PEOPLES FINANCIAL CORP /MS/
Form 10-Q
August 13, 2012

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-Q

x **QUARTERLY REPORT PURSUANT TO SECTION 13 or 15 (D) OF THE SECURITIES EXCHANGE ACT OF 1934**

For the quarterly period ended June 30, 2012

or

¨ **TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(D) OF THE SECURITIES EXCHANGE ACT OF 1934**

Commission File Number 001-12103

PEOPLES FINANCIAL CORPORATION

(Exact name of registrant as specified in its charter)

Mississippi	**64-0709834**
(State or other jurisdiction of	**(I.R.S. Employer**
incorporation or organization)	**Identification No.)**

Lameuse and Howard Avenues, Biloxi, Mississippi **39533**
(Address of principal executive offices) **(Zip Code)**
(228) 435-5511

(Registrant s telephone number, including area code)

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

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files.) Yes x No ¨

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

Large accelerated filer ¨	Accelerated filer ¨
Non-accelerated filer ¨ (Do not check if a smaller reporting company)	Smaller reporting company x

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

Indicate the number of shares outstanding of each of the issuer s classes of common stock, as of the last practicable date. Peoples Financial Corporation has only one class of common stock authorized. At July 31, 2012, there were 15,000,000 shares of $1 par value common stock authorized, with 5,136,136,918 shares issued and outstanding.

Part 1 Financial Information

Item 1: Financial Statements

Peoples Financial Corporation and Subsidiaries

Consolidated Statements of Condition

	June 30, 2012 (Unaudited)	December 31, 2011 (Audited)
Assets		
Cash and due from banks	$ 34,202,485	$ 36,928,657
Available for sale securities	327,013,590	278,918,481
Held to maturity securities, fair value of $5,075,817 at June 30, 2012; $1,492,374 at December 31, 2011	4,983,923	1,428,887
Other investments	3,893,458	3,930,300
Federal Home Loan Bank Stock, at cost	4,259,400	2,580,700
Loans	427,591,007	432,407,286
Less: Allowance for loan losses	6,743,248	8,135,622
Loans, net	420,847,759	424,271,664
Bank premises and equipment, net of accumulated depreciation	27,022,147	28,035,308
Other real estate	7,522,811	6,153,238
Accrued interest receivable	3,103,191	2,698,241
Cash surrender value of life insurance	16,513,580	16,196,368
Prepaid FDIC assessments	1,278,989	2,096,320
Other assets	1,966,261	913,926
Total assets	$ 852,607,594	$ 804,152,090

Peoples Financial Corporation and Subsidiaries

Consolidated Statements of Condition (continued)

	June 30, 2012 (Unaudited)	December 31, 2011 (Audited)
Liabilities & Shareholders Equity		
Liabilities:		
Deposits:		
Demand, non-interest bearing	$ 114,738,363	$ 97,581,073
Savings and demand, interest bearing	223,487,560	205,318,859
Time, $100,000 or more	94,501,700	115,014,220
Other time deposits	48,840,880	50,524,930
Total deposits	481,568,503	468,439,082
Federal funds purchased and securities sold under agreements to repurchase	161,987,702	157,600,967
Borrowings from Federal Home Loan Bank	83,017,894	53,323,568
Employee and director benefit plans liabilities	11,959,093	11,310,607
Other liabilities	3,346,358	4,025,565
Total liabilities	741,879,550	694,699,789
Shareholders Equity:		
Common stock, $1 par value, 15,000,000 shares authorized, 5,136,918 shares issued and outstanding at June 30, 2012 and December 31, 2011	5,136,918	5,136,918
Surplus	65,780,254	65,780,254
Undivided profits	34,417,370	33,350,861
Accumulated other comprehensive income, net of tax	5,393,502	5,184,268
Total shareholders equity	110,728,044	109,452,301
Total liabilities & shareholders equity	$ 852,607,594	$ 804,152,090

See accompanying notes to consolidated financial statements.

Peoples Financial Corporation and Subsidiaries

Consolidated Statements of Income

(Unaudited)

	Three Months Ended June 30, 2012	Three Months Ended June 30, 2011	Six Months Ended June 30, 2012	Six Months Ended June 30, 2011
Interest income:				
Interest and fees on loans	$ 4,510,481	$ 4,381,186	$ 9,152,016	$ 9,287,948
Interest and dividends on securities:				
U.S. Treasuries	114,400	62,933	169,225	126,459
U.S. Government agencies	1,198,685	1,676,822	2,240,355	3,074,718
Mortgage-backed securities	70,701	30,957	150,996	30,957
States and political subdivisions	376,146	395,564	739,835	806,468
Other investments	41	2,421	4,750	8,639
Interest on federal funds sold	2,648	3,386	9,066	4,738
Total interest income	6,273,102	6,553,269	12,466,243	13,339,927
Interest expense:				
Deposits	409,184	651,406	843,946	1,354,117
Borrowings from Federal Home Loan Bank	68,502	45,402	119,121	95,467
Federal funds purchased and securities sold under agreements to repurchase	97,988	169,545	217,072	341,568
Total interest expense	575,674	866,353	1,180,139	1,791,152
Net interest income	5,697,428	5,686,916	11,286,104	11,548,775
Provision for allowance for loan losses	1,290,000	546,000	1,830,000	1,187,000
Net interest income after provision for allowance for loan losses	$ 4,407,428	$ 5,140,916	$ 9,456,104	$ 10,361,775

