249,278	85.30%	$245,874	85.65%
Commercial real estate....	45,938	15.14	42,974	14.00	39,177	12.61	34,721	11.88	32,228	11.23
Commercial construction...	2,609	.86	2,385	.78	4,395	1.42	--	--	--	--
Construction.............	1,410	.46	3,258	1.06	3,712	1.20	2,116	.73	2,924	1.02

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Total mortgage loans..	296,029	97.57	301,618	98.27	304,735	98.12	286,115	97.91	281,026	97.90
Consumer and other loans:										
Consumer..................	3,237	1.07	3,609	1.17	4,015	1.29	4,337	1.48	4,317	1.50
Commercial business.......	4,121	1.36	1,712	.56	1,830	.59	1,779	.61	1,712	.60
Total consumer and other loans...............	7,358	2.43	5,321	1.73	5,845	1.88	6,116	2.09	6,029	2.10
Total loans...........	$303,387	100.00%	306,939	100.00%	310,580	100.00%	292,231	100.00%	287,055	100.00%

</TABLE>

Residential Loans. One of the primary lending activities of the Bank has been the origination of conventional mortgage loans to enable borrowers to purchase existing homes, refinance existing mortgage loans or construct new homes. The Bank generally originates mortgage loans with terms of 15 to 30 years, amortized on a monthly basis, with principal and interest due each month. Typically, residential real estate loans remain outstanding for significantly shorter periods than their contractual terms because borrowers may refinance or prepay loans at their option.

The Bank presently offers mortgage loans that adjust every year after an initial fixed term of one, two, five or seven years, at an interest rate indexed higher than the corresponding U.S. Treasury security index. The interest rates on these mortgages adjust annually after the one, two, five or seven year anniversary date of the loan with an interest rate adjustment cap of 1.5% per year and presently not to exceed a rate of 11.5% over the life of the loan. At December 31, 1998, adjustable-rate residential first mortgage loans amounted to $55.1 million or 18.17% of the Bank's total loan portfolio. These loans are generally not originated under terms, conditions and documentation which permit their sale in the secondary mortgage market to Federal Home Loan Mortgage Corporation ("FHLMC") and Federal National Mortgage Association ("FNMA").

Fixed-rate mortgage loans are generally underwritten according to FHLMC and FNMA guidelines. The Bank sells fixed-rate loans in the secondary market from time to time when such sales are consistent with the Bank's asset/liability management goals and can be achieved on terms favorable

to the Bank. The Bank generally charges a higher interest rate on loans if the property is not owner-occupied. At December 31, 1998, $166.8 million or 55% of the Bank's total loan portfolio, consisted of long-term fixed-rate first mortgage loans of which none were classified as held for sale.

The Bank's lending policies generally limit the maximum loan-to-value ratio on owner-occupied residential first mortgage loans to 95% of the lesser of the appraised value or purchase price, with the condition that private mortgage insurance is required on loans with loan-to-value ratios in excess of 80%. Mortgage loans on investment properties are made by the Bank at loan-to-value ratios up to 70%. The loan-to-value ratio, maturity and other provisions of the loans made by the Bank have generally reflected the policy of making less than the maximum loan permissible under applicable regulations, in accordance with established lending practices, market conditions and underwriting standards maintained by the Bank. The Bank requires fire and casualty insurance on all properties securing real estate loans made by the Bank. The Bank also performs title searches to ensure its lien position.

The Bank actively solicits and originates home equity loans and equity reserve lines of credit secured by the equity in the borrower's primary residence. These loans generally have terms of 10 to 15 years, some of which are fixed rates and some of which have rates that adjust based upon the prime rate. At December 31, 1998, the Bank had home equity loans in the amount of $14.8 million or 4.88% of its total loan portfolio. Also at December 31, 1998, the Bank had approved $23.8 million in home equity lines of credit, of which $9.3 million was outstanding.

Construction Loans. The Bank originates loans to finance the construction of one-to-four family dwellings and/or commercial real estate. Generally, the Bank only makes interim construction loans to individuals if it also makes the permanent mortgage loan on the property. Construction loans to builders are generally made only if the Bank makes the permanent mortgage loan or if the builder has a contract for sale and the purchaser has received a permanent mortgage commitment. Interim construction loans to builders generally have terms of up to nine months and interest rates which adjust above the prime interest rate (generally 1% to 2%).

Construction financing is generally considered to involve a higher

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degree of risk of loss than long-term financing on improved, occupied real estate. Risk of loss on a construction loan is dependent largely upon the accuracy of the initial estimate of the property's value at completion of construction and development and the estimated cost (including interest) of construction. During the construction phase, a number of factors could result in delays and cost overruns. If the estimate of construction costs proves to be inaccurate, the Bank may be required to advance funds beyond the amount originally committed to permit completion of the development. If the estimate of value proves to be inaccurate, the Bank may be confronted, at or prior to the maturity of the loan, with a project having a value which is insufficient to assure full repayment.

Commercial Real Estate Loans. The Bank's commercial real estate loans are loans secured by commercial real estate (e.g., shopping centers, medical buildings, retail offices) and multi-family dwelling units (e.g., apartment projects with more than four units), in the Bank's market area. Commercial real estate loans and multi-family residential loans have been made in amounts up to $3.8 million, with most of such loans ranging in size from $100,000 to $1.0 million. Permanent loans on commercial properties are generally originated in amounts up to 75% of the appraised value of the property. The Bank's permanent commercial real estate loans are secured by improved property such as office buildings, retail stores, warehouse, church buildings and other non-residential buildings, most of which are located in the Bank's primary market area. Commercial real estate loans and multi-family residential loans are

generally made at rates which adjust above the prime interest rate (generally 1% to 2%) or a specified treasury index or are balloon loans with fixed interest rates which mature in three to five years with principal amortization for a period of up to 25 years.

Loans secured by commercial real estate are generally larger and involve a greater degree of risk than one-to-four family residential mortgage loans. Of primary concern, in commercial and multi-family real estate lending, is the borrower's creditworthiness and the feasibility and cash flow potential of the project. Loans secured by income properties are generally larger and involve greater risks than residential mortgage loans because payments on loans secured by income properties are often dependent on successful operation or management of the properties. As a result, repayment of such loans may be subject to a greater extent than residential real estate loans to adverse conditions in the real estate market or the economy.

Consumer. Regulations permit federally chartered thrift institutions to make secured and unsecured consumer loans up to 35% of the institution's assets. The Bank makes various types of secured and unsecured consumer loans including education loans, lines of credit, automobile loans (new and used) and loans secured by deposit accounts. Consumer loans generally have terms of six months to five years, some of which are at fixed rates and some of which have rates that adjust periodically.

Consumer loans are advantageous to the Bank because of their interest rate sensitivity, but they also involve more credit risk than residential mortgage loans because of the higher potential of defaults and the difficulties involved in disposing of the collateral, if any.

Commercial Business Loans. The Bank's commercial business loans are underwritten on the basis of the borrower's ability to service such debt from income. The Bank's commercial business loans are generally made to small and mid-sized companies located within the Bank's primary lending area. In most cases, the Bank requires additional collateral of equipment, chattel or other assets before making a commercial business loan.

Loan Commitments. The Bank issues loan origination commitments to real estate developers and qualified borrowers primarily for the construction, purchase and refinancing of residential real estate and commercial real estate. Such commitments are made on specified terms and conditions, including in most cases, the payment of a non-refundable commitment fee based on a percentage of the amount of committed funds. At December 31, 1998, the Bank had unused lines of credit and outstanding loan origination commitments of approximately $29.8 million.

Loan Origination and Loan Servicing Fees. The Bank receives loan origination fees or "points" for originating loans. Loan points are a percentage of the principal amount of the mortgage loan which are charged to the borrower for origination of the loan. The Bank's loan origination fees generally range from 2% to 3% on conventional residential mortgages and 1% to 2% on commercial real estate loans. All loan origination fees, net of incremental direct loan origination costs, are deferred and amortized over the contractual life of the related loans.

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At December 31, 1998, the Bank serviced for others 492 loans with an outstanding aggregate balance of $20.4 million. Loan servicing income for the years ended December 31, 1998, 1997 and 1996, was $68 thousand, $83 thousand and $98 thousand, respectively. Such loans were originated by the Bank and sold through the secondary mortgage market with the servicing rights to those loans retained

by the Bank. The loan servicing activities of the Bank include collecting and remitting loan payments, holding escrow funds for the payment of real estate taxes and insurance premiums and generally administering the loans.

Non-Performing and Problems Assets

When a loan is more than 30 days delinquent, the borrower will be contacted by mail or phone and payment requested. If the delinquency continues, subsequent efforts will be made to contact the delinquent borrower. In certain instances, the Bank may modify the loan or grant a limited moratorium on loan payments to enable the borrower to reorganize his financial affairs. If the loan continues in a delinquent status for 90 days or more, the Bank generally will initiate foreclosure proceedings.

Loans are generally placed on non-accrual status when either principal or interest is 90 days or more past due. Interest accrued and unpaid at the time a loan is placed on non-accrual status is charged against interest income by the establishment of a reserve on uncollected interest. Such interest, when ultimately collected, is credited to the income in the period received.

Non-Performing Assets. The following table sets forth information regarding impaired loans, troubled debt restructured and real estate owned assets by the Bank at the dates indicated.
<TABLE>
<CAPTION>

	At December 31,				
	1998	1997	1996	1995	1994
	(Dollars in Thousands)				
<S>	<C>	<C>	<C>	<C>	<C>
Loans accounted for on a non-accrual basis:					
Mortgage loans:					
One-to-four family............................	$ 1,733	$2,394	$2,413	$2,502	$1,446
Commercial real estate.........................	1,205	1,163	1,663	1,604	1,040
Consumer and other............................	282	80	15	6	469
Total mortgage non-accrual loans............	$ 3,220	$3,637	$4,091	$4,112	$2,955
Other nonaccrual loans..........................	--	--	--	$ 354	--
Troubled debt restructuring.....................	$ 477(1)	$ 684(1)	$ 560(1)	634(1)	$1,143
Real estate owned, net..........................	168	446	622	669	1,812
Other non-performing assets.....................	644	644	1,228	1,228	1,428
Total non-performing assets.....................	$ 4,509	$5,411	$6,501	$6,997	$7,338
Total non-accrual loans to net loans............	1.08%	1.20%	1.33%	1.43%	1.04%
Total non-accrual loans to total assets..........	.47%	.58%	.76%	0.82%	0.61%
Total non-performing assets to total assets......	.65%	.86%	1.20%	1.39%	1.52%

</TABLE>

----

(1) Loans restructured prior to SFAS Nos. 114 and 118 effective date and performing in accordance with the terms of the restructuring agreement.

Classified Assets. OTS regulations provide for a classification system for problem assets of insured institutions which covers all problem assets. Under this classification system, problem assets of insured institutions are classified as "substandard," "doubtful," or "loss." An asset is considered substandard if it is inadequately protected by the current net worth and paying capacity of the obligor or of the collateral pledged, if any. Substandard assets include those characterized by the "distinct possibility" that the insured institution will sustain "some loss" if the deficiencies are not corrected.

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Assets classified as doubtful have all of the weaknesses inherent in those classified substandard, with the added characteristic that the weaknesses present make "collection or liquidation in full," on the basis of currently existing facts, conditions, and values, "highly questionable and improbable." Assets classified as loss are those considered "uncollectible" and of such little value that their continuance as assets without the establishment of a specific loss reserve is not warranted. Assets may be designated "special mention" because of potential weaknesses that do not currently warrant classification in one of the aforementioned categories.

When an insured institution classifies problem assets as either substandard or doubtful, it may establish general allowances for loan losses in an amount deemed prudent by management. General allowances represent loss allowances which have been established to recognize the inherent risk associated with lending activities, but which, unlike specific allowances, have not been allocated to particular problem assets. When an insured institution classifies problem assets as loss, it is required either to establish a specific allowance for losses equal to 100% of that portion of the asset so classified or to charge off such amount. An institution's determination as to the classification of its assets and the amount of its valuation allowances is subject to review by the OTS, which may order the establishment of additional general or specific loss allowances. A portion of general loss allowances established to cover possible losses related to assets classified as substandard or doubtful may be included in determining an institution's regulatory capital, while specific valuation allowances for loan losses generally do not qualify as regulatory capital.

In accordance with its classification of assets policy, the Bank regularly reviews the problem assets in its portfolio to determine whether any assets require classification in accordance with applicable regulations. On the basis of management's review of its assets, at December 31, 1998, the Bank had $314 thousand, $6.8 million, and $9 thousand, classified as special mention, substandard, and loss assets.

Allowances for Loan Losses. It is management's policy to provide for losses on unidentified loans in its loan portfolio. A provision for loan losses is charged to operations based on management's evaluation of the potential losses that may be incurred in the Bank's loan portfolio. Such evaluation, which includes a review of all loans of which full collectibility of interest and principal may not be reasonably assured, considers the Bank's past loan loss experience, known and inherent risks in the portfolio, adverse situations that may affect the borrower's ability to repay, estimated value of any underlying collateral, and current economic conditions.

The following table sets forth the allocation of the allowance by category, which management believes can be allocated only on an approximate basis. The allocation of the allowance to each category is not necessarily indicative of future loss and does not restrict the use of the allowance to absorb losses in any category.

The following table sets forth an analysis of the Bank's allowance for loan losses for the periods indicated.
<TABLE>
<CAPTION>

	For the Year Ended December 31,				
	1998	1997	1996	1995	1994
	(Dollars in Thousands)				
<S>	<C>	<C>	<C>	<C>	<C>
Balance at beginning of period	$ 3,138	$ 2,782	$ 2,767	$ 2,622	$ 2,589
Loans charged-off:					
One-to-four family	(37)	(8)	(114)	(13)	(44)
Commercial real estate	--	--	--	--	--
Construction	--	--	--	--	--
Consumer	(1)	(40)	(1)	(6)	(37)
Commercial business	--	(1)	--	--	(38)
Total charge-offs	(38)	(49)	(115)	(19)	(119)
Recoveries	2	5	10	44	86
Net loans charged-off	(36)	(44)	(105)	25	(33)
Provision for possible loan losses	240	400	120	120	66
Balance at end of period	$ 3,342	$ 3,138	$ 2,782	$ 2,767	$ 2,622

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Ratio of net charge-offs to average loans outstanding during the period	0.012%	0.014%	0.035%	(0.009%)	0.012%

</TABLE>

Analysis of the Allowance for Loan Losses

The following table sets forth the breakdown of the allowance for loan losses by loan category and the percent of loans in each category to total loans receivable for the periods indicated. The allocation of the allowance to each category is not necessarily indicative of future losses and does not restrict the use of the allowances to absorb losses in any category.

<TABLE>
<CAPTION>

	At December 31,									
	1998		1997		1996		1995		1994	
	Amount	Percent of Loans to Total Loans	Amount	Percent of Loans to Total Loans	Amount	Percent of Loans to Total Loans	Amount	Percent of Loans to Total Loans	Amount	Percent of Loans to Total Loans
Loans:	(Dollars in Thousands)									
One-to-four family..............	$1,929	81.11%	$2,016	82.43%	$1,716	82.89%	$1,718	85.30%	$1,656	85.65%
Commercial real estate...........	1,232	15.14	954	14.00	877	12.61	819	11.88	757	11.23
Commercial construction..........	26	.86	24	.78	44	1.42	--	--	--	--
Construction.....................	14	.46	32	1.06	37	1.20	21	.73	29	1.02
Consumer and other...............	65	1.07	62	1.17	76	1.29	68	1.48	70	1.50
Commercial business..............	76	1.36	50	.56	32	.59	141	.61	110	.60
Total allowance for loan losses	$3,342	100.00%	$3,138	100.00%	$2,782	100.00%	$2,767	100.00%	$2,622	100.00%

</TABLE>

Investment Activities and Mortgage-Backed Securities

General. The Bank is required under federal regulations to maintain a minimum amount of liquid assets which may be invested in specified short term securities and certain other investments. The Bank has maintained a liquidity portfolio in excess of regulatory requirements. Liquidity levels may be increased or decreased depending upon the yields on investment alternatives and upon management's judgment as to the attractiveness of the yields then available in relation to other opportunities and its expectation of future yield levels, as well as management's projections as to the short term demand for funds to be used in the Bank's loan origination and other activities. The Bank classifies its investments as securities available-for-sale or investments securities held-to-maturity in accordance with SFAS No. 115. At December 31, 1998, the Bank's investment portfolio policy allowed investments in instruments such as U.S. Treasury obligations, U.S. federal agency or federally sponsored agency obligations, municipal obligations, mortgage-backed securities, banker's acceptances, certificates of deposit, federal funds, including FHLB overnight and term deposits, as well as investment grade corporate bonds, commercial paper and the mortgage derivative products described below. The Bank's Board of Directors may authorize additional investments.

The Bank's securities available-for-sale and investment securities held-to-maturity portfolios at December 31, 1998 did not contain securities of any issuer with an aggregate book value in excess of 10% of the Bank's equity, excluding those issued by the United States Government or its agencies.

Mortgage-Backed Securities. To supplement lending activities, the Bank has invested in residential mortgage-backed securities ("MBS"). Mortgage-backed securities can serve as collateral for borrowings and, through repayments, as a source of liquidity. Mortgage-backed securities represent a participation interest in a pool of single-family or other type of mortgages, the principal and interest payments on which are passed from the mortgage originators, through

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intermediaries (generally quasi-governmental agencies) that pool and repackage the participation interests in the form of securities, to investors such as the Bank. Such quasi-governmental agencies, which guarantee the payment of principal and interest to investors, primarily include FHLMC, Government National Mortgage Association ("GNMA"), and FNMA.

Mortgage-backed securities typically are issued with stated principal amounts and the securities are backed by pools of mortgages that have loans with interest rates that are within a range and have varying maturities. The underlying pool of mortgages can be composed of either fixed-rate or adjustable-rate mortgage loans. Mortgage-backed securities are generally referred to as mortgage participation certificates or pass-through certificates. As a result, the interest rate risk characteristics of the underlying pool of mortgages (i.e., fixed-rate or adjustable-rate), as well as prepayment risk, are passed on to the certificate holder. The life of a mortgage-backed pass-through security is equal to the life of the underlying mortgages.

The following table sets forth the carrying value and market value of the Bank's mortgage backed securities and investment securities held to maturity and securities available for sale, FHLB stock, and interest bearing deposits and overnight investments at the dates indicated.

<TABLE>
<CAPTION>

	At December 31,					
	1998		1997		1996	
	Carrying Value	Estimated Market Value	Carrying Value	Estimated Market Value	Carrying Value	Estimated Market Value
	(In Thousands)					
Investment securities held to maturity:						
<S>	<C>	<C>	<C>	<C>	<C>	<C>
U.S. government and agency securities.......	$ 78,292	$ 78,242	$ 79,347	$ 79,498	$ 46,792	$ 46,156
Reverse repurchase agreements..............	--	--	30,185	30,185	20,000	20,000
Municipal bonds............................	3,824	3,827	2,802	2,816	795	800
U.S. treasuries............................	--	--	15	14	15	14
CMO's......................................	47,302	47,297	--	--	--	--
MBS..	90,593	92,262	92,021	94,307	104,313	105,558
Investment securities available for sale:						
U.S. agencies..............................	18,501	18,501	7,871	7,871	4,997	4,997
U.S. treasuries............................	--	--	--	--	1,999	1,999
CMO's......................................	91,332	91,332	72,468	72,468	18,451	18,451
Total investment securities............	329,844	331,461	284,709	287,159	197,362	197,975
Federal Home Loan Bank of New York stock ...	4,861	4,861	3,631	3,631	3,621	3,621
Interest bearing deposits and overnight investments..............................	--	--	827	827	347	347
Total investments.......................	$334,705	$336,322	$289,167	$291,617	$201,330	$201,943

</TABLE>

The following table sets forth the scheduled maturities, carrying values, market values and average yields for the Bank's investment securities at December 31, 1998.