Peoples Financial Corporation and Subsidiaries

Consolidated Statements of Income (continued)

(Unaudited)

	Three Months Ended June 30, 2012	Three Months Ended June 30, 2011	Six Months Ended June 30, 2012	Six Months Ended June 30, 2011
Non-interest income:				
Trust department income and fees	$ 328,093	$ 323,468	$ 671,892	$ 669,923
Service charges on deposit accounts	1,427,287	1,455,146	2,884,235	2,874,174
Gain on sales and calls of securities	859,942	7,174	964,175	7,174
Gain (loss) on other investments	17,796		(36,843)	10,124
Increase in cash surrender value of life insurance	125,283	125,380	246,674	257,680
Gain on death benefits from life insurance		389,119		389,119
Other income	139,241	151,035	286,202	266,038
Total non-interest income	2,897,642	2,451,322	5,016,335	4,474,232
Non-interest expense:				
Salaries and employee benefits	3,047,676	3,395,090	6,319,397	6,771,387
Net occupancy	655,345	655,236	1,274,288	1,269,170
Equipment rentals, depreciation and maintenance	876,961	951,812	1,654,076	1,822,212
FDIC assessments	443,338	437,086	884,483	842,912
Data processing	364,908	148,562	736,589	292,860
ATM Expense	494,701	519,622	973,823	1,004,382
Other expense	917,388	866,957	1,710,274	1,927,667
Total non-interest expense	6,800,317	6,974,365	13,552,930	13,930,590
Income before income tax benefit	504,753	617,873	919,509	905,417
Income tax benefit	(57,000)	(192,000)	(147,000)	(342,000)
Net income	$ 561,753	$ 809,873	$ 1,066,509	$ 1,247,417
Basic and diluted earnings per share	$ .11	$ .16	$ .21	$ .24
Dividends declared per share	$	$ .09	$	$ .09

See accompanying notes to consolidated financial statements.

Peoples Financial Corporation and Subsidiaries

Consolidated Statements of Comprehensive Income

(Unaudited)

	Three Months Ended June 30, 2012	Three Months Ended June 30, 2011	Six Months Ended June 30, 2012	Six Months Ended June 30, 2011
Net Income	$ 561,753	$ 809,873	$ 1,066,509	$ 1,247,417
Other comprehensive income (loss), net of tax:				
Net unrealized gain on available for sale securities, net of taxes of $1,311,457 and $1,744,254 for the three months ended June 30, 2012 and 2011, respectively, and $435,606 and $2,216,603 for the six months ended June 30, 2012 and 2011, respectively	2,545,771	3,385,905	845,590	4,302,818
Reclassification gains on available for sale securities called or sold in current year, net of taxes of $(246,462) and $(2,439) for the three months ended June 30, 2012 and 2011, respectively, and $(327,819) and $(2,439) for the six months ended June 30, 2012 and 2011, respectively	(478,427)	(4,735)	(636,356)	(4,735)
Total other comprehensive income	2,067,344	3,381,170	209,234	4,298,083
Total comprehensive income	$ 2,629,097	$ 4,191,043	$ 1,275,743	$ 5,545,500

See accompanying notes to consolidated financial statements.

Peoples Financial Corporation and Subsidiaries

Consolidated Statement of Changes in Shareholders Equity

	Number of Common Shares	Common Stock	Surplus	Undivided Profits	Accumulated Other Comprehensive Income	Total
Balance, January 1, 2012	5,136,918	$ 5,136,918	$ 65,780,254	$ 33,350,861	$ 5,184,268	$ 109,452,301
Net income				1,066,509		1,066,509
Other comprehensive income, net of tax					209,234	209,234
Balance, June 30, 2012	5,136,918	$ 5,136,918	$ 65,780,254	$ 34,417,370	$ 5,393,502	$ 110,728,044

Note: Balances as of January 1, 2012 were audited.

See accompanying notes to consolidated financial statements.

Peoples Financial Corporation and Subsidiaries

Consolidated Statements of Cash Flows

(Unaudited)

	Six Months Ended June 30, 2012	2011
Cash flows from operating activities:		
Net income	$ 1,066,509	$ 1,247,417
Adjustment to reconcile net income to net cash provided by operating activities:		
Depreciation	1,034,000	1,176,000
Provision for allowance for loan losses	1,830,000	1,187,000
Writedown of other real estate	153,300	124,606
Loss on sales of other real estate	24,739	25,291
Gain (loss) on other investments	36,843	(10,124)
Gain on sales and calls of securities	(964,175)	(7,174)
Accretion of held to maturity securities	(436)	(1,444)
Change in accrued interest receivable	(404,950)	(239,584)
Gain on death benefits from life insurance		(389,119)
Increase in cash surrender value of life insurance	(246,674)	(257,680)
Change in other assets	(235,443)	2,605,373
Change in other liabilities	381,770	80,850
Net cash provided by operating activities	$ 2,675,483	$ 5,541,412

Peoples Financial Corporation and Subsidiaries

Consolidated Statements of Cash Flows (continued) (unaudited)

	Six Months Ended June 30, 2012	2011
Cash flows from investing activities:		
Proceeds from maturities, sales and calls of available for sale securities	$ 180,716,805	$ 78,710,848
Purchases of available for sale securities	(227,537,305)	(104,646,484)
Purchases of held to maturity securities	(3,554,600)	
Redemption of other investments		93,040
(Purchases) redemption of Federal Home Loan Bank stock	(1,678,700)	128,200
Proceeds from sales of other real estate	344,061	358,526
Loans, net change	(297,768)	12,457,729
Acquisition of premises and equipment	(20,839)	(272,904)
Proceeds from death benefits from life insurance		583,793
Investment in cash surrender value of life insurance	(70,099)	(62,015)
Net cash used in investing activities	(52,098,445)	(12,649,267)
Cash flows from financing activities:		
Demand and savings deposits, net change	35,325,991	25,664,495
Time deposits, net change	(22,196,570)	(11,384,574)
Cash dividends	(513,692)	(462,323)
Retirement of common stock		(192,560)
Borrowings from Federal Home Loan Bank	1,185,266,252	330,002,395
Repayments to Federal Home Loan Bank	(1,155,571,926)	(344,003,538)
Federal funds purchased and securities sold under agreements to repurchase, net change	4,386,735	28,942,450
Net cash provided by financing activities	46,696,790	28,566,345
Net increase (decrease) in cash and cash equivalents	(2,726,172)	21,458,490
Cash and cash equivalents, beginning of period	36,928,657	24,146,939
Cash and cash equivalents, end of period	$ 34,202,485	$ 45,605,429

See accompanying notes to consolidated financial statements.

PEOPLES FINANCIAL CORPORATION AND SUBSIDIARIES

NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS

For the Six Months Ended June 30, 2012 and 2011

1. Basis of Presentation:

Peoples Financial Corporation (the Company) is a one-bank holding company headquartered in Biloxi, Mississippi. Its two operating subsidiaries are The Peoples Bank, Biloxi, Mississippi (the Bank), and PFC Service Corp. Its principal subsidiary is The Peoples Bank, Biloxi, Mississippi, which provides a full range of banking, financial and trust services to state, county and local government entities and individuals and small and commercial businesses operating in those portions of Mississippi, Louisiana and Alabama which are within a fifty mile radius of the Waveland, Wiggins and Gautier branches, the Bank s three most outlying locations (the trade area).

The accompanying unaudited consolidated financial statements and notes thereto contain all adjustments, consisting only of normal recurring adjustments, necessary to present fairly, in accordance with accounting principles generally accepted in the United States of America (GAAP), the financial position of the Company and its subsidiaries as of June 30, 2012 and the results of their operations and their cash flows for the periods presented. The interim financial information should be read in conjunction with the annual consolidated financial statements and the notes thereto included in the Company s 2011 Annual Report and Form 10-K.

The results of operations for the quarter ended June 30, 2012, are not necessarily indicative of the results to be expected for the full year.

Use of Estimates The preparation of financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the consolidated financial statements and the reported amounts of revenues and expenses during the reported period. Actual results could differ from those estimates. Material estimates common to the banking industry that are particularly susceptible to significant change in the near term include, but are not limited to, the determination of the allowance for loan losses, the valuation of other real estate acquired in connection with foreclosure or in satisfaction of loans and valuation allowances associated with the realization of deferred tax assets, which are based on future taxable income.

Summary of Significant Accounting Policies The accounting and reporting policies of the Company conform with GAAP and general practices within the banking industry. There have been no material changes or developments in the application of principles or in our evaluation of the accounting estimates and the underlying assumptions or methodologies that we believe to be Critical Accounting Policies as disclosed in our Form 10-K for the year ended December 31, 2011.

2. Earnings Per Share:

Per share data is based on the weighted average shares of common stock outstanding of 5,136,918 for the six months ended June 30, 2012 and 2011.

3. Statements of Cash Flows:

The Company has defined cash and cash equivalents as cash and due from banks. The Company paid $1,180,163 and $1,811,218 for the six months ended June 30, 2012 and 2011, respectively, for interest on deposits and borrowings. Income tax payments of $615,000 and $235,000 were made during the six months ended June 30, 2012 and 2011. Loans transferred to other real estate amounted to $1,891,673 and $2,927,510 during the six months ended June 30, 2012 and 2011, respectively. Dividends payable of $513,692 and $462,323 as of December 31, 2011 and 2010, were paid during the six months ended June 30, 2012 and 2011, respectively.

4. Investments:

The amortized cost and fair value of securities at June 30, 2012 and December 31, 2011, are as follows:

June 30, 2012	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
Available for sale securities:				
Debt securities:				
U.S. Treasuries	$ 48,912,626	$ 604,585	$ (11,218)	$ 49,505,993
U.S. Government agencies	215,666,588	1,838,275	(64,400)	217,440,463
Mortgage-backed securities	19,168,371	356,332	(6,543)	19,518,160
States and political subdivisions	37,659,159	2,239,832		39,898,991
Total debt securities	321,406,744	5,039,024	(82,161)	326,363,607
Equity securities	649,983			649,983
Total available for sale securities	$ 322,056,727	$ 5,039,024	$ (82,161)	$ 327,013,590
Held to maturity securities:				
States and political subdivisions	$ 4,983,923	$ 92,535	$ (641)	$ 5,075,817
Total held to maturity securities	$ 4,983,923	$ 92,535	$ (641)	$ 5,075,817

December 31, 2011	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
Available for sale securities:				
Debt securities:				
U.S. Treasuries	$ 53,994,598	$ 33,297	$ (18,284)	$ 54,009,611
U.S. Government agencies	176,985,676	2,220,753	(26,144)	179,180,285
Mortgage-backed securities	4,727,055	274,100		5,001,155
States and political subdivisions	37,914,334	2,163,113		40,077,447
Total debt securities	273,621,663	4,691,263	(44,428)	278,268,498
Equity securities	649,983			649,983
Total available for sale securities	$ 274,271,646	$ 4,691,263	$ (44,428)	$ 278,918,481
Held to maturity securities:				
States and political subdivisions	$ 1,428,887	$ 63,487	$	$ 1,492,374
Total held to maturity securities	$ 1,428,887	$ 63,487	$	$ 1,492,374

The amortized cost and fair value of debt securities at June 30, 2012, by contractual maturity, are shown on the next page. Expected maturities will differ from contractual maturities because borrowers may have the right to call or prepay obligations with or without call or prepayment penalties.