<TABLE>
<CAPTION>

	One Year or Less		One to Five Years		Five to Ten Years		More than Ten Years		Total Investment Securities		
	Carrying Value	Average Yield	Carrying Value	Average Yield	Carrying Value	Average Yield	Carrying Value	Average Yield	Carrying Value	Market Value	Average Yield
	(Dollars in Thousands)										
<S>	<C>	<C>	<C>	<C>	<C>	<C>	<C>	<C>	<C>	<C>	<C>
Investment securities held to maturity:											
U.S. government and agency obligations...........	$ --	--%	$ 5,000	6.05%	$53,387	6.33%	$ 19,905	6.96%	$ 78,292	$78,242	6.47%
Municipal bond..............	3,594	3.91	--	--	--	--	230	5.60	3,824	3,827	4.01

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CMO's	--	--	--	--	5,456	6.50	41,846	6.69	47,302	47,297	6.66
MBS..........................	1,008	6.84	5,166	7.17	7,253	7.54	77,166	7.19	90,593	92,262	7.21
Investment securities available for sale:											
U.S. Government and Agency......................	--	--	--	--	17,503	6.46	998	7.00	18,501	18,501	6.49
CMO's........................	--	--	354	7.00	9,537	5.85	81,442	6.84	91,332	91,333	6.73
Total......................	$4,602	4.56%	$10,520	6.63%	$93,136	6.39%	$221,587	6.94%	$329,844	$331,461	6.74%

</TABLE>

Sources of Funds

General. Deposits are the major external source of the Bank's funds for lending and other investment purposes. The Bank derives funds from amortization and prepayment of loans and, to a lesser extent, maturities of investment securities, borrowings, mortgage-backed securities and operations. Scheduled loan principal repayments are a relatively stable source of funds, while deposit inflows and outflows and loan prepayments are significantly influenced by general interest rates and market conditions.

Deposits. Deposits are attracted from within the Bank's primary market area of Burlington County, New Jersey, through the offering of a broad selection of deposit instruments including regular checking accounts, non-interest checking accounts, money market accounts, regular passbook accounts, certificates of deposit and IRA accounts. Deposit account terms vary according to the minimum balance required, the time periods the funds must remain on deposit and the interest rate, among other factors. The Bank regularly evaluates the internal cost of funds, surveys rates offered by competing institutions, reviews the Bank's cash flow requirements for lending and liquidity and executes rate changes when deemed appropriate. The Bank does not have any brokered deposits and has no present intention to accept or solicit such deposits.

Certificates of Deposit in Excess of $100,000. The following table indicates the amount of the Bank's certificates of deposit of $100,000 or more by time remaining until maturity as of December 31, 1998.

Maturity Period of Deposits	Certificates of Deposit
	(In Thousands)
Three months or less............	$ 11,541
Three through six months.........	4,966
Six through twelve months........	4,650
Over twelve months..............	5,647
Total......................	$ 26,804

Deposit Rate. The following table sets forth the distribution of the Bank's average balance of deposit accounts at the dates indicated and the weighted average nominal interest rates on each category of deposits presented.
<TABLE>
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	At December 31, 1998			1997			1996		
	Average Balance	Percent of Total Deposits	Weighted Average Nominal Rate	Average Balance	Percent of Total Deposits	Weighted Average Nominal Rate	Average Balance	Percent of Total Deposits	Weighted Average Nominal Rate
	(Dollars In Thousands)								
<S>	<C>	<C>	<C>	<C>	<C>	<C>	<C>	<C>	<C>
Passbook and regular savings....	$ 84,480	16.31%	2.53%	$ 73,802	15.6%	2.56%	$69,666	16.22%	2.52%
Checking accounts..............	128,259	24.76	1.89	89,418	18.8	.92	72,427	16.87	.96

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Money market deposit accounts...	62,099	11.99	2.64	59,797	12.6	2.72	57,399	13.37	2.65
Certificates of deposit.........	234,471	45.26	5.35	243,381	51.3	5.32	228,974	53.32	5.30
Surrogate statement.............	8,714	1.68	5.80	7,860	1.7	5.80	947	.22	6.12
Total Deposits................	$518,023	100.00%	3.49%	$474,258	100.00%	3.74%	$429,413	100.00%	3.77%

</TABLE>

Personnel

As of December 31, 1998 the Corporation, including its subsidiaries, had 226 full-time employees and 141 part-time employees. The employees are not represented by a collective bargaining unit. Management believes its relationship with its employees is good.

Regulation

Set forth below is a brief description of certain laws which are related to the regulation of the Corporation and the Bank. The description does not purport to be complete and is qualified in its entirety by reference to applicable laws and regulations.

Regulation of the Corporation

General. The Corporation is a unitary savings and loan holding company subject to regulatory oversight by the OTS. As such, the Corporation is required to register and file reports with the OTS and is subject to regulation and examination by the OTS. In addition, the OTS has enforcement authority over the Corporation and its non-savings association subsidiaries which also permits the OTS to restrict or prohibit activities that are determined to be a serious risk to the subsidiary savings association. This regulation and oversight is intended primarily for the protection of the depositors of the Bank and not for stockholders of the Corporation.

Qualified Thrift Lender Test. As a unitary savings and loan holding company, the Corporation generally is not subject to activity restrictions, provided the Bank satisfies the Qualified Thrift Lender ("QTL") test or a somewhat similar test for domestic building and loan associations. If the Corporation acquires control of another savings association as a separate subsidiary, it would become a multiple savings and loan holding company, and the activities of the Corporation and any of its subsidiaries (other than the Bank or any other SAIF-insured savings association) would become subject to restrictions applicable to bank holding companies unless such other associations each also qualify as a QTL and were acquired in a supervisory acquisition. See "-- Regulation of the Bank -- Qualified Thrift Lender Test."

Regulation of the Bank

General. As a federally-chartered, SAIF-insured savings bank, the Bank is subject to extensive regulation by the OTS and the FDIC. Lending activities and other investments must comply with various federal statutory and regulatory requirements. The Bank is also subject to certain reserve requirements promulgated by the Federal Reserve Board.

The OTS, in conjunction with the FDIC, regularly examines the Bank and prepares reports for the consideration of the Bank's Board of Directors on any deficiencies that they find in the Bank's operations. The Bank's relationship with its depositors and borrowers is also regulated to a great extent by federal law, especially in such matters as the ownership of savings accounts and the form and content of the Bank's mortgage documents.

The Bank must file reports with the OTS and the FDIC concerning its activities and financial condition, in addition to obtaining regulatory approvals prior to entering into certain transactions such as mergers with or acquisitions of other savings institutions. This regulation and supervision establishes

a comprehensive framework of activities in which an institution can engage and

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is intended primarily for the protection of depositors. The regulatory structure also gives the regulatory authorities extensive discretion in connection with their supervisory and enforcement activities and examination policies, including policies with respect to the classification of assets and the establishment of adequate loan loss reserves for regulatory purposes. Any change in such regulations, whether by the OTS, the FDIC or the Congress could have a material adverse impact on the Corporation, the Bank and their operations.

Insurance of Deposit Accounts. The Bank's deposit accounts are insured by the SAIF to a maximum of $100,000 for each insured member (as defined by law and regulation). Insurance of deposits may be terminated by the FDIC upon a finding that the institution has engaged in unsafe or unsound practices, is in an unsafe or unsound condition to continue operations or has violated any applicable law, regulation, rule, order or condition imposed by the FDIC or the institution's primary regulator.

Prior to January 1, 1997, as a member of the SAIF, the Bank paid an insurance premium to the FDIC equal to a minimum of 0.23% of its total deposits. The FDIC also maintains another insurance fund, the Bank Insurance Fund ("BIF"), which primarily insures commercial bank deposits. In 1996, the annual insurance premium for most BIF members was lowered to $2,000. The lower insurance premiums for BIF members placed SAIF members at a competitive disadvantage to BIF members.

Effective September 30, 1996, federal law was revised to mandate a one-time special assessment on SAIF members such as the Bank of approximately .657% of deposits held on March 31, 1995. Beginning January 1, 1997, the deposit insurance assessment for SAIF members was reduced to .064% of deposits on an annual basis through the end of 1999. During this same period, BIF members will be assessed approximately .013% of deposits. After 1999, assessments for BIF and SAIF members should be the same. It is expected that these continuing assessments for both SAIF and BIF members will be used to repay outstanding Financing Corporation bond obligations. As a result of these changes, beginning January 1, 1997, the rate of deposit insurance assessed the Corporation declined by approximately 70%.

Regulatory Capital Requirements. OTS capital regulations require savings institutions to meet three capital standards: (1) tangible capital equal to 1.5% of total adjusted assets, (2) a leverage ratio (core capital) equal to at least 3% of total adjusted assets, and (3) a risk-based capital requirement equal to 8.0% of total risk-weighted assets. In addition, the OTS prompt corrective action regulation provides that a savings institution that has a leverage capital ratio of less than 4% (3% for institutions receiving the highest examination rating) will be deemed to be "undercapitalized" and may be subject to certain restrictions.

Dividend and Other Capital Distribution Limitations. Current OTS regulations require the Bank to give the OTS 30 days advance notice of any proposed declaration of dividends to the Corporation and the OTS has the authority under its supervisory powers to prohibit the payment of dividends to the Corporation.

Current OTS regulations impose limitations upon all capital distributions by savings institutions, such as cash dividends, payments to repurchase or otherwise acquire its shares, payments to shareholders of another institution in a cash-out merger and other distributions charged against capital. The rule establishes three tiers of institutions, based primarily on an institution's capital level. An institution that exceeds all requirements before and after a proposed capital distribution ("Tier 1 institution") and has not

been advised by the OTS that it is in need of more than the normal supervision can, after prior notice, but without the approval of the OTS, make capital distributions during a calendar year equal to the greater of (i) 100% of its net income to date during the calendar year plus the amount that would reduce by one-half its "surplus capital ratio" (the excess over its capital requirements) at the beginning of the calendar year, or (ii) 75% of its net income over the most recent four quarter period. Any additional capital distributions require prior regulatory approval. As of December 31, 1998, the Bank was a Tier 1 institution. In the event the Bank's capital fell below its requirement or the OTS notified it that it was in need of more than normal supervision, the Bank's ability to make capital distributions could be restricted. In addition, the OTS could prohibit a proposed capital distribution by any institution, which would otherwise be permitted by the regulation, if the OTS determines that such distribution would constitute an unsafe or unsound practice.

Qualified Thrift Lender Test. HOLA requires savings institutions to meet a qualified thrift lender ("QTL") test. If the Bank maintains an appropriate level of Qualified Thrift Investments (primarily residential mortgages and related investments, including certain mortgage-backed securities)

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("QTIs") and otherwise qualifies as a QTL, it will continue to enjoy full borrowing privileges from the FHLB of New York. The required percentage of QTIs is 65% of portfolio assets (defined as all assets minus intangible assets, property used by the institution in conducting its business and liquid assets equal to 10% of total assets). Certain assets are subject to a percentage limitation of 20% of portfolio assets. In addition, savings associations may include shares of stock of the FHLBs, FNMA and FHLMC as qualifying QTIs. As of December 31, 1998, the Bank was in compliance with its QTL requirement with 92.31% of its assets invested in QTIs.

Loans-to-One Borrower. Under the HOLA, as amended, savings institutions are subject to the national bank limits on loans-to-one borrower. Generally, a savings association may not make a loan or extend credit to a single or related group of borrowers in excess of 15% of the association's unimpaired capital and surplus. An additional amount may be lent, equal to 10% of unimpaired capital and surplus, if such loan is secured by readily-marketable collateral, which is defined to include certain securities and bullion, but generally does not include real estate. The Bank does not have any loans-to-one borrower which exceed these limits.

Federal Home Loan Bank System. The Bank is a member of the FHLB of New York, which is one of 12 regional FHLBs that administers the home financing credit function of savings associations. Each FHLB serves as a reserve or central bank for its members within its assigned region. It is funded primarily from proceeds derived from the sale of consolidated obligations of the FHLB System. It makes loans to members (i.e., advances) in accordance with policies and procedures established by the Board of Directors of the FHLB.

As a member, the Bank is required to purchase and maintain stock in the FHLB of New York in an amount equal to at least 1% of its aggregate unpaid residential mortgage loans, home purchase contracts or similar obligations at the beginning of each year.

Federal Reserve System. The Federal Reserve Board requires all depository institutions to maintain non-interest bearing reserves at specified levels against their transaction accounts (primarily non-interest checking and interest-bearing checking accounts) and non-personal time deposits. The balances maintained to meet the reserve requirements imposed by the Federal Reserve Board may be used to satisfy the liquidity requirements that are imposed by the OTS.

Item 2. Properties

The Bank conducts its business through its two administrative offices located in Burlington, New Jersey and its 23 branch locations in Burlington County, New Jersey. All of the Bank's office and branch facilities are owned by the Bank, except for two branch office locations in Lumberton and Medford, New Jersey. Management of the Bank considers the physical condition of each of the Bank's administrative and branch offices to be good and adequate for the conduct of the Bank's business.

Item 3. Legal Proceedings

The Bank is periodically involved as a plaintiff or defendant in various legal actions, such as actions to enforce liens, condemnation proceedings on properties in which the Bank holds mortgage interests, matters involving the making and servicing of mortgage loans and other matters incident to the Bank's business. In the opinion of management, none of these actions individually or in the aggregate is believed to be material to the financial condition or results of operations of the Bank.

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

No matters were submitted to a vote of security holders during the fourth quarter of the fiscal year ended December 31, 1998.

Part II

Item 5. Market for the Registrant's Common Equity and Related Stockholder Matters

The information contained under the section captioned "Stock Market Information" in the Corporation's 1998 Annual Report to Stockholders (the "Annual Report") is incorporated herein by reference.

Item 6. Selected Financial Data

The information contained in the table captioned "Financial Highlights" in the Annual Report is incorporated herein by reference.

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

The information contained in the section captioned "Management's Discussion and Analysis of Financial Condition and Results of Operations" in the Annual Report is incorporated herein by reference.

Item 7A. Quantitative and Qualitative Disclosures About Market Risk

The information contained in the section captioned "Asset and Liability Management" in the Annual Report is incorporated herein by reference.

Item 8. Financial Statements and Supplementary Data

The Corporation's financial statements listed in Item 14 herein are incorporated herein by reference.

Item 9. Changes in and Disagreements with Accountants on Accounting and Financial Disclosure

None.

Part III

Item 10. Directors and Executive Officers of the Registrant

The information contained under the sections captioned "Section 16(a) Beneficial Ownership Reporting Compliance" and "I - Information with Respect to Nomineed for Director, Directors Continuing in Office, and Executive Officers - Election of Directors" and "- Biographical Information" in the 1999 Proxy Statement are incorporated herein by reference.

Executive Officers of the Company Who Are Not Directors

Name and Title	Age as of December 31, 1998
Channing L. Smith Vice President and Chief Financial Officer	55
James E. Igo Senior Vice President and Chief Lending Officer	42
Thomas M. Topley Senior Vice President and Corporate Secretary	38

Channing L. Smith has served as Vice President and Chief Financial Officer of the Corporation and the Bank since October 1994. In this capacity, he is responsible for the management of the accounting, treasury, and investments of the Bank. From April 1994 to October 1994, he served as controller of the Corporation and the Bank. From January 1990 to April 1993 he served as corporate Controller for Circuit Foil USA.

James E. Igo has served as Senior Vice President and Senior Mortgage Lending Officer of the Corporation and the Bank since November 1991. In that capacity, he is responsible for overall loan production, credit quality, product development, loan servicing and the creation of lending policies and procedures. From September 1990 to November 1991, he served as the Vice President, Commercial Lending of the Corporation and the Bank. Prior to 1990, Mr. Igo was Senior Vice President and Senior Lending Officer for a commercial bank.

Thomas M. Topley has served as Senior Vice President of Operations since April 1993 and as Corporate Secretary of the Corporation and the Bank since April 1992. In that capacity, he is responsible for corporate records, retail branch administration, human resources, data processing and accounting operations. From June 1990 to April 1993, Mr. Topley served as Vice President and Controller for the Bank.

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Item 11. Executive Compensation

The information contained under the section captioned "Proposal I -- Election of Directors - Executive Compensation" in the Proxy Statement is incorporated herein by reference.

Item 12. Security Ownership of Certain Beneficial Owners and Management

(a) Security Ownership of Certain Beneficial Owners

Information required by this item is incorporated herein by reference to the Section captioned "Voting Securities and Principal Holders Thereof" of the Proxy Statement.

(b) Security Ownership of Management

Information required by this item is incorporated herein by reference to the section captioned "Proposal I -- Election of Directors" of the Proxy Statement.

(c) Management of the Corporation knows of no arrangements, including any pledge by any person of securities of the Corporation, the operation of which may at a subsequent date result in a change in control of the registrant.

Item 13. Certain Relationships and Related Transactions

The information required by this item is incorporated herein by reference to the section captioned "Proposal I -- Election of Directors" and "Voting Securities and Principal Holders Thereof" of the Proxy Statement.

Part IV

Item 14. Exhibits, Financial Statements, and Reports on Form 8-K

(a) Listed below are all financial statements and exhibits filed as part of this report, and are incorporated by reference.

1. The consolidated statements of financial conditions of FMS Financial Corporation and subsidiary as of December 31, 1998 and 1997, and the related consolidated statements of income, changes in stockholders' equity and cash flows for each of the years in the three year period ended December 31, 1998, together with the related notes and the independent auditors' report of PricewaterhouseCoopers, LLP, independent accountants.

2. Schedules omitted as they are not applicable.

3. Exhibits

The following Exhibits are filed as part of this report:

3.1 Certificate of Incorporation (Incorporated by reference to the Registrant's Form S-1 Registration Statement No. 33-24340).
3.2 Bylaws (Incorporated by reference to the Registrant's Form S-1 Registration Statement No. 33-24340).
4 Agreement to furnish copy to Securities and Exchange Commission upon request of Indenture dated July 28, 1994, relating to 10% Subordinated Debentures due 2004 in aggregate principal amount of $10 million. (Incorporated by reference to Registrant's Annual Report on Form 10-K for the fiscal year ended December 31, 1994).
10.1 Stock Option and Incentive Plan (Incorporated by reference to the Registrant's Form S-8 Registration Statement No. 33-24340).
13 1998 Annual Report to Stockholders
21 Subsidiaries of the Registrant
23 Consent of Independent Auditors
27 Financial Data Schedule (electronic filing only)

(b) No Reports on Form 8-K were filed during the last quarter of the fiscal year covered by this Report.

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SIGNATURES

Pursuant to the requirements of Section 13 or 15(d) of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned, thereunto duly authorized as of March 26, 1999.

FMS FINANCIAL CORPORATION

By: /s/ Craig W. Yates

Craig W. Yates, President and
Chief Executive Officer
(Duly Authorized Representative)

Pursuant to the requirement of the Securities Exchange Act of 1934, this report has been signed below on March 26, 1999 by the following persons on behalf of the registrant and in the capacities indicated.

/s/ Charles B. Yates

Charles B. Yates
Chairman of the Board

/s/ Craig W. Yates

Craig W. Yates
President, Chief Executive Officer
and Director
(Principal Executive Officer)

/s/ George J. Barber

George J. Barber, Director

/s/ Channing L. Smith

Channing L. Smith
Vice President and Chief Financial Officer
(Principal Financial and Accounting Officer)

/s/ Edward J. Staats, Jr.

Edward J. Staats, Jr., Director

/s/ Wayne H. Page

Wayne H. Page, Director

/s/ James C. Lignana

James C. Lignana, Director

/s/ Dominic W. Flamini

Dominic W. Flamini, Director

/s/ Vincent R. Farias

Vincent R. Farias, Director

/s/ Ruppert A. Hall, Jr.

Ruppert A. Hall, Jr., Director

/s/ Mary Wells

Mary Wells, Director

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CORPORATE PROFILE

FMS Financial Corporation is the holding company for Farmers & Mechanics Bank. Farmers & Mechanics Bank, with total assets of $692 million, is the largest community bank headquartered in its primary market area of Burlington County, New Jersey.

Founded in Burlington City in 1871 under the name of Farmers' and Mechanics' Building and Loan Association, the Bank operates twenty-three banking offices, all of which are in Burlington County, New Jersey.

The daily stock quotation for FMS Financial Corporation is listed in the Nasdaq National Market System published in The Wall Street Journal, the Philadelphia Inquirer and other leading newspapers under the trading symbol of FMCO.

FINANCIAL HIGHLIGHTS

Financial Condition: (In Thousands)

December 31,	1998	1997	1996 (a)	1995	1994
Assets	$691,812	$628,403	$541,710	$501,550	$483,776
Loans receivable and loans held for sale, net	298,603	302,831	306,871	288,400	283,260
Deposits	536,310	489,440	453,277	428,809	429,431
Stockholders' equity	43,469	38,916	33,826	33,053	29,159

Operations: (In Thousands, except earnings per share data)

Year Ended December 31,	1998	1997	1996 (a)	1995	1994
Interest income	$46,563	$40,813	$36,841	$35,201	$32,270
Interest expense	24,869	20,879	18,978	18,041	15,336
Net interest income	21,694	19,934	17,863	17,160	16,934
Net income	5,271	5,491	3,026	4,343	4,455
Basic earnings per common share	0.73	0.77	0.41	0.58	0.58
Diluted earnings per common share	0.72	0.75	0.40	0.56	0.56
Dividends declared per common share	0.11	0.08	0.07	0.07	0
Weighted average common shares outstanding	7,204	7,165	7,411	7,512	7,728
Weighted average common shares and common stock equivalents outstanding	7,314	7,346	7,573	7,695	7,926

Other Selected Data:

Year Ended December 31,	1998	1997	1996 (a)	1995	1994
Net interest rate spread	3.50%	3.60%	3.50%	3.49%	3.64%

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Net interest margin	3.48	3.72	3.66	3.66	3.72
Return on average assets	0.85	0.98	0.60	0.89	0.94
Dividend payout ratio	15.28	10.67	17.50	12.43	0.00
Equity-to-asset ratio	6.28	6.19	6.24	6.59	6.03

</TABLE>

(a) Includes $2.7 million for the one-time assessment to recapitalize the SAIF.

To Our Shareholders:

Farmers & Mechanics Bank had satisfactory financial results for 1998 and continued to make progress in expanding our branch system and improving customer service.

Deposits and assets continued to increase, but operating results declined moderately due to the lower interest rate environment and higher operating costs. We have continued to achieve significant growth in our core deposit base of checking and savings accounts. Business and local government deposits have also increased.

During December, 1998 we changed our computer system from a main frame system which was once again approaching capacity limits to a new client-server PC based system. This "conversion" required a year long process of preparation and training. This change was virtually seamless to our customers but there continues to be further work for our staff on changes and enhancements. The new system will give us greater flexibility and allow further program additions and improvements in the future.

We are continuing to improve our coverage of the Burlington County market area. During 1998 we increased our branches to 22 with the opening of a temporary branch in Browns Mills and construction of a new branch in Cinnaminson, New Jersey. Early in 1999 we have opened additional branches in Medford Village and Chesterfield, in facilities purchased from larger banks that were consolidating. During April, we will open a temporary branch in Riverside in a recently purchased old bank building that will get extensive further renovation. Later in the year, we plan to begin construction of new branches in Burlington and Pemberton, and remodel and open a branch in Mt. Holly. More branch locations, combined with our long hours and seven day banking, increase our cost of operations and reduce current profitability, but are an important investment in the growth of our franchise.

Once again, we wish to thank our customers, our staff, and our shareholders for their continued support.

Sincerely,

/s/ Craig W. Yates	/s/ Charles B. Yates
Craig W. Yates President	Charles B. Yates Chairman

MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

General

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The Private Securities Litigation Reform Act of 1995 contains safe harbor provisions regarding forward-looking statements. When used in this discussion, the words "believes", "anticipates", "contemplates", "expects", and similar expressions are intended to identify forward-looking statements. Such statements are subject to certain risks and uncertainties which could cause actual results to differ materially from those projected. Those risks and uncertainties include changes in interest rates, risks associated with the effect of opening a new branch, the ability to control costs and expenses, and general economic conditions. FMS Financial Corporation undertakes no obligation to publicly release the results of any revisions to those forward looking statements which may be made to reflect events or circumstances after the date hereof or to reflect the occurrence of unanticipated events.

FMS Financial Corporation ("the Corporation") is the parent company of Farmers & Mechanics Bank ("the Bank"), its only subsidiary. Earnings of the Corporation are primarily dependent on the earnings of the Bank as the Corporation has engaged in no significant operations of its own. Accordingly, the earnings of the Corporation are largely dependent on the receipt of earnings from the Bank in the form of dividends.

The earnings of the Bank depend primarily on its net interest income. Net interest income is affected by: (i) the volume of interest-earning assets and interest-bearing liabilities (see "Rate Volume Analysis"), (ii) rates of interest earned on interest-earning assets and rates paid on interest-bearing liabilities and (iii) the difference ("interest rate spread") between average rates of interest earned on interest-earning assets and average rates paid on interest-bearing liabilities. When interest-earning assets approximate or exceed interest-bearing liabilities, any positive interest rate spread will generate net interest income.

The Bank also derives income from service charges on customer deposit accounts and fees on loans. In addition to interest expense, the Bank incurs operating expenses such as salaries, employee benefits, deposit insurance premiums, depreciation, property maintenance and advertising.

Market Risk

Market risk is the risk of loss from adverse changes in market risk prices and rates. The Bank's market risk arises primarily from interest rate risk inherent in its lending, investment and deposit taking activities. The Bank's profitability is affected by fluctuations in interest rates. A sudden and substantial increase in interest rates may adversely impact the Bank's earnings to the extent that the interest rates borne by assets and liabilities do not change at the same speed, to the same extent or on the same basis. To that end, management actively monitors and manages its interest rate risk exposure. The Bank does not participate in hedging programs, interest rate swaps or other activities involving the use of off-balance sheet derivative financial instruments, but may do so in the future to mitigate interest rate risk. The Bank's policy allows investment only in securities which have a rating of AA or better. The Bank holds a substantial component of its investment portfolio in mortgage-backed securities and collateralized mortgage obligations (collectively, "MBS"). At the end of 1998, the total investment in MBS amounted to $229 million, or 68% of total investments. These are instruments collateralized by pools of residential and commercial mortgages which return interest and principal payments to the investor. Approximately 39% of the Bank's MBS holdings are U.S. Government Agency securities (GNMA, FNMA and FHLMC), which carry either direct government or quasi-government guarantees and are rated AAA in terms of quality. The Bank also owns non-agency MBS, issued by major financial institutions, which are rated AAA and AA. MBS are generally very liquid issues with major brokerage houses providing ready markets. However, MBS are subject to prepayment and extension risk which can adversely affect their yields and expected maturities. MBS of $1.7 million and $1.2 million were used to secure

public funds on deposit at December 31, 1998 and 1997, respectively.

Interest rate risk is the risk of loss in value due to changes in interest rates. This risk is addressed by the Bank's Asset Liability Management Committee ("ALCO"), which includes senior management. The ALCO monitors and considers methods of managing interest rate risk by monitoring changes in the interest rate repricing GAP ("GAP"), the net portfolio values ("NPV") and net interest income under various interest rate scenarios. The ALCO attempts to manage the various components of the Bank's balance sheet to minimize the impact of sudden and sustained changes in interest rates through GAP, NPV and net interest income scenarios.

The Bank's exposure to interest rate risk is reviewed on a periodic basis by the Board of Directors and the ALCO. Interest rate sensitivity is a measure of the difference between amounts of interest-earning assets and interest-bearing liabilities which either reprice or mature within a given period of time.

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The difference, or the interest rate repricing "GAP", provides an indication of the extent to which an institution's interest rate spread will be affected by changes in interest rates over a period of time. A GAP is considered positive when the amount of interest-rate sensitive assets maturing or repricing over a specified period of time exceeds the amount of interest-rate sensitive liabilities maturing or repricing within that period and is considered negative when the amount of interest-rate sensitive liabilities maturing or repricing over a specified period of time exceeds the amount of interest-rate sensitive assets maturing or repricing within that period. Generally, during a period of rising interest rates, a negative GAP within a given period of time would adversely affect net interest income, while a positive GAP within such period of time may result in an increase in net interest income; during a period of falling interest rates, a negative GAP within a given period of time may result in an increase in net interest income while a positive GAP within such period of time may have the opposite effect.

GAP Table

The following table sets forth the amounts of interest-earning assets and interest-bearing liabilities and borrowings outstanding at December 31, 1998, which are expected to reprice or mature in each of the future time periods shown. The amount of assets or liabilities shown which reprice or mature during a particular period were determined by the contractual terms or assumed decay rates of the asset or liability. The table assumes prepayments and scheduled principal amortization of fixed-rate loans and mortgage-backed securities, and assumes that adjustable-rate mortgage loans will reprice at contractual repricing intervals. There has been no adjustment for the impact of future loan commitments and loans in process.

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FARMERS & MECHANICS BANK GAP TABLE	3 Months or Less	3 Months to 1 year	1 to 3 Years	3 to 5 Years	Over 5 Years	Total
			(Dollars in Thousands)			
<S>	<C>	<C>	<C>	<C>	<C>	<C>
Interest-earning assets:						
Investment securities	$ 19,641	$ 104,399	$ 24,110	$ 11,736	$ 95,980	$ 255,866
Loans	8,007	56,178	93,860	70,386	74,956	303,387
Mortage-backed securities	15,564	26,236	18,015	11,842	18,936	90,593
Total	43,212	186,813	135,985	93,964	189,872	649,846
Interest-bearing liabilities:						
Now, Super Now, Passbook and Club accounts	12,563	27,388	50,179	27,070	53,675	170,875
Money market accounts	11,719	31,393	17,397	3,522	3,659	67,690
Certificates of Deposit	51,580	107,367	51,868	17,594	0	228,409
Borrowings	0	0	75,000	20,000	4,568	99,568
Total	75,862	166,148	194,444	68,186	61,902	566,542
Interest Rate Sensitivity GAP	(32,650)	20,665	$ (58,459)	$ 25,778	$ 127,970	$ 83,304
Cumulative Interest Rate Sensitivity GAP	(32,650)	(11,985)	$ (70,444)	$ (44,666)	$ 83,304	
Ratio of Interest Rate Sensitive Assets to Interest Rate Sensitive Liabilities	56.96%	112.44%	69.94%	137.81%	306.73%	114.70%

Ratio of Cumulative GAP

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to Total Bank Assets	-4.72%	-1.73%	-10.19%	-6.46%	12.05%
	==========	===========	=========	============	===========

</TABLE>

The Bank's analysis of its interest-rate sensitivity incorporates certain assumptions concerning the amortization of loans and other interest-earning assets and the repricing characteristics of deposits. The Bank has made the following assumptions in calculating the values in the GAP table: adjustable-rate mortgage loans have a constant prepayment rate of 21%; fixed-rate mortgage loans have a prepayment rate that is constant through time at 18%; fixed and adjustable rate commercial loans have a constant prepayment rate of 10%; consumer loans have a prepayment rate that is constant over time at 16%; mortgage-backed securities and CMOs and REMICs have a prepayment rate that is constant over time at 21%. Core savings and NOW checking deposits have a decay rate of 17% and money market accounts have a decay rate of 80%. These decay rates are based on FHLB assumption rates using industry experience adjusted by the Bank as needed to reflect our individual experience. The interest-rate sensitivity of the Bank's assets and liabilities illustrated in the table could vary substantially if different assumptions were used or if actual experience differs from the assumptions used.

The table indicates the time period in which interest-earning assets and interest-bearing liabilities will mature or reprice in accordance with their contractual terms or assumed decay rates, as applicable. However, this table does not necessarily indicate the impact of general interest rate movements on the Bank's net interest income because the repricing of various categories of assets and liabilities is discretionary and is subject to competition and other pressures. As a result, various assets and liabilities indicated as repricing within the same period may in fact reprice at different times and at different rate levels.

Interest rate risk exposure is also measured using interest rate sensitivity analysis to determine the Bank's change in NPV in the event of hypothetical changes in interest rates and interest liabilities. If potential changes to NPV and net interest income resulting from hypothetical interest rate changes are not within the limits established. The Board of Directors may direct management to adjust its asset and liability mix to bring interest rate risk within Board approved limits.

The Bank has developed strategies to manage its liquidity, shorten the effective maturities of certain interest-earning assets and increase the effective maturities of certain liabilities, to reduce the exposure to interest rate fluctuations. These strategies include focusing its investment activities on short and medium-term securities, maintaining and increasing the transaction deposit accounts, as these accounts are considered to be relatively resistant to changes in interest rates and utilizing FHLB borrowings and deposit marketing programs to adjust the term or repricing of its liabilities.

The Bank also measures its interest rate risk using the OTS's NPV method. NPV is calculated based on the net present value of estimated cash flows utilizing market prepayment assumptions and market rates of interest provided by independent broker quotations and other public sources. An institution's Interest rate risk is measured as the change to its NPV as a result of a hypothetical immediate 200 basis point change in market interest rates. Based on this analysis at December 31, 1998, the Bank would experience a 75 basis point decrease in its NPV as a percent of assets if rates rise by 200 basis points in comparison to a flat rate scenario and a 121 basis point decrease in NPV if rates decline 200 basis points.

Although the NPV calculation provides an indication of the Bank's interest rate risk at a particular point in time, such measurements are not intended to and do not provide a precise forecast of the effect of changes in market interest rates on the Bank's net interest income and will differ from actual results.

Results of Operations
Net Interest Income

The earnings of the Corporation depend primarily upon the level of net interest income, which is the difference between interest earned on its interest-earning assets, such as loans and investments, and the interest paid on interest-bearing liabilities, such as deposits including non-interest checking accounts and borrowings. Net interest income is a function of the interest rate spread, which is the difference between the weighted average yield earned on

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interest-earning assets and the weighted average rate paid on interest-bearing liabilities, as well as the average balance of interest-earning assets as compared to interest-bearing liabilities. Net income is also affected by non-interest income, such as gains (losses) on the sale of loans and investments, provision for loan losses and real estate owned, service charges and other fees, and operating expenses.

The following table sets forth certain information relating to the Corporation's average balance sheet and reflects the average yield on assets and average rates paid on liabilities for the periods indicated. Such yields and rates are derived by dividing income or expense by the average balance of interest-earning assets or interest-bearing liabilities, respectively, for the periods presented.

Average Balances, Interest and Yields/Rates

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	Years Ended December 31,								
	1998			1997			1996		
	Average Balance	Interest	Average Yield/Rate	Average Balance	Interest	Average Yield/Rate	Average Balance	Interest	Average Yield/Rate
	(Dollars in Thousands)								
Interest-earning assets:									
<S>	<C>	<C>	<C>	<C>	<C>	<C>	<C>	<C>	<C>
Loans receivable	$ 303,330	$ 24,316	8.02%	$ 310,540	$ 25,038	8.06%	$ 296,276	$ 23,797	8.03%
Mortgage-backed securities	88,339	6,376	7.22%	97,013	7,062	7.28%	107,268	7,499	6.99%
Investment securities	231,610	15,871	6.85%	127,937	8,713	6.81%	84,762	5,545	6.54%
Total interest-earning assets	623,279	46,563	7.47%	535,490	40,813	7.62%	488,306	36,841	7.54%
Interest-bearing liabilities:									
Deposits	518,023	18,091	3.49%	474,258	17,755	3.74%	429,413	16,176	3.77%
Borrowings	98,459	5,721	5.81%	34,776	2,067	5.94%	29,450	1,745	5.93%
Subordinated debentures	10,000	1,057	10.57%	10,000	1,057	10.57%	10,000	1,057	10.57%
Total interest-bearing liabilities	$ 626,482	24,869	3.97%	$ 519,034	20,879	4.02%	468,863	18,978	4.05%
Net interest income		$ 21,694			$ 19,934			$ 17,863	
Interest rate spread			3.50%			3.60%			3.50%
Net yield on average interest-earning assets			3.48%			3.72%			3.66%
Ratio of average interest-earning assets to average interest-bearing liabilities			99.49%			103.17%			104.15%

</TABLE>

Rate Volume Analysis

The following table sets forth certain information regarding changes in interest income and interest expense of the Corporation for the periods indicated. For each category of interest-earning assets and interest-bearing liabilities, information is provided on changes attributable to (i) changes in rates; (ii) changes in volume; iii) total change in rate and volume (the combined effect of changes in both volume and rate, not separately identified, has been allocated to rate). Because average balances on loans include non-performing loans which reduce the computed yield, a higher level of non-performing loans affects both the changes due to volume and rate.

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	Years Ended December 31,					
	1998 vs. 1997			1997 vs. 1996		
	Increase (Decrease) Due to change in			Increase (Decrease) Due to change in		
	Rate	Volume	Total	Rate	Volume	Total
	(In Thousands)					
Interest income:						
Loans	$ (141)	$ (581)	$ (722)	$ 95	$ 1,146	$ 1,241
Mortgage-backed securities	(55)	(631)	(686)	280	(717)	(437)
Investment securities	97	7,061	7,158	344	2,824	3,168
Total change - interest income	(99)	5,849	5,750	719	3,253	3,972
Interest expense:						
Deposits	(1,302)	1,638	336	(110)	1,689	1,579
Borrowings	(131)	3,785	3,654	6	316	322
Subordinated debentures	0	0	0	0	0	0
Total change - interest expense	(1,433)	5,423	3,990	(104)	2,005	1,901
Net change in net interest income	$ 1,334	$ 426	$ 1,760	$ 823	$ 1,248	$ 2,071

</TABLE>

Comparisons of Years Ended December 31, 1998 and 1997.
Net Income

The Corporation and its subsidiary recorded net income of $5.3 million for the year ended December 31, 1998, or $.72 diluted earnings per share as compared to net income of $5.5 million, or $.75 diluted earnings per share for the year ended December 31, 1997. Net interest income was $21.7 million in 1998 compared to $19.9 million in 1997. Provisions for loan losses were $240 thousand in 1998 compared to $400 thousand in 1997. Other income totaled $2.4 million in 1998 compared to $2.1 million for the same period in 1997. Total operating expenses for the year ended December 31, 1998 were $15.6 million compared to $13.0 million in the previous year. During 1998, the Corporation declared dividends which totaled $.11 per share which resulted in a dividend payout ratio of 15.28%. The ability of the Corporation to pay dividends to shareholders is directly dependent upon the ability of the Bank to pay dividends to the Corporation. See Stockholders' Equity footnote.

Interest Income

Total interest income increased $5.8 million to $46.6 million in 1998 from $40.8 million in 1997. The increase is attributable to increases in interest income on investment securities of $7.2 million, partially offset by a decrease in interest income on loans of $722 thousand and mortgage-backed securities of $686 thousand.

The increase in interest income on investment securities was due to a $103.7 million increase in the average balance of investment securities to $231.6 million in 1998 from $127.9 million in 1997. The investment portfolio increased primarily due to the net purchase in 1998 of $131.3 million in collateralized mortgage obligations (CMOs), partially offset by $65.1 million in principal paydowns and $9.6 million net reductions in U.S. Agency notes. The increases in the average balance of investment securities resulted in an increase in interest income of $7.1 million in 1998 from the previous year. Average yields increased to 6.85% in 1998 from 6.81% in 1997, which resulted in an increase in interest income of $97 thousand.