	Amortized Cost	Fair Value
Available for sale securities:		
Due in one year or less	$ 15,777,229	$ 15,783,341
Due after one year through five years	75,682,518	76,496,170
Due after five years through ten years	117,542,039	120,432,646
Due after ten years	93,236,587	94,133,290
Mortgage-backed securities	19,168,371	19,518,160
Totals	$ 321,406,744	$ 326,363,607
Held to maturity securities:		
Due in one year or less	$ 169,813	$ 172,603
Due after one year through five years	1,545,816	1,595,798
Due after five years through ten years	1,206,445	1,221,271
Due after ten years	2,061,849	2,086,145
Totals	$ 4,983,923	$ 5,075,817

Available for Sale and Held to Maturity Securities with gross unrealized losses at June 30, 2012 and December 31, 2011, aggregated by investment category and length of time that individual securities have been in a continuous loss position are as follows:

	Less Than Twelve Months		Over Twelve Months		Total	
	Fair Value	Gross Unrealized Losses	Fair Value	Gross Unrealized Losses	Fair Value	Gross Unrealized Losses
June 30, 2012:						
U.S. Treasuries	$ 21,978,420	$ 11,218	$	$	$ 21,978,420	$ 11,218
U.S. Government agencies	24,935,600	64,400			24,935,600	64,400
Mortgage-backed securities	5,097,099	6,543			5,097,099	6,543
States and political subdivisions	285,841	641			285,841	641
TOTAL	$ 52,296,960	$ 82,802	$	$	$ 52,296,960	$ 82,802
December 31, 2011:						
U.S. Treasuries	$ 16,975,720	$ 18,284	$	$	$ 16,975,720	$ 18,284
U.S. Government agencies	15,075,582	26,144			15,075,582	26,144
TOTAL	$ 32,051,302	$ 44,428	$	$	$ 32,051,302	$ 44,428

Management evaluates securities for other-than-temporary impairment on a monthly basis. In performing this evaluation, the length of time and the extent to which the fair value has been less than cost, the fact that the Company s securities are primarily issued by U.S. Treasury and U.S. Government Agencies and the cause of the decline in value are considered. In addition, the Company does not intend to sell and it is not more likely than not that it will be required to sell these securities before maturity. While some available for sale securities have been sold for liquidity purposes or for gains, the Company has traditionally held its securities, including those classified as available for sale, until maturity. As a result of the evaluation of these securities, the Company has determined that the unrealized losses summarized in the tables above are not deemed to be other-than-temporary.

Proceeds from sales of available for sale debt securities were $44,771,114 and $3,025,000 for the six months ended June 30, 2012 and 2011, respectively. Available for sale debt securities were sold and called for realized gains of $964,175 and $7,174 for the six months ended June 30, 2012 and 2011, respectively.

5. Loans:

The composition of the loan portfolio at June 30, 2012 and December 31, 2011, is as follows:

	June 30, 2012	December 31, 2011
Gaming	$ 59,296,895	$ 57,219,236
Residential and land development	27,631,420	29,026,076
Real estate, construction	53,829,647	61,041,510
Real estate, mortgage	245,962,520	238,411,440
Commercial and industrial	30,846,870	33,950,494
Other	10,023,655	12,758,530
Total	$ 427,591,007	$ 432,407,286

The age analysis of the loan portfolio, segregated by class of loans, as of June 30, 2012 and December 31, 2011, is as follows:

	Number of Days Past Due						Loans Past Due Greater Than 90
	30 - 59	60 - 89	Greater Than 90	Total Past Due	Current	Total Loans	Days & Still Accruing
June 30, 2012:							
Gaming	$	$	$	$	$ 59,296,895	$ 59,296,895	$
Residential and land development			1,615,039	1,615,039	26,016,381	27,631,420	
Real estate, construction	1,763,617	2,105,773	4,427,823	8,297,213	45,532,434	53,829,647	
Real estate, mortgage	7,908,629	1,859,221	7,596,158	17,364,008	228,598,512	245,962,520	67,011
Commercial and industrial	2,344,367	69,549	393,942	2,807,858	28,039,012	30,846,870	
Other	241,878	29,578	387	271,843	9,751,812	10,023,655	387
Total	$ 12,258,491	$ 4,064,121	$ 14,033,349	$ 30,355,961	$ 397,235,046	$ 427,591,007	$ 67,398
December 31, 2011:							
Gaming	$	$	$	$	$ 57,219,236	$ 57,219,236	$
Residential and land development			24,161,722	24,161,722	4,864,354	29,026,076	
Real estate, construction	2,084,061	1,394,738	6,364,135	9,842,934	51,198,576	61,041,510	368,524
Real estate, mortgage	13,569,639	2,340,776	12,963,395	28,873,810	209,537,630	238,411,440	1,314,317
Commercial and industrial	1,536,073	166,070	387,963	2,090,106	31,860,388	33,950,494	142,125
Other	183,900	22,665	130,576	337,141	12,421,389	12,758,530	
Total	$ 17,373,673	$ 3,924,249	$ 44,007,791	$ 65,305,713	$ 367,101,573	$ 432,407,286	$ 1,824,966