The average balance of the loan portfolio decreased $7.2 million to $303.3 million in 1998 from $310.5 million in 1997. The decline in loan volume during 1998 resulted in a decrease in interest income of $581 thousand. The average yield on the loan portfolio decreased to 8.02% in 1998 from 8.06% in 1997 which resulted in a decrease in interest income of $141 thousand.

Interest income on mortgage-backed securities decreased $686 thousand in 1998 primarily due to volume decreases in the portfolio. The average balance of the portfolio decreased $8.7 million to $88.3 million in 1998 from $97.0 million in 1997, resulting in a decrease in interest income of $631 thousand. The decline in the average balance is due to principal paydowns of $32.8 million, partially offset by purchases of $31.1 million during the year. The average yield on the portfolio decreased to 7.22% in 1998 from 7.28% in 1997, which resulted in a decrease in interest income of $55 thousand.

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Interest Expense

Total interest expense increased $4.0 million to $24.9 million in 1998 from $20.9 million in 1997. The increase was due to an increase in interest expense on borrowings and deposits.

Interest expense on borrowings increased $3.7 million to $5.7 million in 1998 from $2.1 million in 1997. This increase was due to an increase in the average balance of borrowings, partially offset by a decline in the average rate. The average balance of borrowings increased $63.7 million to $98.5 million in 1998 from $34.8 million in 1997, resulting in a $3.8 million increase in interest expense due to volume. This was primarily the result of a $70.7 million increase in the average balance of repurchase agreements during the year. The average rate on borrowings decreased to 5.81% in 1998 from 5.94% in 1997, resulting in a $131 thousand decrease in interest expense due to rate.

Interest expense on deposits increased $336 thousand to $18.1 million in 1998 from $17.8 million in 1997. The average balance of deposits increased $43.8 million to $518.0 million in 1998 from $474.3 million in 1997, resulting in an increase in interest expense of $1.6 million. Increases in deposits in 1998 are primarily due to an increase in the average balances of checking accounts of $38.2 million and savings accounts of $11.5 million, partially offset by a decline in the average balance of certificates of deposit of $8.9 million. These increases were partially offset by a decline in the average rate paid on deposits of 25 basis points to 3.49% in 1998 from 3.74% in 1997, resulting in a decrease in interest expense of $1.3 million. The lowering of the average rate on deposits in 1998 was due to an increase in the average balance of non-interest "Free Personal Checking" and "Free Business Checking" accounts of $19.7 million.

Provision For Loan Losses

The provision for loan losses decreased $160 thousand to $240 thousand in 1998 from $400 thousand in 1997. The determination of the allowance level for loan losses is based on management's analysis of risk characteristics of various classifications of loans, previous loan loss experience, estimated fair value of the underlying collateral and current economic conditions. The Corporation will continue to monitor its allowance for loan losses and make future adjustments to the allowance through the provision for loan losses as economic conditions dictate. Although the Corporation maintains its allowance for loan losses at a level that it considers to be adequate to provide for the inherent risk of loss in its loan portfolio, there can be no assurance that future losses will not exceed estimated amounts or that additional provisions for loan losses will not be required in future periods due to the higher degree of credit risk which might result form the change in the mix of the loan portfolio.

Other Income (Expense)

Other income from operations increased $280 thousand to $2.4 million in 1998 compared with $2.1 million in 1997.

Loss on disposal of fixed assets of $210 thousand relates to the write-off of obsolete computer hardware and software due to the computer system conversion completed during 1998.

Real estate owned operations, net in 1998 resulted in a loss of $64 thousand, which was comprised of $57 thousand in real estate owned operating expenses, $108 thousand of provisions for loss on real estate, net of charge-offs, and realized gains of $101 thousand on the sale of real estate owned properties.

Service charges on accounts increased $165 thousand to $2.4 million in 1998 from $2.2 million in 1997. The increase is the result of additional retail banking fees due to higher transaction volume during the year.

Operating Expenses

Total operating expenses increased $2.6 million to $15.6 million in 1998 from $13.0 million in 1997.

Salaries and benefits increased $1.7 million to $9.0 million in 1998 from $7.3 million in 1997. The increase was due to additional staff in the new branches opened during the year as well as an increase in branch staff for extended weekday hours until 9:00 p.m. Average full time equivalent employees during 1998 were 335 as compared to 299 during 1997.

Occupancy and equipment expense increased $281 thousand to $3.0 million

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in 1998 from $2.7 million in 1997. This increase is due to additional depreciation and occupancy expenses on two new branches opened in 1998, as well as other facility and equipment additions and improvements during the year.

Purchased services expense increased $232 thousand to $1.3 million in 1998 from $1.1 million in 1997. Check processing costs increased $101 thousand and MAC charges increased $94 thousand due to higher transaction volume in 1998.

Advertising expense increased by $77 thousand to $206 thousand in 1998 from $129 thousand in 1997. The Bank has engaged in a newspaper advertising campaign emphasizing our twenty-three branch locations and increased hours of operations.

Comparisons of Years Ended December 31, 1997 and 1996.
Net Income

The Corporation and its subsidiary recorded net income of $5.5 million for the year ended December 31, 1997, or $.75 diluted earnings per share as compared to net income of $3.0 million, or $.40 diluted earnings per share for the year ended December 31, 1996. Net interest income was $19.9 million in 1997 compared to $17.9 million in 1996. Provisions for loan losses were $400 thousand in 1997 compared to $120 thousand in 1996. Other income totaled $2.1 million in 1997 compared to $2.3 million for the same period in 1996. Total operating expenses for the year ended December 31, 1997 were $13.0 million compared to $15.7 million in the previous year which included $2.7 million for the one-time special assessment to recapitalize the Savings Association Insurance Fund. During 1997, the Corporation declared dividends which totaled $.08 per share which resulted in a dividend payout ratio of 10.67%. The ability of the Corporation to pay dividends to shareholders is directly dependent upon the ability of the Bank to pay dividends to the Corporation. See Stockholders' Equity footnote.

Interest Income

Total interest income increased $4.0 million to $40.8 million in 1997 from $36.8 million in 1996. The increase is

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attributable to increases in interest income on investment securities of $3.2 million and loans of $1.2 million, partially offset by a decrease in interest income on mortgage-backed securities of $437 thousand.

The increase in interest income on investment securities was due to a $43.1 million increase in the average balance of investment securities to $127.9 million in 1997 from $84.8 million in 1996. The investment portfolio increased primarily due to the net purchase in 1997 of $59.0 million in collateralized mortgage obligations (CMOs), partially offset by $10.3 million in principal paydowns, $35.4 million in U.S. Agency notes and $10.2 million in reverse repurchase agreements. The increases in the average balance of investment securities resulted in an increase in interest income of $2.8 million in 1997 from the previous year. Average yields increased to 6.81% in 1997 from 6.54% in 1996, which resulted in an increase in interest income of $344 thousand.

The average balance of the loan portfolio increased $14.2 million to $310.5 million in 1997 from $296.3 million in 1996. In August 1996 the Bank purchased $14.5 million of adjustable rate mortgages from First Tennessee Bank. These loans are residential mortgages on properties primarily located within the Bank's lending area of Burlington County, NJ. The 1997 increase in loan volume resulted in a $1.1 million increase in interest income. The average yield on the loan portfolio increased to 8.06% in 1997 from 8.03% in 1996 which resulted in an increase in interest income of $95 thousand.

Interest income on mortgage-backed securities decreased $437 thousand in 1997 due to volume decreases in the portfolio, partially offset by increases in the yield on the portfolio. The average balance of the portfolio decreased $10.3 million to $97.0 million in 1997 from $107.3 million in 1996, resulting in a decrease in interest income of $717 thousand. The decline in the average balance is primarily due to principal paydowns of $21.6 million, partially offset by purchases of $9.4 million during the year. The average yield on the portfolio increased to 7.28% in 1997 from 6.99% in 1996, which resulted in an increase in interest income of $280 thousand.

Interest Expense

Total interest expense increased $1.9 million to $20.9 million in 1997 from $19.0 million in 1996. The increase was due to an increase in interest expense on deposits and borrowings.

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Interest expense on deposits increased $1.6 million to $17.8 million in 1997 from $16.2 million in 1996. The average balance of deposits increased $44.8 million to $474.2 million in 1997 from $429.4 million in 1996, resulting in an increase in interest expense of $1.7 million. Increases in deposits in 1997 are primarily due to increases in the average balances of checking accounts of $17.2 million, certificates of deposit accounts of $14.4 million and savings accounts of $11.0 million. These increases were partially offset by a decline in the average rate paid on deposits of 3 basis points to 3.74% in 1997 from 3.77% in 1996, resulting in a decrease in interest expense of $110 thousand. The lowering of the average rate on deposits in 1997 was due to an increase in the average balance of non-interest "Free Checking" accounts of $12.7 million.

Interest expense on borrowings increased $322 thousand to $2.1 million in 1997 from $1.7 million in 1996. This increase was due to an increase in the average balance of borrowings as well as an increase in the average rate. The average balance of borrowings increased $5.3 million to $34.8 million in 1997 from $29.5 million in 1996, resulting in a $316 thousand increase in interest expense due to volume. This was primarily the result of a $8.9 million increase in the average balance of repurchase agreements during the year. The average rate on borrowings increased to 5.94% in 1997 from 5.93% in 1996, resulting in a $6 thousand increase in interest expense due to rate.

Provision For Loan Losses

The provision for loan losses increased $280 thousand to $400 thousand in 1997 from $120 thousand in 1996. The determination of the allowance level for loan losses is based on management's analysis of risk characteristics of various classifications of loans, previous loan loss experience, estimated fair value of the underlying collateral and current economic conditions.

Other Income (Expense)

Other income from operations decreased $152 thousand to $2.1 million in 1997 compared with $2.3 million in 1996.

Loss from real estate held for development of $200 thousand was the result of an increase in the valuation allowance for the loss on the sale of one of the land development properties in 1997.

Real estate owned operations, net in 1997 resulted in a loss of $180 thousand, which was comprised of $48 thousand in real estate owned operating expenses, $123 thousand of provisions for loss on real estate, net of charge-offs, and realized gains of $11 thousand on the sale of real estate owned properties.

Service charges on accounts increased $258 thousand to $2.2 million in 1997 from $1.9 million in 1996. The increase is the result of additional retail banking fees due to higher transaction volume during the year.

Operating Expenses

Total operating expenses decreased $2.7 million to $13.0 million in 1997 from $15.7 million in 1996. The decrease in operating expenses was primarily due to the absence in 1997 of the one-time special assessment of $2.7 million in 1996 charged in connection with the federal legislation requiring the recapitalization of the Savings Association Insurance Fund (SAIF).

Salaries and benefits increased $276 thousand to $7.3 million in 1997 from $7.0 million in 1996. The increase was due to additional staff in the new branches opened during the year as well as an increase in branch staff for additional operating hours, principally for "Sunday Banking" and extended weekday hours until 9:00 p.m. Average full time equivalent employees during 1997 were 299 as compared to 236 during 1996.

Occupancy and equipment expense increased $174 thousand to $2.7 million in 1997 from $2.5 million in 1996. This increase is due to additional depreciation and occupancy expenses on two new branches opened in 1997, as well as other facility and equipment additions and improvements during the year.

Federal deposit insurance premiums decreased $714 thousand to $233 thousand in 1997 from $947 thousand in 1996. The decrease reflects the reduction in rates charged by the FDIC to $.065 per $100 of deposits during 1997 from $.23 per $100 in 1996, partially offset by an increase in average deposits of the Bank.

Purchased services expense increased $155 thousand to $1.1 million in 1997 from $917 thousand in 1996. This increase is primarily the result of an

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increase in check processing costs of $59 thousand and MAC charges of $53 thousand.

Advertising expense increased by $86 thousand to $129 thousand in 1997 from $43 thousand in 1996. The Bank has engaged in a newspaper advertising campaign emphasizing our branch locations and increased hours of operations.

Impact of Inflation and Changing Prices

Unlike most industrial companies, substantially all the assets of the Corporation are monetary in nature. As a result, interest rates have a greater impact on the Corporation's performance than do the effects of general levels of inflation. Interest rates do not necessarily move in the same direction or to the same extent as the price of goods and services.

Year 2000

The Year 2000 issue concerns the potential impact of historic computer software code that only utilizes two digits to represent the calendar year (e.g. "99" for "1999"). Software so developed could produce inaccurate or unpredictable results upon the change to January 1, 2000, when current and future dates represent a lower two digit year number than dates in the prior century. The Bank, similar to most financial institutions, is significantly subject to the potential impact of the "Year 2000 issue" due to the nature of financial information. Potential impact to the Bank may arise from software, hardware, and equipment both within the Bank's direct control and outside of the Bank's ownership, yet with which the Bank electronically or operationally interfaces (e.g. vendors providing credit bureau information). The Bank has a year 2000 compliance program in place to ensure that all software applications will be year 2000 certified compliant. The program includes Year 2000 committees consisting of directors and executive officers of the Bank. The purpose of the committees are to oversee and manage the year 2000 compliance program providing regular reports to the Board of Directors detailing progress with the Year 2000 issue. Management expects that it will be able to satisfy year 2000 compliance issues by the end of 1999. Management intends to perform testing on all systems throughout 1999.

The Bank replaced its core bank processing systems in December 1998 as the existing systems had reached their limit in capacity and function. The new systems provide Year 2000 compliance.

The Bank has established a written Year 2000 Contingency Plan for all vital mission critical applications. It states both the plans in the event of non-compliance and the dates in which the contingency plans will be put into effect. The scope of the plan includes five phases. They are as follows: Awareness, Assessment, Renovation, Validation, and Implementation. As defined by the Federal Financial Institutions Examination Council and the banking regulatory agencies which regulate the Bank.

The Assessment of the impact of the Year 2000 issues on the Bank's computer systems has been completed. Based on the assessment the Bank has identified and prioritized those Systems deemed to be mission critical or those that have significant impact on normal operations.

The Bank has contacted all significant vendors and suppliers regarding their Year 2000 readiness. These third party vendors have delivered written assurance that they are or expect to be Year 2000 prior to the end of 1999. Their progress in meeting their targeted scheduled readiness is being monitored for any indication that they may not be able to address their Year 2000 problems in a timely fashion. Management testing on all banking systems is progressing according to plan. Mission critical testing began in the second quarter of 1998 and will continue through the first quarter of 1999. At the current time management estimates its Year 2000 readiness is 80%. The following table provides a summary of the current status of the five phases involved in our Year 2000 readiness Plan.

Project Phase	Percent Complete	Projected Date of Completion	Comments
Awareness	100%	Complete	
Assessment	85%	March 1999	On Schedule
Renovation	85%	March 1999	On Schedule
Validation	85%	June 1999	On Schedule
Implementation	80%	June 1999	On Schedule
Overall Completion	80%	June 1999	On Schedule

The Bank has thus far primarily used and expects to continue to use internal resources to implement its readiness plan. At this time management currently estimates Year 2000 compliance costs at between $50,000 and $150,000 of which $48,000 was expensed in 1998. The Bank does not expect that these cost will be material to its financial condition or results of operation.

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Non-compliance with the Year 2000 issue could have an adverse affect on the operation of the business. Successful and timely completion of the Year 2000 compliance are based upon management's best estimates, which were derived

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using numerous assumptions of future events which are inherently uncertain including the continued availability of certain resources, the progress and results of the Bank's testing plans, and all vendors, suppliers and customer readiness.

Based upon current information management has determined that the year 2000 issues will not pose significant operational problems for its Systems. This is based on the ability of the Bank to renovate, in a timely manner, the products and services on which the Bank's Systems rely. Bank management believes, based on information and testing results from our mission critical vendors, that these systems are and it is anticipated will remain Year 2000 compliant. The will continue to monitor compliance of the mission critical systems.

The Bank is in the process of updating contingency plans for each critical system, in the event one of those systems fail, despite our best efforts. The Bank's contingency plans to provide resources during the weekend of December 31, 1999 and for a period of time afterward. It is anticipated that the Bank, and or its vendors will be able to overcome any unforeseen problems associated with the millennium change.

Liquidity and Capital Resources

The Bank's liquidity is a measure of its ability to fund loans, withdrawals of deposits and other cash outflows in a cost effective manner. The Bank's primary sources of funds are deposits and scheduled amortization and prepayments of loan principal. The Bank also obtains funds from the sale and maturity of investment securities and short-term investments as well as the maturity of mortgage-backed securities and funds provided by operations. During the past several years, the Bank has used such funds primarily to meet its ongoing commitments to fund maturing time deposits and savings withdrawals, to fund existing and continuing loan commitments and to maintain liquidity. While the Bank has been able to fund its operations internally during recent periods, it has periodically supplemented its liquidity needs with securities sold under agreements to repurchase (repurchase agreements) and advances from the Federal Home Loan Bank of New York (FHLB). At December 31, 1998 the Bank had $80.0 million in repurchase agreements and $16.4 million in advances from the FHLB of New York. While loan payments, maturing investments and mortgage-backed securities are relatively predictable sources of funds, deposit flows and loan prepayments are greatly influenced by general interest rates, economic conditions and competition. The Bank's liquidity is also influenced by the level of demand for funding loan originations. Liquidity may be adversely affected by unexpected deposit outflows, excessive interest rates paid by competitors, adverse publicity relating to the Banking industry and similar matters. Management monitors projected liquidity needs and determines the level desirable, based in part on the Company's commitment to make loans and management's assessment of the Company's ability to generate funds. The Company is also subject to federal regulations that impose certain minimum capital requirements.

The Bank is required under applicable federal regulations to maintain a specified level of "liquid investments", which include certain United States government and federal agency securities and other approved investments. Regulations currently in effect require the Bank to maintain liquid assets of not less than 4% of its withdrawable accounts plus short-term borrowings. These levels are changed from time to time by the regulators to reflect the current economic conditions. The Bank has generally maintained liquidity in excess of the required level. The Office of Thrift Supervision ("OTS") on November 24, 1997 changed the definition and calculation of liquidity. The December 31, 1998 regulatory liquidity number of 31.35% reflects these changes.

The amount of certificate accounts which are scheduled to mature during the twelve months ending December 31, 1999 is approximately $158 million. To the extent these deposits do not remain at the Bank upon maturity, the Bank believes it can replace these funds with deposits, FHLB advances or outside borrowings. It has been the Bank's experience that a substantial portion of such maturing deposits remain with the Bank.

At December 31, 1998, the Bank had loan commitments outstanding of $29.8 million, of which $6.6 million were for fixed-rate loans and $23.2 million were for adjustable-rate loans. Funds required to fulfill the commitments are derived primarily from loan repayments, net deposit inflows or, when appropriate, borrowings.

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Under the Financial Institutions Reform, Recovery and Enforcement Act of 1989 ("FIRREA") the Bank must have core capital equal to 4% of assets, of which 2% must be tangible capital, excluding goodwill. FIRREA also established risk-based capital standards. In measuring the Bank's compliance with FIRREA capital standards, the Bank must deduct from its regulatory capital calculation investments in, and advances to, subsidiaries engaged in activities not permissible for national banks. At December 31, 1998, the Bank exceeded all three required regulatory capital levels. At December 31, 1998, the Bank's regulatory tangible and core capital was $48.4 million or 7.02% of total bank assets and risk-based capital was $51.5 million or 18.13% of risk-weighted assets.