The Company monitors the credit quality of its loan portfolio through the use of a loan grading system. A score of 1 5 is assigned to the loan on factors including repayment ability, trends in net worth and/or financial condition of the borrower and guarantors, employment stability, management ability, loan to value fluctuations, the type and structure of the loan, conformity of the loan to bank policy and payment performance. Based on the total score, a loan grade of A F is applied. A grade of A will generally be applied to loans for customers that are well known to the Company and that have excellent sources of repayment. A grade of B will generally be applied to loans for customers that have excellent sources of repayment which have no identifiable risk of collection. A grade of C will generally be applied to loans for customers that have adequate sources of repayment which have little identifiable risk of collection. Loans with a grade of C may be placed on the watch list if weaknesses are not resolved which could result in potential loss. A grade of D will generally be applied to loans for customers that are inadequately protected by current sound net worth, paying capacity of the borrower, or pledged collateral. Loans with a grade of D have unsatisfactory characteristics such as cash flow deficiencies, bankruptcy filing by the borrower or dependence on the sale of collateral for the primary source of repayment, causing more than acceptable levels of risk. Loans 60 to 89 days past due receive a grade of D. A grade of E will generally be applied to loans for customers with weaknesses inherent in the D classification and in which collection or liquidation in full is questionable. All loans 90 days or more past due are rated E. A grade of F is applied to loans which are considered uncollectible and of such little value that their continuance in an active bank is not warranted. Loans with this grade are charged off, even though partial or full recovery may be possible in the future. All loans 180 days or more past due are rated F and charged off unless the Bank is in the process of collection.

An analysis of the loan portfolio by loan grade, segregated by class of loans, as of June 30, 2012 and December 31, 2011, is as follows:

	Loans With A Grade Of:				
	A or B	C	D	E	Total
June 30, 2012:					
Gaming	$ 26,471,751	$ 7,815,522	$ 10,108,687	$ 14,900,935	$ 59,296,895
Residential and land development	6,291,938			21,339,482	27,631,420
Real estate, construction	41,088,982	2,065,821	3,492,777	7,182,067	53,829,647
Real estate, mortgage	199,127,681	10,372,796	22,428,354	14,033,689	245,962,520
Commercial and industrial	20,390,301	7,684,953	2,646,851	124,765	30,846,870
Other	9,849,420	45,419	128,429	387	10,023,655
Total	$ 303,220,073	$ 27,984,511	$ 38,805,098	$ 57,581,325	$ 427,591,007
December 31, 2011:					
Gaming	$ 41,816,764	$	$	$ 15,402,472	$ 57,219,236
Residential and land development	4,865,153		50,545	24,110,378	29,026,076
Real estate, construction	50,797,910	357,114	3,695,437	6,191,049	61,041,510
Real estate, mortgage	197,509,767	2,862,368	25,869,734	12,169,571	238,411,440
Commercial and industrial	23,972,076	6,551,489	3,077,347	349,582	33,950,494
Other	12,266,764	40,454	384,146	67,166	12,758,530
Total	$ 331,228,434	$ 9,811,425	$ 33,077,209	$ 58,290,218	$ 432,407,286

Total loans on nonaccrual as of June 30, 2012 and December 31, 2011, are as follows:

	June 30, 2012	December 31, 2011
Gaming	$ 14,900,935	$ 15,402,472
Residential and land development	21,339,482	24,110,378
Real estate, construction	5,680,262	6,041,822
Real estate, mortgage	12,928,691	11,661,628
Commercial and industrial	118,843	245,839
Other		130,576
Total	$ 54,968,213	$ 57,592,715

The Company has modified certain loans by granting interest rate concessions to these customers. These loans are in compliance with their modified terms, are currently accruing and the Company has classified them as troubled debt restructurings. Troubled debt restructurings as of June 30, 2012 and December 31, 2011 were as follows:

	Number of Contracts	Pre-Modification Outstanding Recorded Investment	Post-Modification Outstanding Recorded Investment	Related Allowance
June 30, 2012:				
Real estate, construction	1	$ 181,364	$ 181,364	$ 86,000
Real estate, mortgage	3	9,072,468	9,072,468	833,000
Commercial and industrial	1	705,262	705,262	
Total	5	$ 9,959,094	$ 9,959,094	$ 919,000
December 31, 2011:				
Real estate, construction	3	$ 1,075,176	$ 1,075,176	$ 112,000
Real estate, mortgage	5	9,915,672	9,915,672	809,000
Commercial and industrial	1	706,336	706,336	
Total	9	$ 11,697,184	$ 11,697,184	$ 921,000

During the six months ended June 30, 2012, four loans which had been classified as troubled debt restructurings at December 31, 2011 became in default of their modified terms and were placed on nonaccrual. These loans included two loans that were included in the real estate construction segment with a total balance of $891,986 and two loans that were included in the real estate mortgage segment with a total balance of $1,018,076 as of December 31, 2011.