Consolidated Summary of Quarterly Earnings (Unaudited)

The following table presents summarized quarterly data for 1998 and 1997:

(In Thousands, except per share amounts)

1998	1st Quarter	2nd Quarter	3rd Quarter	4th Quarter	Total Year
Total interest income	$ 11,424	$ 11,805	$ 11,748	$ 11,586	$ 46,563
Total interest expense	6,136	6,365	6,290	6,078	24,869
Net interest income	5,288	5,440	5,458	5,508	21,694
Provision for loan losses	60	60	60	60	240
Net interest income after provision for loan losses	5,228	5,380	5,398	5,448	21,454
Total other income	605	536	590	650	2,381
Total operating expenses	3,892	3,820	3,814	4,054	15,580
Income before income taxes	1,941	2,096	2,174	2,044	8,255
Federal and state income taxes	700	761	785	738	2,984
Net income	$ 1,241	$ 1,335	$ 1,389	$ 1,306	$ 5,271
Basic earnings per common share	$ 0.17	$ 0.19	$ 0.19	$ 0.18	$ 0.73
Diluted earnings per common share	$ 0.17	$ 0.18	$ 0.19	$ 0.18	$ 0.72

(In Thousands, except per share amounts)

1997	1st Quarter	2nd Quarter	3rd Quarter	4th Quarter	Total Year
Total interest income	$ 9,744	$ 10,080	$ 10,267	$ 10,722	$ 40,813
Total interest expense	4,978	5,092	5,184	5,625	20,879
Net interest income	4,766	4,988	5,083	5,097	19,934
Provision for loan losses	30	50	60	260	400
Net interest income after provision for loan losses	4,736	4,938	5,023	4,837	19,534
Total other income	582	569	542	408	2,101
Total operating expenses	3,204	3,221	3,384	3,208	13,017
Income before income taxes	2,114	2,286	2,181	2,037	8,618
Federal and state income taxes	766	829	787	745	3,127
Net income	$ 1,348	$ 1,457	$ 1,394	$ 1,292	$ 5,491

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Basic earnings per common share	$ 0.19	$ 0.20	$ 0.19	$ 0.19	$ 0.77
Diluted earnings per common share	$ 0.18	$ 0.20	$ 0.19	$ 0.18	$ 0.75

</TABLE>

FMS FINANCIAL CORPORATION AND SUBSIDIARY
CONSOLIDATED STATEMENTS OF FINANCIAL CONDITION

<TABLE>
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December 31,	1998	1997
ASSETS		
Cash and amounts due from depository institutions	$ 18,142,316	$ 11,637,181
Interest-bearing deposits	0	826,823
Short term funds	11,754,075	167,618
Total cash and cash equivalents	29,896,391	12,631,622
Investment securities held to maturity	129,417,826	112,349,476
Investment securities available for sale	109,833,133	80,338,661
Loans, net	298,603,223	302,831,031
Mortgage-backed securities held to maturity	90,592,647	92,020,517
Accrued interest receivable:		
Loans	1,839,217	1,750,966
Mortgage-backed securities	633,667	715,981
Investments	2,371,410	1,934,925
Federal Home Loan Bank stock	4,861,410	3,630,800
Real estate held for development, net	644,487	644,487
Real estate owned, net	167,541	446,361
Office properties and equipment, net	19,292,247	15,692,055
Deferred income taxes	2,015,772	1,507,307
Excess cost over fair value of net assets acquired	164,969	469,444
Prepaid expenses and other assets	1,156,573	1,061,125
Subordinated debentures issue costs, net	321,113	378,460
TOTAL ASSETS	$ 691,811,626	$ 628,403,218
LIABILITIES AND STOCKHOLDERS' EQUITY		
Liabilities:		
Deposits	$ 536,309,623	$ 489,439,980
Securities sold under agreements to repurchase	80,000,000	60,000,000
Advances from the Federal Home Loan Bank	16,368,321	24,496,476
10% Subordinated debentures, due 2004	10,000,000	10,000,000
Guarantee of employee stock ownership plan debt	0	33,481
Advances by borrowers for taxes and insurance	2,259,435	2,192,541
Accrued interest payable	1,304,742	1,114,304
Dividends payable	216,953	167,154
Other liabilities	1,883,887	2,043,465
Total liabilities	648,342,961	589,487,401
Commitments and contingencies		
Stockholders' Equity:		
Preferred stock - $.10 par value 5,000,000 shares authorized; none issued		
Common stock - $.10 par value 10,000,000 shares authorized; shares issued 7,897,191* and 2,604,370, and shares outstanding 7,231,767* and 2,387,916 as of December 31, 1998 and 1997, respectively	789,719	260,437
Paid-in capital in excess of par*	8,216,820	8,419,167
Unrealized (loss)gain on securities available for sale - net of deferred income taxes	(21,793)	53,955
Guarantee of employee stock ownership plan debt	0	(33,481)
Retained earnings	37,860,291	33,406,060
Less: Treasury stock (665,424* and 216,454 shares, at cost, as of December 31, 1998 and 1997, respectively)	(3,376,372)	(3,190,321)
Total stockholders' equity	43,468,665	38,915,817

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TOTAL LIABILITIES AND STOCKHOLDERS' EQUITY	$ 691,811,626	$ 628,403,218

</TABLE>

* Common stock, paid-in capital in excess of par and treasury stock at December 31, 1998 reflect a three-for-one stock split paid in July 1998.

See notes to consolidated financial statements.

FMS FINANCIAL CORPORATION AND SUBSIDIARY
CONSOLIDATED STATEMENTS OF OPERATIONS
<TABLE>
<CAPTION>

Years Ended December 31,	1998	1997	1996
<S>	<C>	<C>	<C>
INTEREST INCOME:			
Interest income on:			
Loans	$ 24,315,646	$ 25,037,855	$ 23,797,512
Mortgage-backed securities	6,375,729	7,062,459	7,499,231
Investments	15,871,239	8,712,928	5,544,668
Total interest income	46,562,614	40,813,242	36,841,411
INTEREST EXPENSE:			
Interest expense on:			
Deposits	18,090,683	17,754,531	16,176,223
Borrowings	5,720,876	2,066,929	1,745,032
Subordinated debentures	1,057,348	1,057,348	1,057,348
Total interest expense	24,868,907	20,878,808	18,978,603
NET INTEREST INCOME	21,693,707	19,934,434	17,862,808
PROVISION FOR LOAN LOSSES	240,000	400,000	120,000
NET INTEREST INCOME AFTER PROVISION FOR LOAN LOSSES	21,453,707	19,534,434	17,742,808
OTHER INCOME (EXPENSE):			
Loan service charges and other fees	147,080	170,766	219,639
Gain on sale of loans	5,423	9,804	8,432
Gain on sale of investment securities	0	1,711	54,406
Loss on disposal of fixed assets	(209,935)	0	0
Loss from real estate held for development	0	(200,000)	0
Real estate owned operations, net	(64,215)	(179,879)	(174,503)
Service charges on accounts	2,369,112	2,204,167	1,946,307
Other income	133,584	94,664	199,097
Total other income (expense)	2,381,049	2,101,233	2,253,378
OPERATING EXPENSES:			
Salaries and employee benefits	8,971,707	7,319,822	7,043,584
Occupancy and equipment	2,996,435	2,715,513	2,541,296
Purchased services	1,303,637	1,071,697	916,803
Federal deposit insurance premiums	294,912	232,739	946,594
SAIF recapitalization assessment	0	0	2,720,765
Professional fees	369,987	331,436	285,972
Advertising	206,120	129,278	42,956
Other	1,436,937	1,216,951	1,192,896
Total operating expenses	15,579,735	13,017,436	15,690,866
INCOME BEFORE INCOME TAXES	8,255,021	8,618,231	4,305,320
INCOME TAXES:			
Current	3,293,115	3,195,477	2,044,225
Deferred	(309,582)	(68,400)	(764,726)
Total income taxes	2,983,533	3,127,077	1,279,499
NET INCOME	$ 5,271,488	$ 5,491,154	$ 3,025,821
BASIC EARNINGS PER COMMON SHARE*	$0.73	$0.77	$0.41
DILUTED EARNINGS PER COMMON SHARE*	$0.72	$0.75	$0.40
Weighted average common shares outstanding*	7,203,862	7,165,455	7,411,083
Potential dilutive effect of the exercise of stock options*	109,779	180,864	161,862
Adjusted weighted average common shares outstanding*	7,313,641	7,346,319	7,572,945

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</TABLE>

* Basic and diluted earnings per common share, weighted average common shares outstanding and the potential dilutive effect of the exercise of stock options were restated to reflect a three-for-one stock split paid in July 1998.

See notes to consolidated financial statements.

FMS FINANCIAL CORPORATION AND SUBSIDIARY
CONSOLIDATED STATEMENTS OF CASH FLOWS
<TABLE>
<CAPTION>

Years Ended December 31,	1998	1997	1996
<S>	<C>	<C>	<C>
OPERATING ACTIVITIES:			
Net income	$ 5,271,488	$ 5,491,154	$ 3,025,821
Adjustments to reconcile net income to net cash provided by operating activities:			
Provision for loan losses	240,000	400,000	120,000
Depreciation and amortization	1,999,005	1,876,773	1,639,469
Provision for real estate owned	108,102	142,630	124,315
Provision for real estate held for development	0	200,000	0
Realized (gains) and losses on:			
Sale of loans and loans held for sale	(5,423)	(9,804)	(8,432)
Sale of investments available for sale	0	(1,711)	(54,406)
Disposal and sale of fixed assets	209,935	7,122	7,240
Sale of real estate owned	(101,349)	(10,630)	8,235
Proceeds from sale of loans held for sale	0	101,625	112,226
Loans originated for sale	0	(100,000)	(110,000)
Increase in accrued interest receivable	(442,422)	(770,837)	(24,702)
Increase in prepaid expenses and other assets	(95,448)	(171,226)	(120,213)
Increase (Decrease) in accrued interest payable	190,438	253,759	(27,911)
(Decrease) Increase in other liabilities	(61,539)	(46,544)	241,148
Provision for deferred income taxes	(465,972)	(67,530)	(705,382)
Other	33,481	72,982	75,981
Net cash provided by operating activities	6,880,296	7,367,763	4,303,389
INVESTING ACTIVITIES:			
Proceeds from sale of:			
Education loans	1,658,700	953,442	846,443
Real estate held for development	0	333,245	0
Real estate owned	603,095	75,630	396,519
Office property and equipment	0	0	1,700
Principal collected and proceeds from maturities of investment investment securities held to maturity	294,889,937	265,776,982	157,566,650
Proceeds from maturities of investment securities available for sale	86,593,751	11,942,666	16,327,791
Principal collected and proceeds from maturities of mortgage-backed securities	32,754,399	33,458,783	32,335,567
Principal collected on loans, net	60,258,471	53,020,808	52,372,663
Longer-term loans originated or acquired, net	(58,185,394)	(50,305,474)	(72,113,495)
Purchase of investment securities and mortgage-backed securities held to maturity	(343,502,524)	(320,005,763)	(199,107,774)
Purchase of investment securities available for sale	(116,472,554)	(78,570,231)	(26,797,361)
(Purchase) Redemption of Federal Home Loan Bank stock	(1,230,610)	(10,200)	437,500
Purchase of office property and equipment	(4,912,791)	(2,077,581)	(3,271,960)
Net cash received from deposit and branch purchase, net	0	0	9,044,846
Net cash used by investing activities	(47,545,520)	(85,407,693)	(31,960,911)
FINANCING ACTIVITIES:			
Net increase in demand deposits and savings accounts	61,509,157	27,376,384	3,813,048
Net (decrease) increase in time deposits	(14,639,514)	2,095,304	11,470,940
Net (decrease) increase in FHLB advances and advances from Bank	(8,128,155)	(8,053,524)	14,741,758
Proceeds from securities sold under agreement to repurchase	20,000,000	60,000,000	0
Principal repayment of employee stock ownership plan debt	(33,481)	(72,982)	(75,981)
Increase in advances from borrowers for taxes and insurance	66,894	53,903	45,508
Purchase of treasury stock	(186,051)	(127,361)	(1,913,191)
Dividends paid on common stock	(767,461)	(525,479)	(495,434)
Net proceeds from issuance of common stock	108,604	5,758	4,843
Net cash provided by financing activities	57,929,993	80,752,003	27,591,491
INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS	17,264,769	2,712,073	(66,031)
CASH AND CASH EQUIVALENTS, BEGINNING OF YEAR	12,631,622	9,919,549	9,985,580
CASH AND CASH EQUIVALENTS, END OF YEAR	$ 29,896,391	$ 12,631,622	$ 9,919,549

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Supplemental Disclosures:			
Cash paid for:			
Interest on deposits, advances, and other borrowings	$ 24,678,469	$ 20,625,049	$ 19,006,514
Income taxes	2,906,347	3,456,506	1,647,476
Non cash investing and financing activities:			
Dividends declared and not paid at year end	216,953	167,154	119,636
Non-monetary transfers from loans to real estate acquired through foreclosure	331,028	32,435	481,833

</TABLE>

See notes to consolidated financial statements.

15

FMS FINANCIAL CORPORATION

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FMS FINANCIAL CORPORATION AND SUBSIDIARY
CONSOLIDATED STATEMENTS OF CHANGES IN STOCKHOLDERS' EQUITY

	Common shares outstanding	Common stock	Paid-in capital	Accumulated comprehensive income	Guarantee of employee stock ownership plan debt	Retained earnings	Treasury stock	Total Stockholders' Equity
<S>	<C>	<C>	<C>	<C>	<C>	<C>	<C>	<C>
Balances at December 31, 1995	2,505,756	$260,163	$8,408,840	$ (236,154)	$ (182,444)	$25,951,864	$(1,149,769)	$33,052,500
Net Income						3,025,821		3,025,821
Other comprehensive income, net of tax								
Unrealized gain on securities available for sale				70,002				70,002

Total comprehensive income								3,095,823
Dividends declared						(489,782)		(489,782)
Decrease in guarantee of employee stock ownership plan debt					75,981			75,981
Exercise of stock options	1,250	125	4,718					4,843
Purchase of common stock	(114,299)						(1,913,191)	(1,913,191)
Balances at December 31, 1996	2,392,707	260,288	8,413,558	(166,152)	(106,463)	28,487,903	(3,062,960)	33,826,174
Net Income						5,491,154		5,491,154
Other comprehensive income, net of tax								
Unrealized gain on securities available for sale				220,107				220,107

Total comprehensive income								5,711,261
Dividends declared						(572,997)		(572,997)
Decrease in guarantee of employee stock ownership plan debt					72,982			72,982
Exercise of stock options	1,486	149	5,609					5,758
Purchase of common stock	(6,277)						(127,361)	(127,361)
Balances at December 31, 1997	2,387,916	260,437	8,419,167	53,955	(33,481)	$33,406,060	(3,190,321)	38,915,817
Net Income						5,271,488		5,271,488
Other comprehensive income, net of tax								
Unrealized gain (loss) on securities available for sale				(75,748)				(75,748)

Total comprehensive income								5,195,740
Dividends declared						(817,257)		(817,257)
Decrease in guarantee of employee stock ownership plan debt					33,481			33,481
Exercise of stock options	47,451	4,745	103,859					108,604
Tax benefit from gains on stock options exercised			218,331					218,331
Purchase of common stock	(5,354)						(186,051)	(186,051)
Three-for-one stock split	4,801,754	524,537	(524,537)					0
Balances at December 31, 1998	7,231,767	$789,719	$8,216,820	$ (21,793)	$ 0	$37,860,291	$(3,376,372)	43,468,665

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FMS FINANCIAL CORPORATION AND SUBSIDIARY
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
FOR THE YEARS ENDED DECEMBER 31, 1998, 1997, and 1996

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1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Principles of Consolidation

The consolidated financial statements are prepared in accordance with generally accepted accounting principles. The consolidated financial statements include the accounts of FMS Financial Corporation ("the Corporation"), Farmers & Mechanics Bank, and its wholly-owned subsidiaries ("the Bank"). Material intercompany accounts and transactions have been eliminated in consolidation.

Regulatory Authorities

The regulatory agency overseeing savings associations is the Office of Thrift Supervision ("OTS") and the deposits of the Bank are insured by the Federal Deposit Insurance Corporation ("FDIC").

At periodic intervals, both the OTS and the FDIC routinely examine the Corporation as part of their legally prescribed oversight of the savings and loan industry. Based on these examinations, the regulators can direct that the Corporation's financial statements be adjusted in accordance with their findings. In addition, the Corporation is subject to regulations of the Securities and Exchange Commission ("SEC").

SAIF Recapitalization Assessment

Legislation was signed by the President on September 30, 1996 requiring savings institutions with SAIF insured deposits to pay a one-time special assessment to facilitate the recapitalization of the SAIF. The assessment was based on 65.7 cents per $100 of deposits at March 31, 1995. This assessment resulted in a charge of approximately $2.7 million to operating expenses during the year ended December 31, 1996.

Cash and Cash Equivalents

Cash and cash equivalents include cash and amounts due from depository institutions, interest-bearing deposits with an original maturity of 90 days or less, money market funds and federal funds sold. Cash and cash equivalents exclude reverse repurchase agreements which are generally classified as investments held to maturity. Generally, federal funds are purchased and sold for one-day periods. The Bank is required to maintain certain average reserve balances as established by the Federal Reserve Bank. The amount of those balances for the reserve computation periods which include December 31, 1998 and 1997 were $11.0 million and $6.8 million, respectively. These requirements were satisfied through the balance of vault cash and a balance at the Federal Home Loan Bank.

Investments and Mortgage-Backed Securities

In accordance with Statement of Financial Accounting Standards No. 115 (SFAS No. 115), "Accounting for Certain Investments in Debt and Equity Securities" the Corporation classifies investments into three categories, as applicable; trading, available for sale or held to maturity. Upon the adoption of SFAS No. 115 on January 1, 1994, the Corporation categorized selected investments and mortgage-backed securities that are part of the Corporation's asset/liability management strategy and that may be sold in response to changes in interest rates, prepayments and similar factors, as available for sale. Investments classified as available for sale are reported at the current market value with net unrealized gains and losses, net of applicable deferred tax effects, added to or deducted from the Corporation's total stockholders' equity until realized. Gains and losses on the sale of investment securities are recognized utilizing the specific identification method.

Investment and mortgage-backed securities classified as held to maturity are recorded at cost, adjusted for amortization of premiums or accretion of discounts. Premiums are amortized over the average life of the security. Discounts are amortized using a method which in total approximates the interest method over the remaining contractual life of the security. The Corporation has the intent and ability to hold these securities to maturity.

Securities Purchased under Agreements to Resell

The Bank invests excess funds in securities purchased under agreements to resell (reverse repurchase agreements). Generally, the maturity date of the reverse repurchase agreement is less than 90 days. Due to the short-term nature of the agreement, the Bank does not take possession of the securities; instead,

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the securities are held in safekeeping by the Bank's agent. The carrying value of the agreements approximates fair market value because of the short maturity of the investment.

Allowance for Possible Loan Losses

An allowance for possible loan losses is maintained at a level that management considers adequate to provide for potential losses based upon the portfolio's past loss experience, current economic conditions and other relevant factors. When collection of a loan's principal balance or portion thereof is considered doubtful, management charges the allowance for possible loan losses based on their assessment of the loan's underlying collateral, if collateral dependent, or present value of

estimated future cash flows. While management uses the best information available to make evaluations about the adequacy of the allowance for loan losses, future adjustments to the allowance may be necessary if conditions differ substantially from the assumptions used in making evaluations.

Loans Held for Sale

The Bank periodically sells selected fixed-rate residential mortgage loans, without recourse, to provide additional funds for lending and to restructure the loan portfolio to improve interest rate risk. These loans are carried at the lower of cost or estimated market value, determined on a net aggregate basis.

Interest on Loans

The Bank recognizes interest income on loans when earned. Generally, the Bank does not recognize interest income on loans three months or more delinquent. Such interest ultimately collected is recorded as income in the period of recovery.

Real Estate Owned

Real estate owned consists of properties acquired by or in-lieu of foreclosure. These assets are carried at the lower of cost or estimated fair value at the time the loan is foreclosed less estimated cost to sell. The amounts recoverable from real estate owned could differ materially from the amounts used in arriving at the net carrying value of the assets because of future market factors beyond the control of the Bank. Costs to improve the property are capitalized, whereas costs of holding the property are charged to expense.

Real Estate Held for Development

Real estate held for development is carried at cost not to exceed net realizable value. Net realizable value is determined based on a discounted estimate of the fair market value.

Office Properties and Equipment

Office properties and equipment are recorded at cost. Depreciation is computed using the straight-line method over the expected useful lives of the assets. The costs of maintenance and repairs are expensed as they are incurred. Renewal and improvement costs are capitalized.

Deferred Loan Fees

The Bank defers all loan fees and related direct loan origination costs. Deferred loan fees and costs are generally capitalized and amortized as a yield adjustment over the life of the loan using the interest method.

Loans Serviced for Others

Servicing loans for others generally consists of collecting mortgage payments, disbursing payments to investors and processing foreclosures. Loan servicing income is recorded upon receipt and includes servicing fees from investors and certain charges collected from borrowers, such as late payment fees. The total amount of loans being serviced for the benefit of others was $20.4 million and $25.6 million at December 31, 1998

and 1997, respectively. Loan servicing fee income was approximately $70 thousand, $83 thousand and $98 thousand for the years ended December 31, 1998, 1997 and 1996, respectively.

Excess Cost over Fair Value of Net Assets Acquired

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The excess costs over the fair value of assets acquired are being amortized over a five year period using the straight-line method.

Income Taxes

The Corporation computes its taxable income for both financial reporting and federal tax purposes on the accrual basis. The Corporation reports certain items of income and expense in its consolidated financial statements in periods different from those in which such items enter into the determination of taxable income. In conformity with generally accepted accounting principles, the Corporation provides for the tax effects of such timing differences in its consolidated financial statements, subject to the deferred tax asset realizability provisions of Statement of Financial Accounting Standards No. 109 (SFAS No. 109), "Accounting for Income Taxes". These differences between pretax accounting income and taxable income for return purposes consist primarily of the calculations for loan loss allowance, real estate losses, depreciation, recognition of income and expenses associated with loan origination, profit recognition on discounted mortgages and securities income.

Reclassifications

Certain items in the 1997 and 1996 consolidated financial statements have been reclassified to conform with the presentation in the 1998 consolidated financial statements.

Earnings Per Share

Statement of Financial Accounting Standards No. 128 (SFAS No. 128), "Earnings per Share", requires the dual presentation of basic and diluted EPS on the face of the income statement for all entities with complex capital structures and requires a reconciliation of the numerator and denominator of the basic EPS computation to the numerator and denominator of the diluted EPS computation. Basic EPS excludes dilution and is computed by dividing income available to common stockholders by the weighted-average number of common shares outstanding for the period. Diluted EPS reflects the potential dilution that could occur if securities or other contracts to

issue common stock were exercised or converted into common stock or resulted in the issuance of common stock that then shared in the earnings of the entity. Diluted EPS is computed similarly to fully diluted EPS pursuant to Opinion 15. The Corporation has presented both basic and diluted earnings per share as well as the reconciliation of the denominator in the consolidated statement of operations.

Basic and diluted earnings per share and weighted average common shares outstanding and common stock equivalents have been retroactively restated to reflect the increased number of common shares resulting from the three-for-one stock split that was paid to shareholders on July 14, 1998. A total of 5,245,370 additional shares were issued in conjunction with the stock split. The par value of the Corporation's stock remained unchanged. As a result, $524,537 was transferred from paid-in capital in excess of par to common stock.

2. INVESTMENT SECURITIES HELD TO MATURITY

A comparison of amortized cost and estimated market value of investment securities held to maturity at December 31, 1998 and 1997 are as follows:

	December 31, 1998			
	Amortized Cost	Gross Unrealized Gains	Gross Unrealized (Losses)	Estimated Market Value
U.S. Gov't Agencies	$ 78,291,686	$ 151,165	$ (201,073)	$ 78,241,778
Municipal bonds	3,823,802	2,833	0	3,826,635
CMOs	47,302,338	53,888	(59,017)	47,297,209
Total	$ 129,417,826	$ 207,886	$ (260,090)	$ 129,365,622

	December 31, 1997			
	Amortized Cost	Gross Unrealized Gains	Gross Unrealized (Losses)	Estimated Market Value
U.S. Gov't Agencies	$ 79,347,265	$ 220,876	$ (70,550)	$ 79,497,591
Reverse Repos	30,185,402	0	0	30,185,402
Municipal bonds	2,801,809	14,609	0	2,816,418
U.S. Treasury	15,000	0	(500)	14,500

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Total	$ 112,349,476	$ 235,485	$ (71,050)	$ 112,513,911

The Bank has the intent and ability to hold these securities to maturity. During December 1997 the Bank purchased $30.2 million of reverse repurchase agreements with Paine Webber and Merrill Lynch, with an average maturity of 29 days and a weighted average yield of 6.17%.

The amortized cost and estimated market value of investments held to maturity at December 31, 1998, by contractual maturity are shown in the following table. Expected maturities may differ as borrowers have the right to call certain obligations. CMOs are shown separately due to the amortization and prepayment of principal occurring throughout the life of these instruments.

	December 31,1998	
	Amortized Cost	Estimated Market Value
Due one year or less	$ 3,594,071	$ 3,596,635
Due one to five years	5,000,000	4,960,000
Due five to ten years	53,387,121	53,371,278
Due after ten years	20,134,296	20,140,500
CMO's	47,302,338	47,297,209
Total	129,417,826	129,365,622

3. INVESTMENT SECURITIES AVAILABLE FOR SALE

The amortized cost and estimated market value of investment securities available for sale at December 31, 1998 and 1997 are as follows:

	December 31, 1998			
	Amortized Cost	Gross Unrealized Gains	Gross Unrealized (Losses)	Estimated Market Value
U.S. Gov't Agencies	$ 18,492,035	$ 26,683	$ (18,102)	$ 18,500,616
CMOs	91,377,435	206,435	(251,353)	91,332,517
Total	$ 109,869,470	$ 233,118	$ (269,455)	$ 109,833,133

	December 31, 1997			
	Amortized Cost	Gross Unrealized Gains	Gross Unrealized (Losses)	Estimated Market Value
U.S. Gov't Agencies	$ 7,850,135	$ 21,646	$ (1,200)	$ 7,870,581
CMOs	72,406,623	284,720	(223,263)	72,468,080
Total	$ 80,256,758	$ 306,366	$ (224,463)	$ 80,338,661

The amortized cost and estimated market value of investments available for sale at December 31, 1998, by contractual maturity are shown in the following table. Expected maturities may differ as borrowers have the right to call or prepay certain obligations. CMOs are shown separately due to the amortization and prepayment of principal occurring throughout the life of these

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instruments.

	December 31, 1998	
	Amortized Cost	Estimated Market Value
Due five to ten years	$ 17,492,036	$ 17,502,717
Due after ten years	1,000,000	997,900
CMOs	91,377,434	91,332,516
Total	$ 109,869,470	$ 109,833,133

There were no sales during 1998. During 1997, FNMA-mortgage-backed securities available for sale were sold which resulted in realized gain of $2 thousand. During 1996, Common Stock and FHLMC-REMICs were sold which resulted in realized gains of $51 thousand and $3 thousand, respectively.

4. LOANS, NET

Loans, net at December 31, 1998 and 1997 consist of the following:

	1998	1997
Mortgage Loans	$ 246,071,511	$ 253,000,504
Construction Loans	1,410,456	3,257,798
Commercial Construction	2,609,315	2,385,192
Consumer Loans	3,237,176	3,609,033
Commercial Real Estate	45,937,998	42,974,261
Commercial Business	4,120,967	1,712,099
Subtotal	303,387,423	306,938,887
Less:		
Deferred loan fees	1,441,926	970,075
Allowance for possible loan losses	3,342,274	3,137,781
Total loans, net	$ 298,603,223	$ 302,831,031

At December 31, 1998 and 1997 the recorded investment in loans for which impairment had been recognized in accordance with SFAS Nos. 114 and 118 totaled $3.2 million and $3.6 million, respectively. At December 31, 1998, impaired loans of $1.6 million related to loans that were individually measured for impairment with a valuation allowance of $363 thousand and $1.6 million of loans that were collectively measured for impairment with a valuation allowance of $69 thousand. At December 31, 1997 impaired loans of $1.6 million related to loans that were individually measured for impairment with a valuation allowance of $319 thousand and $2.0 million of loans that were collectively measured for impairment with a valuation allowance of $97 thousand. For the years ended December 31, 1998 and 1997, the average recorded investment in impaired loans was approximately $3.4 million and $3.5 million, respectively. During the years ended December 31, 1998 and 1997 the Corporation recognized $125 thousand and $192 thousand, respectively, of interest on impaired loans, all of which was recognized on the cash basis.

Loans which are 90 days delinquent as to principal and/or interest are placed on a non-accrual status and all previously accrued interest is reversed. The principal amount of non-accrual loans at December 31, 1998 and 1997 was $3.2 million and $3.6 million, respectively. Interest income on non-accrual loans that would have been recorded in 1998 under the original terms of such loans was $266 thousand, and the interest income actually recognized in 1998 for such loans was $119 thousand. Interest income on non-accrual loans that would have been recorded in 1997 under the original terms of such loans was $354 thousand, and the actual interest income recognized in 1997 for such loans was $185 thousand.

The Bank originates and purchases both adjustable and fixed interest rate loans. At December 31, 1998, the composition of these loans is as follows:

(In Thousands)	Maturing during 1999	Maturing from 2000 through 2003	Maturing after 2003	Total
Mortgage Loans (1-4 dwelling)	$ 1,715	$ 15,811	$ 228,546	$ 246,072
Construction Loans	1,264	0	146	1,410

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Commercial Construction	1,640	24	945	2,609
Consumer Loans	1,635	1,201	401	3,237
Commercial Real Estate	5,829	18,233	21,876	45,938
Commercial Business	1,892	1,740	489	4,121
Total	$ 13,975	$ 37,009	$ 252,403	$ 303,387
Interest sensitivity on the above loans:				
Loans with predetermined rates	$ 8,281	$ 30,331	$ 173,568	$ 212,180
Loans with adjustable or floating rates	5,695	6,678	78,834	91,207
Total	$ 13,976	$ 37,009	$ 252,402	$ 303,387

Construction, commercial and land loans are generally indexed to the prime rate plus a percentage (generally 1% to 2%). The adjustable rate mortgage loans have interest rate adjustment limitations and are generally indexed to the one year U.S. Treasury constant maturity yield. Future market factors may affect the correlation of the interest rate adjustment with the rates the Bank pays on the short-term deposits that have been primarily utilized to fund these loans.

Changes in the allowance for possible loan losses are as follows:

	Years ended December 31,		
	1998	1997	1996
Balance at beginning of year	$ 3,137,781	$ 2,781,937	$ 2,766,779
Provision charged to operations	240,000	400,000	120,000
Charge-offs	(37,876)	(49,042)	(115,253)
Recoveries	2,369	4,886	10,411
Balance at end of year	$ 3,342,274	$ 3,137,781	$ 2,781,937

5. MORTGAGE-BACKED SECURITIES

Mortgage-backed securities held to maturity at December 31, 1998 and 1997 are summarized as follows:

	December 31, 1998			
	Amortized Cost	Gross Unrealized Gains	Gross Unrealized (Losses)	Estimated Market Value
GNMA	$ 31,716,739	$ 599,765	$ (3,615)	$ 32,312,889
FNMA	37,531,455	597,103	(49,100)	38,079,458
FHLMC	21,255,729	524,392	(476)	21,779,645
Private	88,724	1,610	(33)	90,301
Total	$ 90,592,647	$ 1,722,870	$ (53,224)	$ 92,262,293

	December 31, 1997			
	Amortized Cost	Gross Unrealized Gains	Gross Unrealized (Losses)	Estimated Market Value
GNMA	$ 22,586,373	$ 785,155	$ (6)	$ 23,371,522
FNMA	35,648,943	604,826	(54,848)	36,198,921
FHLMC	33,379,272	968,264	(23,500)	34,324,036
Private	405,929	6,221	0	412,150
Total	$ 92,020,517	$ 2,364,466	$ (78,354)	$ 94,306,629

The Bank has the intent and ability to hold these securities to maturity. At December 31, 1998, neither a disposal, nor a condition that could lead to a decision not to hold these securities to maturity were reasonably foreseen.

6. OFFICE PROPERTIES AND EQUIPMENT, NET

Office properties and equipment at December 31, 1998 and 1997 are summarized by major classification, as follows:

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	December 31,	
	1998	1997
Land, buildings and improvements	$ 18,900,216	$ 16,269,867
Furniture and equipment	4,153,118	3,665,361
Computers	3,629,926	2,316,398
Total	26,683,260	22,251,626
Less accumulated depreciation	(7,391,013)	(6,559,571)
Office properties and equipment, net	$ 19,292,247	$ 15,692,055

7. REAL ESTATE HELD FOR DEVELOPMENT, NET

The Bank, through its wholly-owned subsidiary, Land Financial Services, Inc., has entered into several real estate investments. Real estate held for development is carried at the lower of cost or estimated net realizable value. Intercompany loans from the Bank are the primary sources of funding and have been eliminated in consolidation. Such investments in real estate at December 31, 1998 and 1997, are summarized as follows:

	December 31,	
	1998	1997
Real Estate held for development	$ 933,256	$ 933,256
Valuation allowance	(288,769)	(288,769)
Net	$ 644,487	$ 644,487

During 1997, the Bank recorded an additional $200 thousand provision on the real estate held for development. The losses were reflected as a charge to income in the other income section of the consolidated statements of operations.

Under the Financial Institutions Reform, Recovery and Enforcement Act of 1989 ("FIRREA"), the Bank is required to deduct from capital its investments in and advances to subsidiaries engaged in activities not permissible for national banks (i.e. real estate development).

8. REAL ESTATE OWNED, NET

Real estate owned, which was acquired through foreclosure and deeds in lieu of foreclosure, totaled $168 thousand and $446 thousand, net at December 31, 1998 and 1997, respectively. Changes in allowance for real estate owned is as follows:

	Years ended December 31,		
	1998	1997	1996
Balance at beginning of year	$ 560,137	$ 437,507	$ 313,192
Provisions charged to operations	108,102	142,630	153,482
Charge-offs	0	(20,000)	(29,717)
Recoveries	0	0	550
Balance at end of year	$ 668,239	$ 560,137	$ 437,507

9. DEPOSITS

Deposits at December 31, 1998 and 1997 consisted of the following major classifications and weighted average rates:

	December 31, 1998		
	Weighted Average Rate	Amount	Percent of Total
Non-interest checking	0.00 %	$ 69,336,887	12.93 %
Checking accounts	1.89	75,280,395	14.04
Savings accounts	2.83	95,591,907	17.82
Money market accounts	2.64	67,690,222	12.62

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Certificates	5.35	228,410,212	42.59
Total	3.49 %	$ 536,309,623	100.00 %

	December 31, 1997		
	Weighted Average Rate	Amount	Percent of Total
Non-interest checking	0.00 %	$ 49,875,981	10.19 %
Checking accounts	1.69	54,688,332	11.17
Savings accounts	2.87	83,824,897	17.13
Money market accounts	2.72	58,001,044	11.85
Certificates	5.32	243,049,726	49.66
Total	3.74 %	$ 489,439,980	100.00 %

A summary of certificates by maturity at December 31, 1998 is as follows:

Years ended December 31,	Amount
1999	$ 157,821,422
2000	37,135,760
2001	15,754,388
Thereafter	17,698,642
Total	$ 228,410,212

A summary of interest expense on deposits is as follows:

	Years ended December 31,		
	1998	1997	1996
Checking accounts	$ 1,263,105	$ 825,672	$ 693,879
Savings accounts	2,591,626	2,347,193	1,816,081
Money market accounts	1,697,154	1,629,248	1,519,789
Certificates	12,538,798	12,952,418	12,146,474
Total interest expense	$ 18,090,683	$ 17,754,531	$ 16,176,223

10. ADVANCES FROM FEDERAL HOME LOAN BANK

At December 31, 1998, the Bank had advances from the Federal Home Loan Bank of New York (FHLB) in the amount of $16.4 million with a weighted average interest rate of 6.00%. Advances are collateralized by certain first mortgage loans.

Years ended December 31,					
1998			1997		
Amount	Weighted Average Rate	Maturity Date	Amount	Weighted Average Rate	Maturity Date
			$ 2,100,000	7.13%	1/2/98
			1,000,000	4.95%	10/13/98
			5,000,000	6.14%	6/8/98
$ 10,000,000	6.32%	6/6/00	10,000,000	6.32%	6/6/00
5,000,000	5.62%	2/15/01	5,000,000	5.62%	2/15/01
1,368,321	5.00%	10/9/07	1,396,476	5.00%	10/9/07
$ 16,368,321	6.00%		$ 24,496,476	6.08%	

11. SECURITIES SOLD UNDER AGREEMENTS TO REPURCHASE

At December 31, 1998, the Bank had securities sold under the agreements to repurchase (repurchase agreements) in the aggregate amount of $80.0 million. The repurchase agreements are collateralized by U.S. Agency Notes and CMOs with a market value of $80.4 million. Accrued interest payable totaled $446 thousand at December 31, 1998.

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Year ended December 31, 1998

1998

Counterparty	Amount	Weighted Average Rate	Maturity Date	Call Feature
Merrill Lynch	$20,000,000	5.79%	9/19/02	9/19/00
FHLB	20,000,000	5.65%	11/18/02	11/18/00
FHLB	20,000,000	5.72%	12/19/07	12/19/02
FHLB	20,000,000	5.13%	1/14/08	1/14/01
Total	$80,000,000	5.57%		

Year ended December 31, 1997

Counterparty	Amount	Weighted Average Rate	Maturity Date	Call Feature
Merrill Lynch	$20,000,000	5.79%	9/19/02	9/19/00
FHLB	20,000,000	5.65%	11/18/02	11/18/00
FHLB	20,000,000	5.72%	12/19/07	12/19/02
Total	$60,000,000	5.72%		

12. INCOME TAXES

In accordance with the provisions of Statement of Financial Accounting Standards No. 109, "Accounting for Income Taxes" (SFAS No. 109), deferred tax assets and liabilities are established for the temporary differences between accounting bases and tax bases of the Corporation's assets and liabilities at the tax rates expected to be in effect when the temporary differences are realized or settled. Management believes the existing net deductible temporary differences which give rise to the net deferred income tax assets are realizable on a more likely than not basis.

The temporary differences that give rise to significant portions of deferred tax assets and deferred tax liability are as follows:

	December 31, 1998	December 31, 1997
Deferred income tax assets:		
Allowance for possible loan losses	$ 924,040	$ 677,181
Real estate losses	482,409	435,010
Deferred loan fees, net	(2,225)	(11,113)
Compensation and pension liability	49,822	49,822
Amortization of deposit premium	274,034	259,723
Post retirement benefits	185,000	185,000
Capitalized interest	284,690	274,951
Other	155,340	61,287
Gross deferred tax assets	2,353,110	1,931,861
Deferred income tax liabilities:		
Prepaid deposit insurance premium	48,912	26,936
Depreciation	288,426	397,618
Gross deferred tax liabilities:	337,338	424,554
Deferred income tax assets, net	$ 2,015,772	$ 1,507,307

The following represents the components of income tax expense for the years ended December 31, 1998, 1997 and 1996, respectively.

	1998	1997	1996
Current Federal tax provision	$ 3,008,922	$ 2,903,256	$ 1,862,681
Current State tax provision	284,193	292,221	181,544
Total Current provision	3,293,115	3,195,477	2,044,225
Deferred Federal tax benefit	(283,771)	(62,697)	(725,109)
Deferred State tax benefit	(25,811)	(5,703)	(39,617)

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Total Deferred benefit	(309,582)	(68,400)	(764,726)
Total	$ 2,983,533	$ 3,127,077	$ 1,279,499

On August 21, 1996, the Small Business Job Protection Act was signed into law which repealed the favorable reserve method available to savings banks. The Bank was required to change its tax bad debt method to the specific charge-off method effective for the fiscal year ended December 31, 1996. The change in method resulted in taxable income of approximately $2.4 million representing the excess of the Bank's tax bad debt reserve at December 31, 1995 over the base year reserve amount that arose in tax years beginning before December 31, 1987. The income will be recognized for tax purposes ratably over a six year period.