Impaired loans, segregated by class of loans, as of June 30, 2012 and December 31, 2011, are as follows:

	Unpaid Principal Balance	Recorded Investment	Related Allowance	Average Recorded Investment
June 30, 2012:				
With no related allowance recorded:				
Gaming	$ 14,900,935	$ 14,900,935	$	$ 15,054,087
Residential and land development	22,442,813	21,339,482		22,170,733
Real estate, construction	5,022,369	4,958,814		4,263,144
Real estate, mortgage	11,675,201	11,039,458		10,883,018
Commercial and industrial	858,105	824,105		814,174
Total	$ 54,899,423	$ 53,062,794	$	$ 53,185,156
With a related allowance recorded:				
Real estate, construction	$ 902,812	$ 902,812	$ 246,000	$ 912,159
Real estate, mortgage	10,961,701	10,961,701	1,254,054	9,370,443
Total	$ 11,864,513	$ 11,864,513	$ 1,500,054	$ 10,282,602
Total by class of loans:				
Gaming	$ 14,900,935	$ 14,900,935	$	$ 15,054,087
Residential and land development	22,442,813	21,339,482		22,170,733
Real estate, construction	5,925,181	5,861,626	246,000	5,175,303
Real estate, mortgage	22,636,902	22,001,159	1,254,054	20,253,461
Commercial and industrial	858,105	824,105		814,174
Total	$ 66,763,936	$ 64,927,307	$ 1,500,054	$ 63,467,758

	Unpaid Principal Balance	Recorded Investment	Related Allowance	Average Recorded Investment
December 31, 2011:				
With no related allowance recorded:				
Gaming	$ 15,402,472	$ 15,402,472	$	$ 12,488,307
Residential and land development	24,940,695	21,745,946		7,382,320
Real estate, construction	4,743,490	4,711,470		297,328
Real estate, mortgage	9,965,290	9,956,982		1,110,547
Commercial and industrial	864,485	864,485		412,683
Other	5,308	5,308		
Total	$ 55,921,740	$ 52,686,663	$	$ 21,691,185
With a related allowance recorded:				
Gaming	$	$	$	$
Residential and land development	2,364,432	2,364,432	900,000	
Real estate, construction	2,405,528	2,405,528	720,000	184,519
Real estate, mortgage	12,550,318	11,620,318	1,314,011	5,971,190
Commercial and industrial	87,690	87,690	76,818	
Other	125,268	125,268	16,900	30,733
Total	$ 17,533,236	$ 16,603,236	$ 3,027,729	$ 6,186,442
Total by class of loans:				
Gaming	$ 15,402,472	$ 15,402,472	$	$ 12,488,307
Residential and land development	27,305,127	24,110,378	900,000	7,382,320
Real estate, construction	7,149,018	7,116,998	720,000	481,847
Real estate, mortgage	22,515,608	21,577,300	1,314,011	7,081,737
Commercial and industrial	952,175	952,175	76,818	412,683
Other	130,576	130,576	16,900	30,733
Total	$ 73,454,976	$ 69,289,899	$ 3,027,729	$ 27,877,627

Interest income of $173,712 and $211,188 was recognized on impaired loans for the six months ended June 30, 2012 and the year ended December 31, 2011.

6. Allowance for Loan Losses:

Transactions in the allowance for loan losses for the quarters and six months ended June 30, 2012 and 2011, and the balances of loans, individually and collectively evaluated for impairment as of June 30, 2012 and 2011, are as follows (in thousands):

	Gaming	Residential and Land Development	Real Estate, Construction	Real Estate, Mortgage	Commercial and Industrial	Other	Total
For the Six Months Ended June 30, 2012:							
Allowance for Loan Losses:							
Beginning Balance	$ 457	$ 1,081	$ 937	$ 4,800	$ 557	$ 304	$ 8,136
Charge-offs	(275)	(1,103)	(474)	(1,102)	(160)	(179)	(3,293)
Recoveries					14	56	70
Provision	292	225	(14)	1,178	46	103	1,830
Ending Balance	$ 474	$ 203	$ 449	$ 4,876	$ 457	$ 284	$ 6,743
For the Quarter Ended June 30, 2012:							
Allowance for Loan Losses:							
Beginning Balance	$ 632	$ 1,041	$ 496	$ 5,016	$ 547	$ 316	$ 8,048
Charge-offs	(275)	(1,103)		(1,003)	(101)	(126)	(2,608)
Recoveries					4	9	13
Provision	117	265	(47)	863	7	85	1,290
Ending Balance	$ 474	$ 203	$ 449	$ 4,876	$ 457	$ 284	$ 6,743
Allowance for loan losses, June 30, 2012:							
Ending balance: individually evaluated for impairment	$	$	$ 401	$ 1,605	$ 236	$ 35	$ 2,277
Ending balance: collectively evaluated for impairment	$ 474	$ 203	$ 48	$ 3,271	$ 221	$ 249	$ 4,466
Total Loans, June 30, 2012:							
Ending balance: Individually evaluated for impairment	$ 25,010	$ 21,339	$ 9,572	$ 36,462	$ 2,772	$ 129	$ 95,284
Ending balance: collectively evaluated for impairment	$ 34,287	$ 6,292	$ 44,258	$ 209,500	$ 28,075	$ 9,895	$ 332,307