The Company has not provided deferred income taxes for the Bank's tax return reserve for bad debts that arose in tax years beginning before December 31, 1987 because it is not expected that this difference will reverse in the foreseeable future. A deferred tax liability has been recognized for the portion of the tax bad debt reserves which arose in years 1988 through 1995.

The Corporation's provision for income taxes differs from that computed by applying the statutory federal income tax rate to income before income taxes as follows:
<TABLE>
<CAPTION>

	1998		1997		1996	
	Amount	Percent	Amount	Percent	Amount	Percent
<S>	<C>	<C>	<C>	<C>	<C>	<C>
Tax at federal tax rate	$ 2,806,707	34.00%	$ 2,930,199	34.00%	$ 1,463,808	34.00%
Increase (Decrease) from:						
State income taxes, net of federal income tax benefit	170,531	2.07	189,102	2.19	93,672	2.18
Change in valuation allowance	0	0.00	0	0	(289,588)	-6.73
Other	6,295	0.00	7,776	0.09	11,607	0.27%
Total	$ 2,983,533	36.15%	$ 2,127,077	36.28%	$ 1,279,499	29.72%

</TABLE>

13. LEASES

The Bank leases two buildings and land to operate three branches under noncancelable leases which expire over the next 25 years. These leases generally provide for the payment of taxes and maintenance by the lessee. Most of these operating leases provide the Bank with the option to renew the lease after the initial lease term. Future minimum rental payments under existing leases as of December 31, 1998 are as follows:

Fiscal Year	Amount
1999	$ 127,202
2000	76,826
2001	76,826
2002	76,826
2003 and beyond	1,133,643
Total	$ 1,491,323

The leases for the buildings contain cost of living adjustments based on changes in the consumer price index. The minimum lease payments shown above include base rentals exclusive of any future adjustments. Total rent expense for all operating leases amounted to $105 thousand, $104 thousand and $107 thousand for fiscal years 1998, 1997 and 1996, respectively.

14. STOCKHOLDERS' EQUITY

On December 14, 1988, the Bank converted to a state chartered stock

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Savings Bank and simultaneously formed FMS Financial Corporation. At the time of conversion, eligible deposit account holders were granted priority in the unlikely event of a future liquidation of the Bank. The special reserve has been decreased to the extent that the balances of eligible account holders were reduced at annual determination dates. The Bank converted its charter to that of a Federal Savings Bank on October 15, 1993.

The ability of the Corporation to pay dividends to stockholders is directly dependent upon the ability of the Bank to pay dividends to the Corporation. OTS regulations restrict the ability of the Bank to pay dividends to the Corporation if such dividends reduce the net worth of the Bank below the amount required in the special reserve account and based on the Bank's net income and capital position.

Under FIRREA the Bank must have core capital equal to 4%, tangible capital equal to 2% and risk-based capital equal to 8%. At December 31, 1998, the Bank exceeded all three regulatory capital levels required under FIRREA. The Bank's regulatory tangible and core capital was $48.4 million or 7.02% of total bank assets and risk-based capital was $51.5 million or 18.13% of risk-weighted assets.

The following is a reconciliation of the Bank's capital under generally accepted accounting principles ("GAAP") to regulatory capital at December 31, 1998:

	Tangible Capital	Core Capital	Risk-based Capital
Bank's GAAP Capital	$ 49,695,061	49,695,061	49,695,061
Add:			
Unrealized loss on investments AFS	21,793	21,793	21,793
Less:			
Subsidiary investments not eligible	(965,474)	(965,474)	(965,474)
Goodwill	(164,969)	(164,969)	(164,969)
REO greater than 5 years	(149,541)	(149,541)	(149,541)
Supplementary qualifying capital item			
General valuation allowance	0	0	3,092,524
Regulatory capital computed	48,436,870	48,436,870	51,529,394
Minimum regulatory capital requirement	13,800,280	27,600,560	22,741,729
Regulatory capital excess	$ 34,636,590	$ 20,836,310	$ 28,787,665

15. PENSION PLAN

The Bank has a defined benefit pension plan for active employees. Net pension expense was $371 thousand, $385 thousand and $412 thousand for years ended December 31, 1998, 1997 and 1996, respectively. The components of net pension cost are as follows:

	Years ended December 31,		
	1998	1997	1996
Service Cost	$ 435,047	$ 401,818	$ 397,001
Interest Cost	270,772	232,376	204,457
Return on Assets	(359,216)	(286,070)	(596,276)
Net Amortization and Deferral	23,921	37,140	406,357
Net periodic pension cost	$ 370,524	$ 385,264	$ 411,539

The following table presents a reconciliation of the funded status of the defined benefit pension plan at December 31, 1998 and 1997:

December 31,

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	1998	1997
Projected benefit obligation	5,200,545	4,419,723
Fair value of plan assets	5,895,741	5,171,488
Excess of plan assets over projected benefit obligation	695,196	751,765
Unrecognized net gain	(1,153,817)	(876,493)
Unrecognized prior service cost	76,135	81,860
Unrecognized net transition obligation	162,569	193,475
(Accrued) Prepaid pension cost included in the consolidated balance sheet	$ (219,917)	$ 150,607

The following table presents a reconciliation of beginning and ending balances of benefit obligations and plan assets.

	December 31,	
Change in Project Benefit Obligation	1998	1997
Projected Benefit Obligation at Beginning of Year	$4,419,723	$3,959,973
Service Cost	435,047	401,818
Interest Cost	270,772	232,376
Amendments	0	0
Actuarial loss (gain)	133,501	(48,603)
Benefits Paid	(58,498)	(125,841)
Projected Benefit Obligation at End of Year	$5,200,545	$4,419,723
Change in Plan Assets		
Fair Value of Plan Assets at Beginnning of Year	$5,171,488	$4,105,395
Actual Return of Plan Assets	782,751	1,022,934
Employer Contribution	0	169,000
Plan Participants' Contributions	0	0
Benefits Paid	(58,498)	(125,841)
Fair Value of Plan Assets at End of Year	$5,895,741	$5,171,488

Actuarial assumptions used in determining pension cost are as follows:

	Years ended December 31,		
	1998	1997	1996
Discount rate for benefit obligation	6.00 %	6.00 %	6.00 %
Rate of increase in compensation levels and social security wage base	4.00 %	4.00 %	4.00 %
Expected long-term rate of return on plan assets	7.00 %	7.00 %	7.00 %

In addition to providing pension plan benefits, the Bank provides certain health care and life insurance benefits to certain retired employees. In accordance with the provisions of Statement of Financial Accounting Standards No. 106, "Employer Accounting for Post Retirement Benefits other than Pensions" (SFAS No. 106) the expected cost of such benefits must be actuarially determined and accrued ratably from the date of hire to the date the employee is fully eligible to receive benefits. The accumulated post-retirement benefit obligation is not funded but is reflected in the statement of financial condition as a liability.

The net periodic post-retirement benefit cost includes the following components:

December 31,

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	1998	1997
Service Cost	$ 0	$ 0
Interest Cost	30,514	31,938
Amortization of prior service cost	(14,499)	(10,854)
Amortization of Gain	(1,763)	(5,229)
Net periodic post-retirement benefit cost	$ 14,252	$ 15,855

The assumed discount rate used in the calculation for net periodic post-retirement benefit cost was 7.0% and 7.5% for 1998 and 1997, respectively. The assumed health care cost trend rate for 1998 was 6% and was graded down in 1% increments per year to an ultimate rate of 5% per year. The impact of a 1% increase in the assumed health care cost trend for each future year would be as follows:

	December 31, 1998
Accumulated post-retirement obligation at year end	$487,849
Service and Interest Cost	$32,847

The following table summarizes the amounts recognized in the Bank's balance sheet:

	December 31,	
	1998	1997
Accumulated post-retirement benefit obligation	$ (451,181)	$ (435,729)
Unrecognized prior service cost	(99,076)	(113,575)
Unrecognized net gain	(59,101)	(89,205)
Accrued post-retirement benefit cost	$ (609,358)	$ (638,509)

The assumed discount rate used in the calculation for the accumulated post-retirement benefit obligation as of December 31, 1998 and 1997 was 6.75% and 7.0%, respectively.

16. SUBORDINATED DEBENTURES

The Corporation issued $10.0 million of subordinated debentures. The debentures are unsecured, bear interest at a rate of 10% per annum and mature on July 28, 2004. Interest payments are due semiannually on February 1 and August 1 commencing February 1, 1995. The debentures are redeemable, in whole or in part, at any time at the option of the Corporation at specified redemption prices, except that the debentures could not be redeemed prior to August 1, 1997. The net proceeds from the sale of the debentures totaled $9.4 million and were used for the expansion of the Bank's operations through branch acquisitions and general corporate purposes. The Corporation is required to retain at all times cash, cash equivalents or marketable securities in an amount not less than the aggregate amount of two consecutive semi-annual interest payments that will be due and payable on the debentures following such declaration date or redemption date.

17. FAIR VALUE OF FINANCIAL INSTRUMENTS

The disclosure of the fair value of all financial instruments is required, whether or not recognized on the balance sheet, for which it is practical to estimate fair value. In cases where quoted market prices are not available, fair values are based on assumptions including future cash flows and discount rates. Accordingly, the fair value estimates cannot be substantiated, may not be realized, and do not represent the underlying value of the Corporation.

The Corporation uses the following methods and assumptions to estimate the fair value of each class of financial instruments for which it is practicable to estimate that value:

Cash and cash equivalents: The carrying value is a reasonable estimate of fair value.

Investment securities held to maturity, securities available for sale and mortgage-backed securties: Fair value is equal to quoted market prices.

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FHLB Stock: The stock of FHLB is issued only to FHLB member institutions and is redeemable only by another member institution or the FHLB at its $100 per share par value.

Loans: For variable-rate loans that reprice frequently and with no significant change in credit risk, fair value is the carrying value. For other categories of loans such as residential mortgages, commercial and consumer loans, fair value is estimated based on discounting the estimated future cash flows using the current rates at which similar loans would be made to borrowers with similar collateral and credit ratings and for similar remaining maturities.

Deposit liabilities: For checking, savings and money market accounts, fair value is the amount payable on demand at the reporting date. For certificates of deposits, fair value is estimated using the rates currently offered for deposits with similar remaining maturities.

Securities sold under agreements to repurchase: For investment securities with a quoted market price, fair value is equal to quoted market prices. If a quoted market price is not available, fair value is estimated using quoted market prices for similar securities.

Subordinated debentures: Fair value is estimated using the quoted average of the broker bid and ask prices at year end.

At December 31, 1998 and December 31, 1997, the carrying amount and the estimated market value of the Corporation's financial instruments are as follows:

<TABLE>
<CAPTION>

	December 31, 1998		December 31, 1997	
	Carrying Amount	Estimated Market Value	Carrying Amount	Estimated Market Value
<S>	<C>	<C>	<C>	<C>
Financial assets:				
Cash and cash equivalents	$ 29,896,391	$ 29,896,391	$ 12,631,622	$ 12,631,622
Investment securities held to maturity and investment securities available for sale	$ 239,250,959	$ 239,198,755	$ 192,688,137	$ 192,852,572
Mortgage-backed securities	$ 90,592,647	$ 92,262,293	$ 92,020,517	$ 94,306,629
FHLB Stock	$ 4,861,410	$ 4,861,410	$ 3,630,800	$ 3,630,800
Loans, net of unearned income	$ 301,945,497	$ 309,708,000	$ 305,968,812	$ 310,340,000
Less: Allowance for possible loan losses	(3,342,274)	(3,342,274)	(3,137,781)	(3,137,781)
Loans, net	$ 298,603,223	$ 306,365,726	$ 302,831,031	$ 307,202,219
Financial liabilities:				
Deposits				
Checking, passbook, and money market accounts	$ 307,899,411	$ 307,899,411	$ 246,390,254	$ 246,390,254
Certificates	$ 228,410,212	$ 229,028,000	$ 243,049,726	$ 241,393,000
Securities sold under agreements to repurchase	$ 80,000,000	$ 83,705,000	$ 60,000,000	$ 58,560,000
Subordinated debentures	$ 10,000,000	$ 10,500,000	$ 10,000,000	$ 10,600,000
Other borrowings	$ 16,368,321	$ 16,467,000	$ 24,529,957	$ 23,941,238
Off-balance sheet financial instruments:				
Commitments to extend credit	$ 29,758,602	$ 29,758,602	$ 25,528,246	$ 25,528,246
Standby letters of credit	$ 1,301,772	$ 1,301,772	$ 761,522	$ 761,522

</TABLE>

Other borrowings: Fair value is estimated using a discounted cash flow analysis.

Advances from Bank: The carrying value is a reasonable estimate of fair value due to the short term nature of these obligations.

Commitments to extend credit and standby letters of credit: For commitments and standby letters of credit expiring within 90 days or with a variable rate, the settlement amount is a reasonable estimate of fair value. For commitments and standby letters of credit expiring beyond 90 days or with a fixed rate, the fair value is the present value of the obligations based on current loan rates.

18. FEDERAL DEPOSIT INSURANCE CORPORATION IMPROVEMENT ACT ("FDICIA")

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The Federal Deposit Insurance Corporation Improvement Act of 1991 ("FDICIA") was enacted into law on December 19, 1991. The statute includes a number of additional supervisory measures. The additional supervisory powers and regulations mandated by FDICIA include a "Prompt Corrective Action" program that permits regulators to take increasingly harsh action against institutions that fail to meet certain new capital-based requirements. Various other sections of FDICIA impose substantial new audit and reporting requirements.

FDICIA also requires each regulatory agency to institute non-capital safety and soundness standards for each institution it regulates. These standards cover (1) internal controls, (2) loan documentation, (3) credit underwriting, (4) interest rate exposure, (5) asset growth, (6) compensation, fees and benefits paid to employees, officers and directors, (7) operational and managerial standards, and (8) asset quality, earnings and stock valuation standards for preserving a minimum ratio of market value to book value for publicly traded shares (if feasible). Many of the regulations required by FDICIA have been promulgated by federal regulators. As of December 31, 1998 management of the Bank believes that it is in compliance with the regulations adopted pursuant to FDICIA.

19. COMMITMENTS AND CONTINGENCIES

The Bank has outstanding loan commitments of $29.8 million as of December 31, 1998. Of these commitments outstanding, the breakdown between fixed and variable rate loans is as follows:

	December 31, 1998		
	Fixed Rate	Variable Rate	Total
Commitments to:			
fund loans	$ 6,566,280	$ 6,203,400	$ 12,769,680
Unused lines:			
Construction	0	1,796,435	1,796,435
Equity line of credit loans	0	15,192,487	15,192,487
	$ 6,566,280	$ 23,192,322	$ 29,758,602

In addition to outstanding loan commitments, the Bank as of December 31, 1998, issued $1.3 million in standby letters of credit to guarantee performance of a customer to a third party.

Commitments and standby letters of credit are issued in accordance with the same loan policies and underwriting standards as settled loans. Since some commitments and standby letters of credit are expected to expire without being drawn down, these amounts do not necessarily represent future cash requirements.

20. LITIGATION

There are no significant pending legal proceedings at December 31, 1998 which will have a material impact on the Corporation's financial position or results of operations.

21. LOANS TO OFFICERS AND DIRECTORS

Regulation O provides that all loans to executive officers and directors be made on substantially the same terms and conditions as are available to the general public. On November 11, 1996, Regulation O was amended to allow executive officers to participate in any employee loan rate discount benefit program available to all full-time employees. Since the Bank offers such an employee benefit program, the policy governing loans to executive officers was amended to allow the executive officers to participate in this loan program and thereby receive rate discounts. These changes went into effect on January 1, 1997. The rate discounts are available to employees as long as they are employed at the Bank. If employment is terminated, the rate discount ceases from the date of termination. At December 31, 1998 and 1997, loans made to directors and executive officers whose indebtedness exceeded $60 thousand amounted to $1.5 million and $764 thousand, respectively. During 1998 new loans to these individuals totaled $785 thousand and repayments totaled $33 thousand.

22. EMPLOYEE STOCK OWNERSHIP PLAN

In connection with the conversion to stock form, the Corporation established an Employee Stock Ownership Plan ("ESOP"), which purchased approximately $660 thousand worth of common stock. In order to make the purchase, the ESOP borrowed approximately $660 thousand on December 8, 1988 from a commercial bank. The debt, which accrues interest at 80% of the commercial bank's base rate, has been guaranteed by the Corporation, and is payable and expensed in ten annual installments of approximately $66 thousand. Additional principal payments may be made from cash dividends paid on the unallocated ESOP

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shares.

Annual contributions to the ESOP are made in amounts determined by the Board of Directors. Because the Corporation's loan guarantee represents a commitment either to make future contributions to the ESOP or to make the principal payments when due, the guarantee has been reflected as a liability, and an offsetting charge equivalent to the future contributions to be made has been reflected as a reduction of stockholders' equity in the accompanying consolidated statements of financial condition.

23. STOCK OPTIONS

The Corporation has established a stock compensation plan (the "Plan") for executive officers and other selected employees of the Corporation. The Plan consists of incentive stock options intended to qualify under Section 422A of the Internal Revenue Code of 1986. These stock options may be surrendered and stock appreciation rights may be granted in their place, with the approval of the Corporation.

A total of 241,926 shares of authorized but unissued common stock of the Corporation has been reserved for future issuance under the Plan. The option price per share for options granted may not be less than the fair market value of the common stock on the date of grant. At December 31, 1998, the option exercise prices are $1.292, $5.333 and $10.00. Options are fully vested at the date of grant and must be exercised within ten years.

A summary of the status of the Bank's Stock Option Plan as of December 31, 1998, 1997 and 1996 and changes during the years ending on those dates is presented below.

	Years Ended December 31,					
	1998		1997		1996	
	Shares	Weighted Average Exercise Price	Shares	Weighted Average Exercise Price	Shares	Weighted Average Exercise Price
Outstanding at the Beginning of the year	235,995	$1.91	246,453	$1.88	287,469	$1.80
Options granted	93,000	10.00	0	0	0	0
Options exercised	(84,081)	1.29	(4,458)	1.29	(3,750)	1.29
Options surrendered	(34,296)	1.29	(6,000)	1.29	(37,266)	1.29
Outstanding at the End of the Year	210,618	$6.83	235,995	$1.91	246,453	$1.88

On January 1, 1996, the Bank adopted Statement of Financial Accounting Standard No. 123, "Accounting for Stock Based Compensation" (SFAS No. 123). As permitted by SFAS No. 123, the Bank has chosen to continue to apply APB Opinion No. 25, "Accounting for Stock Issued to Employees" (APB No. 25) and related interpretations in accounting for its Plan. Accordingly, no compensation cost has been recognized for options granted under the Plan. If the Bank had adopted the fair value method of accounting for stock based compensation the Bank's net income and net income per share would have been as follows:

	December 31, 1998	
	As Reported	Pro Forma
Net Income	$ 5,271,488	$ 5,042,974
Basic Earnings per share	$0.73	$0.70
Diluted Earnings per share	$0.72	$0.69

The fair value of each option grant is estimated on the date of grant using the Black-Scholes option pricing model with the following assumptions: dividend yield of .86%, expected volatility of 26.11%, discount rate of 6.0% and an expected life of 10 years at December 31, 1998. There were no options granted in 1997 or 1996.