	Gaming	Residential and Land Development	Real Estate, Construction	Real Estate, Mortgage	Commercial and Industrial	Other	Total
For the Six Months Ended June 30, 2011:							
Allowance for Loan Losses:							
Beginning Balance	$ 466	$ 1,069	$ 1,020	$ 3,413	$ 480	$ 202	$ 6,650
Charge-offs			(212)	(956)	(46)	(102)	(1,316)
Recoveries	35	32		46	16	63	192
Provision	(249)	(572)	226	1,638	40	104	1,187
Ending Balance	$ 252	$ 529	$ 1,034	$ 4,141	$ 490	$ 267	$ 6,713
For the Quarter Ended June 30, 2011:							
Allowance for Loan Losses:							
Beginning Balance	$ 233	$ 613	$ 1,260	$ 4,217	$ 692	$ 90	$ 7,105
Charge-offs			(212)	(708)	(25)	(72)	(1,017)
Recoveries	35				3	41	79
Provision	(16)	(84)	(14)	632	(180)	208	546
Ending Balance	$ 252	$ 529	$ 1,034	$ 4,141	$ 490	$ 267	$ 6,713
Allowance for loan losses, June 30, 2011:							
Ending balance: individually evaluated for impairment	$	$	$ 250	$ 1,754	$ 302	$ 53	$ 2,359
Ending balance: collectively evaluated for impairment	$ 252	$ 529	$ 784	$ 2,387	$ 188	$ 214	$ 4,354
Total Loans, June 30, 2011:							
Ending balance: Individually evaluated for impairment	$ 22,303	$ 19,891	$ 9,834	$ 32,391	$ 1,892	$ 295	$ 86,606
Ending balance: collectively evaluated for impairment	$ 22,607	$ 9,233	$ 52,175	$ 187,786	$ 22,571	$ 12,411	$ 306,783

7. Deposits:

At June 30, 2012, time deposits of $100,000 or more include brokered deposits of $23,612,000. Of the total brokered deposits, $10,000,000 matures in 2012 and the remaining balance matures in 2013.

8. Shareholders Equity:

On July 25, 2012, the Board of Directors of the Company declared a semi-annual dividend of $ .10 per share. The dividend has a record date of August 10, 2012 and a distribution date of August 17, 2012.

9. Accumulated Other Comprehensive Income:

At June 30, 2012, accumulated other comprehensive income included the unrealized gain on available for sale securities of $3,285,479, net of tax of $1,692,519, and the gain from the unfunded post-retirement benefit obligation of $2,108,023, net of tax of $1,085,528.

10. Fair Value Measurements and Disclosures:

The Company utilizes fair value measurements to record fair value adjustments to certain assets and liabilities and to determine fair value disclosures. Available for sale securities are recorded at fair value on a recurring basis. Additionally, from time to time, the Company may be required to record other assets at fair value on a non-recurring basis, such as impaired loans and ORE. These non-recurring fair value adjustments typically involve application of lower of cost or market accounting or write-downs of individual assets. Additionally, the Company is required to disclose, but not record, the fair value of other financial instruments.

Fair Value Hierarchy

The Company groups assets and liabilities at fair value in three levels, based on the markets in which the assets and liabilities are traded and the reliability of the assumptions used to determine fair value. These levels are:

Level 1 Valuation is based upon quoted prices for identical instruments traded in active markets.

Level 2 Valuation is based upon quoted market prices for similar instruments in active markets, quoted prices for identical or similar instruments in markets that are not active and model-based valuation techniques for which all significant assumptions are observable in the market.

Level 3 Valuation is generated from model-based techniques that use at least one significant assumption not observable in the market. These unobservable assumptions reflect estimates of assumptions that market participants would use in pricing the asset or liability. Valuation techniques include the use of option pricing models, discounted cash flow models and similar techniques.

Following is a description of valuation methodologies used to determine the fair value of financial assets and liabilities.

Cash and Due from Banks

The carrying amount shown as cash and due from banks approximates fair value.

Available for Sale Securities

The fair value of available for sale securities is based on quoted market prices. The Company s available for sale securities are reported at their estimated fair value, which is determined utilizing several sources. The primary source is Interactive Data Corporation, which utilizes pricing models that vary based on asset class and include available trade, bid and other market information and whose methodology includes broker quotes, proprietary models and vast descriptive databases. The other source for determining fair value is matrix pricing, which is a mathematical technique used widely in the industry to value debt securities without relying exclusively on quoted prices for the specific securities but rather by relying on the securities relationship to other benchmark securities. All of the Company s available for sale securities are Level 2 assets.

Held to Maturity Securities

The fair value of held to maturity securities is based on quoted market prices.

Other Investments

The carrying amount shown as other investments approximates fair value.

Federal Home Loan Bank Stock

The carrying amount shown as Federal Home Loan Bank Stock approximates fair value.

Loans

The fair value of fixed rate loans is estimated by discounting the future cash flows using the current rates at which similar loans would be made to borrowers with similar credit ratings for the remaining maturities. The cash flows considered in computing the fair value of such loans are segmented into categories relating to the nature of the contract and collateral based on contractual principal maturities. Appropriate adjustments are made to reflect probable credit losses. Cash flows have not been adjusted for such factors as prepayment risk or the effect of the maturity of balloon notes. The fair value of floating rate loans is estimated to be its carrying value. At each reporting period, the Company determines which loans are impaired. Accordingly, the Company s impaired loans are reported at their estimated fair value on a non-recurring basis. An allowance for each impaired loan, which are generally collateral-dependent, is calculated based on the fair value of its collateral. The fair value of the collateral is based on appraisals performed by third-party valuation specialists. Factors including the assumptions and techniques utilized by the appraiser are considered by Management. If the recorded investment in the impaired loan exceeds the measure of fair value of the collateral, a valuation allowance is recorded as a component of the allowance for loan losses. The Company records impaired loans as a non-recurring Level 3 asset.