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24. RISKS AND UNCERTAINTIES

The earnings of the Corporation depend on the earnings of the Bank. The earnings of the Bank depend primarily upon the level of net interest income, which is the difference between interest earned on its interest-earning assets, such as loans and investments and the interest paid on its interest-bearing liabilities, such as deposits and borrowings. Accordingly, the operations of the Bank are subject to risks and uncertainties surrounding its exposure to changes in the interest rate environment.

Most of the Bank's lending activity is with customers located within southern New Jersey. Generally, the loans are secured by real estate consisting of single family residential properties. While this represents a concentration of credit risk, the credit losses arising from this type of lending compare favorably with the Bank's credit loss experience on its portfolio as a whole. The ultimate repayment of these loans is dependent to a certain degree on the local economy and real estate market.

The financial statements of the Corporation are prepared in conformity with generally accepted accounting principles that require management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosures of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reported period. Actual results could differ from these estimates.

Significant estimates are made by management in determining the allowance for possible loan losses and carrying values of real estate owned and real estate held for development. Consideration is given to a variety of factors in establishing these estimates including current economic conditions, diversification of the loan portfolio, delinquency statistics, results of loan reviews, borrowers' perceived financial and managerial strengths, the adequacy of underlying collateral, if collateral dependent, or present value of future cash flows and other relevant factors. Since the allowance for possible loan losses and carrying value of real estate assets and real estate held for development is dependent, to a great extent, on the general economy and other conditions that may be beyond the Bank's control, it is at least reasonably possible that the estimates of the allowance for possible loan losses and the carrying values of the real estate assets could differ materially in the near term.

25. PARENT COMPANY FINANCIAL INFORMATION

The financial statements for FMS Financial Corporation are as follows:

<TABLE>
<CAPTION>

FMS Financial Corporation Statements of Financial Condition	December 31, 1998	December 31, 1997
<S>	<C>	<C>
Assets:		
Cash	$ 499,293	$ 397,911
Investment in Subsidiary	49,913,393	45,662,960
Investment Securities	1,000,000	1,000,000
Intercompany receivable, net	2,199,643	1,924,945
Subordinated debentures issue costs, net	321,113	378,460
Other	168,843	168,843
Total Assets	$54,102,285	$49,533,119
Liabilities:		
10% Subordinated debentures due 2004	$10,000,000	$10,000,000
Guarantee of employee stock ownership plan debt	0	33,481
Dividends payable	216,953	167,154
Accrued interest payable	416,667	416,667
Total Liabilities	$10,633,620	$10,617,302
Stockholder's Equity:		
Preferred stock -$.10 par value 5,000,000 shares authorized; none issued		
Common stock - $.10 par value 10,000,000 shares authorized; shares issued 7,897,191* and 2,604,370 and shares outstanding 7,231,916 as of December 31, 1998 and 1997, respectively	789,719	260,437
Paid-in capital in excess of par*	8,216,719	8,419,167
Unrealized (loss) gain on securities available for sale, net of deferred income taxes	(21,793)	53,955
Guarantee of employee stock ownership plan debt	0	(33,481)

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Retained earnings	37,860,291	33,406,060
Less: Treasury stock (665,424* and 216,454 shares, at cost at December 31, 1998 and 1997, respectively)	(3,376,372)	(3,190,321)
Total Stockholder's equity	43,468,665	38,915,817
Total Liabilities and Stockholder's Equity	$54,102,285	$49,533,119

</TABLE>

* Common stock, paid-in capital in excess of par and treasury stock at December 31, 1998 reflect a three-for-one stock split paid in July 1998.

<TABLE>
<CAPTION>

FMS Financial Corporation Statements of Operations	Years Ended December 31, 1998	1997	1996
Intercompany interest income	$ 560,750	$ 560,750	$ 560,750
Interest expense	(1,057,348)	(1,057,348)	(1,057,348)
Dividends from subsidiary	1,600,000	1,400,000	1,400,000
Equity in undistributed income of subsidiary	3,999,243	4,418,909	1,953,576
Income before taxes	5,102,645	5,322,311	2,856,978
Income tax benefit	168,843	168,843	168,843
Net Income	$ 5,271,488	$ 5,491,154	$ 3,025,821

</TABLE>

These statements should be read in conjunction with the other notes related to the consolidated financial statements.

<TABLE>
<CAPTION>

FMS Financial Corporation Statements of Cash Flows	For Years Ended December 31, 1998	1997	1996
Operating Activities			
Net income	$ 5,271,488	$ 5,491,154	$ 3,025,821
Adjustments to reconcile net income to net cash provided by operating activities:			
Equity in undistributed earnings of the subsidiary	(3,999,243)	(4,418,909)	(1,953,576)
Amortization of bond issue costs	57,347	57,349	57,348
Decrease in interest payable	0	0	0
Decrease (Increase) in intercompany receivable, net	(274,698)	(333,389)	1,452,440
Other operating activities	33,481	72,982	75,292
Net cash provided by operating activities	1,088,375	869,187	2,657,325
Financing Activities			
Purchase of treasury stock	(186,055)	(127,361)	(1,913,191)
Investment in subsidiary	(108,603)	(5,758)	(4,843)
Cash dividends paid on common stock	(767,457)	(525,479)	(495,434)
Principal repayment of employee stock ownership plan debt	(33,481)	(72,982)	(75,981)
Proceeds from issuance of stock	108,603	5,758	4,843
Net cash used by financing activities	(986,993)	(725,822)	(2,484,606)
INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS	101,382	143,365	172,719
CASH AND CASH EQUIVALENTS, BEGINNING OF YEAR	397,911	254,546	81,827
CASH AND CASH EQUIVALENTS, END OF YEAR	$ 499,293	$ 397,911	$ 254,546

</TABLE>

These statements should be read in conjunction with the other notes related to the consolidated financial statements.

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MANAGEMENT REPORT

To the Federal Deposit Insurance Corporation and the Office of Thrift Supervision:

FINANCIAL STATEMENTS

Management of FMS Financial Corporation and Subsidiary ("the Corporation") is responsible for the preparation, integrity, and fair presentation of its published consolidated financial statements, and Thrift Financial Report (TFR) filed with the Office of Thrift Supervision, as of December 31, 1998, and for the year then ended. The published consolidated financial statements have been prepared in accordance with generally accepted accounting principles, and the Thrift Financial Report has been prepared in accordance with the Office of Thrift Supervision reporting instructions, and, as such, include some amounts that are based upon judgments and estimates of management.

INTERNAL CONTROL STRUCTURE OVER FINANCIAL REPORTING

Management is responsible for establishing and maintaining an effective internal control structure over financial reporting. The system contains monitoring mechanisms and actions are taken to correct deficiencies identified.

There are inherent limitations in the effectiveness of any system of internal control, including the possibility of human error and the circumvention or overriding of controls. Accordingly, even an effective internal control system can provide only reasonable assurance with respect to consolidated financial statement preparation. Further, because of changes in conditions, the effectiveness of an internal control system may vary over time.

Management assessed its internal control structure over financial reporting as of December 31, 1998. This assessment was based on criteria for effective internal control over financial reporting described in "Internal Control-Integrated Framework" issued by the Committee of Sponsoring Organization of the Treadway Commission. Based on this assessment, management believes that the Corporation maintained an effective internal control structure over financial reporting as of December 31, 1998.

COMPLIANCE WITH LAWS AND REGULATIONS

Management is also responsible for compliance with federal and state laws and regulations concerning dividend restrictions and federal laws and regulations concerning loans to insiders designated by the Federal Deposit Insurance Corporation as safety and soundness laws and regulations.

Management assessed its compliance with the designated laws and regulations relating to safety and soundness. Based on this assessment, management believes that the Corporation has complied, in all significant respects, with the designated laws and regulations related to safety and soundness for the year ended December 31, 1998.

/s/ Craig W. Yates
Craig W. Yates
President and Chief Executive Officer

/s/ Channing L. Smith
Channing L. Smith
Vice President and
Chief Financial Officer

FMS Financial Corporation
Burlington, New Jersey
February 16, 1999

PRICEWATERHOUSECOOPERS [LOGO]

REPORT OF INDEPENDENT ACCOUNTANTS

To the Board of Directors of FMS Financial Corporation:

In our opinion, the accompanying consolidated balance sheets and related consolidated statements of operations, changes in stockholders' equity, and cash flows present fairly, in all material respects, the financial position of FMS Financial Corporation and Subsidiary ("the Company") at December 31, 1998 and 1997, and the results of its operations and their cash flows for each of the three years in the period ended December 31, 1998, in conformity with generally accepted accounting principles. These financial statements are the

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responsibility of the Company's management; our responsibility is to express an opinion on these financial statements based on our audits. We conducted our audits of these statements in accordance with generally accepted auditing standards which require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, and evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for the opinion expressed above.

/s/ PricewaterhouseCoopers LLP

2400 Eleven Penn Center
Philadelphia, Pennsylvania
February 16, 1999

CORPORATE INFORMATION

ANNUAL MEETING

The 1999 Annual Shareholders' Meeting of FMS Financial Corporation will be held at 10:00 a.m., on the 29th day of April, 1999 at the Burlington Country Club, Burrrs Road, Westampton, New Jersey.

STOCK MARKET INFORMATION

The common stock of FMS Financial Corporation is traded over-the-counter and is listed on the Nasdaq National Market System under the symbol "FMCO". Daily quotations are included in the Nasdaq National Market stock tables published in the Wall Street Journal and other leading newspapers.

The number of record holders of common stock of the Corporation as of March 1, 1999 was approximately 788, not including those shares registered in names of various investment brokers held in account for their customers.

The following table sets forth the range of closing prices, as reported by Nasdaq, for the periods ended December 31, 1998 and 1997:

	1998	
QUARTER ENDED	HIGH	LOW
March 31,	$ 12.167	$ 11.167
June 30,	$ 17.000	$ 12.201
September 30,	$ 15.500	$ 9.500
December 31,	$ 10.625	$ 6.875

	1997	
QUARTER ENDED	HIGH	LOW
March 31,	$ 6.917	$ 6.125
June 30,	$ 8.500	$ 6.250
September 30,	$ 10.500	$ 7.833
December 31,	$ 11.833	$ 9.083

The Corporation's sole operating assets are derived from its subsidiary, Farmers & Mechanics Bank. Consequently, the ability of the Corporation to accumulate cash for payment of cash dividends to stockholders is directly dependent upon the ability of the Bank to pay dividends to the Corporation.

There are regulatory limitations on the ability of the Bank to pay cash dividends to the Corporation which could, in turn, be used by the Corporation to pay cash dividends to its stockholders. Interest on savings accounts must be paid by the Bank prior to payment of dividends on the common stock. Additionally, the Corporation must pay interest to holders of its debentures before payment of cash dividends to its stockholders. Under the regulations of the OTS, the Bank is not permitted to pay dividends on its stock if its regulatory capital would be reduced below the amount required for the liquidation account established in connection with its mutual-to-stock conversion. The Bank will not be permitted to pay dividends on its capital stock if its regulatory capital would be reduced below the regulatory capital requirements prescribed for institutions regulated by the OTS. Further, income

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appropriated to bad debt reserves and deducted for federal income tax purposes cannot be used to pay cash dividends without the payments of federal income taxes on the amount of such income removed from reserves for such purpose at the then current income tax rate.

The Bank's ability to pay cash dividends or make other capital distributions to the Corporation is also governed by OTS regulations. Under these regulations, "capital distributions" are defined as cash dividends, payments by savings associations to repurchase or otherwise acquire its shares, payments to shareholders of another entity in a cash-out merger, and other distributions charged against capital. An institution that has regulatory capital that is at least equal to its capital requirement and that has not been notified that it "is in need of more than normal supervision," is a Tier 1 institution. A Tier 1 institution is permitted under OTS regulations, after prior notice to (and no objection by) the OTS, to make capital distributions during a calendar year up to 100% of its year to date net income plus the amount that would reduce by one-half its "surplus capital ratio", which is the percentage by which the ratio of its regulatory capital to assets exceeds the ratio of its fully phased-in capital requirement to assets at the beginning of the calendar year. As of December 31, 1998 the Bank was a Tier 1 institution and had available $18.3 million for dividends to the Corporation, subject to nonobjection by the OTS. It is not likely that the Corporation would request a dividend of that magnitude.

The Corporation is not subject to OTS regulatory restrictions on the payment of dividends to its stockholders, although the source of such dividends is dependent upon dividends received by it from the Bank. The Corporation is subject, however, to the requirements of New Jersey law, which permits the Corporation to pay dividends in cash or shares out of the Corporation's surplus, defined as the excess of net assets of the Corporation over stated capital.

BOARD OF DIRECTORS

CHARLES B. YATES
Chairman of the Board

WAYNE H. PAGE
Vice Chairman

GEORGE J. BARBER

DOMINIC W. FLAMINI

VINCENT R. FARIAS

RUPERT A. HALL, JR.

JAMES C. LIGNANA

EDWARD J. STAATS, JR.

MARY WELLS

CRAIG W. YATES

DIRECTORS EMERITUS

ADOLPH N. BRIGHT

KAREN S. OLEKSA

HILYARD S. SIMPKINS

BANK OFFICERS

CHARLES B. YATES*
Chairman of the Board

CRAIG W. YATES*
President

JAMES E. IGO*
Sr. Vice President and Chief Lending Officer

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CHANNING L. SMITH*
Vice President and Chief Financial Officer

THOMAS M. TOPLEY*
Sr. Vice President of Operations and
Corporate Secretary

DOUGLAS B. HALEY
Vice President, Consumer Lending

KAREN R. KOENIG
Vice President, Business Development

NANCY L. PARKER
Vice President, Human Resources

PETER S. SCHOENFELD
Vice President, Investments

KAREN D. SHINN
Vice President, Operations

FRANK E. SMITH
Vice President, Facilities and Design

MERLE A. BROWN
Security Officer

AMY J. HANNIGAN
Controller

MARCELLA F. HATCHER*
Assistant Secretary

* Officers of Bank and Holding Company

MARKET MAKERS

The following companies were making a market in the Corporation's common stock at December 31, 1998:

Advest, Inc.
280 Trumbull Street
1 Commercial Plaza
Hartford, CT 06103
(203) 541-5441

Robert W. Baird & Co., Inc.
4300 W. Cypress Street
Tampa, FL 33607
(813) 877-4000

Ryan Beck & Co.
80 Main Street
W. Orange NJ 07052
(973) 597-6000

Trident Securities
1275 Peachtree Street, NE
Suite 460
Atlanta, GA
(404) 249-7700

FORM 10-K AND OTHER FINANCIAL INQUIRIES

The Corporation's Annual Report on Form 10-K for the fiscal year ended December 31, 1998, as filed with the Securities and Exchange Commission will be furnished to shareholders of the Corporation upon written request without charge. Shareholders, analysts and others seeking this and other requests for information relating to stock, annual shareholders' meeting and related matters on FMS Financial Corporation, should contact the Corporate Secretary at the Executive Offices.

Transfer Agent and Registrar
American Stock Transfer and Trust Company
40 Wall Street
New York, NY 10005

Auditors
PricewaterhouseCoopers LLP
2400 Eleven Penn Center
Philadelphia, PA 19103

Special Counsel
Malizia, Spidi, Sloane & Fisch, P.C.
One Franklin Square
1301 K Street, N.W.
Suite 700 East
Washington, D.C. 20005

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OFFICE LOCATIONS

EXECUTIVE AND ADMINISTRATIVE OFFICES
3 Sunset Road and 811 Sunset Road
Burlington NJ 08016
(609) 386-2400

MAIN BRANCH
3 Sunset Road
Burlington, NJ 08016
(609) 387-2728

BEVERLY
414 Cooper Street
Beverly, NJ 08010
(609) 239-4066

BORDENTOWN
335 Farnsworth Ave.
Bordentown, NJ 08505
(609) 291-8200

BROWNS MILLS
93 Pemberton-Browns Mills Road
Browns Mills, NJ 08015
(609) 893-5540

BURLINGTON CITY
352 High Street
Burlington, NJ 08016
(609) 386-4643

BURLINGTON TOWNSHIP
809 Sunset Road
Burlington, NJ 08016
(609) 387-1150

CHESTERFIELD
305 Bordentown-Chesterfield Road
Chesterfield, NJ 08620
(609) 324-1256

CINNAMINSON
1703 Highland Avenue
Cinnaminson, NJ 08077
(609) 303-1870 *

DELRAN
3002 Route 130 North
Delran, NJ 08075
(609) 764-3740 *

EASTAMPTON
1191 Woodlane Road
Eastampton, NJ 08060
(609) 261-6400

EDGEWATER PARK
1149 Cooper Street
Edgewater Park, NJ 08010
(609) 387-0046

LARCHMONT
3220 Route 38
Mount Laurel, NJ 08054
(609) 235-6666 *

LUMBERTON
1636-61 Route 38 & Eayrestown Road
Lumberton, NJ 08048
(609) 267-6811

MEDFORD
200 Tuckerton Road
Medford, NJ 08055

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(609) 596-4300 *

MEDFORD LAKES
712 Stokes Road
Medford, NJ 08055
(609) 654-6373

MEDFORD VILLAGE
1 S. Main Street at Bank Street
Medford, NJ 08055
(609) 714-1115

MOORESTOWN
53 East Main Street
Moorestown, NJ 08057
(609) 235-0544 *

MOUNT LAUREL
4522 Church Road
Mount Laurel, NJ 08054
(609) 235-4445 *

RIVERSIDE
Scott Street & Pavilion Avenue
Riverside, NJ 08075
(609) 461-4333 *

RIVERTON
604 Main Street
Riverton, NJ 08077
(609) 786-5333 *

SOUTHAMPTON
1841 Route 70
Southampton, NJ 08088
(609) 859-2700

TABERNACLE
1507 Route 206
Tabernacle, NJ 08088
(609) 268-5993

WILLINGBORO
John F. Kennedy Way & Charleston Rd.
Willingboro, NJ 08046
(609) 877-2888

WILLINGBORO EAST
611 Beverly-Rancocas Road
One East Ridge Shopping Center
Willingboro, NJ 08046
(609) 871-4900

WILLINGBORO WEST
1 Rose Street & Beverly-Rancocas Road
Willingboro, NJ 08046
(609) 835-4700
(609) 654-6373

* Effective 6/12/99 the area code for these branches will be changed to #856.

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EXHIBIT 21

Subsidiaries of the Registrant(1)

	State of Incorporation	Percentage Ownership
Farmers and Mechanics Bank	United States	100%
FMS Financial Services, Inc.(2)(4)	New Jersey	100%
Land Financial Services, Inc.(2)	New Jersey	100%
First Plunge, Inc. (3)(4)	New Jersey	100%
Fishpond, Inc. (3)(4)	New Jersey	100%
Angell Ayes, Inc. (3)(4)	New Jersey	100%
Peter's Passion, Inc. (3)(4)	New Jersey	100%
Atlantic Adventures, Inc.(3)	New Jersey	100%

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(1) The operations of the subsidiaries are included in the consolidated financial statements contained in the Annual Report to Stockholders attached as Exhibit 13 to the Form 10-K.

(2) Subsidiary of Farmers and Mechanics Bank.

(3) Subsidiary of Land Financial Services, Inc.

(4) Currently an inactive subsidiary.

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EXHIBIT 23

CONSENT OF INDEPENDENT ACCOUNTANTS

We consent to the incorporation by reference in the Registration Statement of FMS Financial Corporation on Form S-8 (File No. 33-24340) of our report dated February 16, 1999 on our audits of the consolidated financial statements of FMS Financial Corporation and Subsidiary as of December 31, 1998 and 1997 and for each of the three years in the period ended December 31, 1998, which report is incorporated by reference in this Annual Report on Form 10-K.

/s/ PricewaterhouseCoopers LLP

PRICEWATERHOUSECOOPERS LLP

2400 Eleven Penn Center
Philadelphia, Pennsylvania
March 26, 1999

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