Other Real Estate

In the course of lending operations, Management may determine that it is necessary to foreclose on the related collateral. Other real estate acquired through foreclosure is carried at fair value, less estimated costs to sell. The fair value of the collateral is based on appraisals performed by third-party valuation specialists. Factors including the assumptions and techniques utilized by the appraiser are considered by Management. If the current appraisal is more than one year old and/or the loan balance is more than $200,000, a new appraisal is obtained. Otherwise, the Bank s in-house property evaluator and Management will determine the fair value of the collateral, based on comparable sales, market conditions, Management s plans for disposition and other estimates of fair value obtained from principally independent sources, adjusted for estimated selling costs. The Company records other real estate as a non-recurring Level 3 asset.

Cash Surrender Value of Life Insurance

The carrying amount of cash surrender value of bank-owned life insurance approximates fair value.

Deposits

The fair value of non-interest bearing demand and interest bearing savings and demand deposits is the amount reported in the financial statements. The fair value of time deposits is estimated by discounting the cash flows using current rates of time deposits with similar remaining maturities. The cash flows considered in computing the fair value of such deposits are based on contractual maturities, since approximately 98% of time deposits provide for automatic renewal at current interest rates.

Federal Funds Purchased and Securities Sold under Agreements to Repurchase

The carrying amount shown as federal funds purchased and securities sold under agreements to repurchase approximates fair value.

Borrowings from Federal Home Loan Bank

The fair value of FHLB fixed rate borrowings is estimated using discounted cash flows based on current incremental borrowing rates for similar types of borrowing arrangements. The Company has no FHLB variable rate borrowings.

Commitments to Extend Credit and Standby Letters of Credit

Because commitments to extend credit and standby letters of credit are generally short-term and at variable rates, the contract value and estimated value associated with these instruments are immaterial.

The balances of available for sale securities, which are the only assets measured at fair value on a recurring basis, by level within the fair value hierarchy and by investment type, as of June 30, 2012 and December 31, 2011 are as follows:

		Fair Value Measurement Using		
	Total	Level 1	Level 2	Level 3
June 30, 2012:				
U.S. Treasuries	$ 49,505,993	$	$ 49,505,993	$
U.S. Government agencies	217,440,463		217,440,463	
Mortgage-backed securities	19,518,160		19,518,160	
States and political subdivisions	39,898,991		39,898,991	
Equity securities	649,983		649,983	
Total	$ 327,013,590	$	$ 327,013,590	$
December 31, 2011:				
U.S. Treasuries	$ 54,009,611	$	$ 54,009,611	$
U.S. Government agencies	179,180,285		179,180,285	
Mortgage-backed securities	5,001,155		5,001,155	
States and political subdivisions	40,077,447		40,077,447	
Equity securities	649,983		649,983	
Total	$ 278,918,481	$	$ 278,918,481	$

Impaired loans, which are measured at fair value on a non-recurring basis, by level within the fair value hierarchy as of June 30, 2012 and December 31, 2011 are as follows:

		Fair Value Measurement Using		
	Total	Level 1	Level 2	Level 3
June 30, 2012	$ 63,427,253	$	$	$ 63,427,253
December 31, 2011	66,262,170			66,262,170

The following table presents a summary of changes in the fair value of impaired loans which are measured using level 3 inputs:

	For the Six Months Ended June 30, 2012	For the Year Ended December 31, 2011
Balance, beginning of period	$ 66,262,170	$ 14,294,758
Additions to impaired loans and troubled debt restructurings	3,822,892	61,165,501
Principal payments, charge-offs and transfers to other real estate	(8,185,484)	(7,115,192)
Change in allowance for loan losses on impaired loans	1,527,675	(2,082,897)
Balance, end of period	$ 63,427,253	$ 66,262,170

Other real estate, which is measured at fair value on a non-recurring basis, by level within the fair value hierarchy as of June 30, 2012 and December 31, 2011 are as follows:

		Fair Value Measurement Using		
	Total	Level 1	Level 2	Level 3
June 30, 2012	$ 7,522,811	$	$	$ 7,522,811
December 31, 2011	6,153,238			6,153,238

The following table presents a summary of changes in the fair value of other real estate which is measured using level 3 inputs:

	For the Six Months Ended June 30, 2012	For the Year Ended December 31, 2011
Balance, beginning of period	$ 6,153,238	$ 5,744,150
Loans transferred to ORE	1,891,673	3,221,510
Sales	(368,800)	(2,101,416)
Writedowns	(153,300)	(711,006)
Balance, end of period	$ 7,522,811	$ 6,153,238

The carrying value and estimated fair value of financial assets and financial liabilities, by level within the fair value hierarchy, at June 30, 2012 and December 31, 2011, are as follows:

	Carrying Amount	Fair Value Measurement Using Level 1	Level 2	Level 3	Total
June 30, 2012:					
Financial Assets:					
Cash and due from banks	$ 34,202,485	$ 34,202,485	$	$	$ 34,202,485
Available for sale securities	327,013,590		327,013,590		327,013,590
Held to maturity securities	4,983,923		5,075,817		5,075,817
Other investments	3,893,458	3,893,458			3,893,458
Federal Home Loan Bank stock	4,259,400		4,259,400		4,259,400
Loans, net	420,847,759			422,431,841	422,431,841
Other real estate	7,522,811			7,522,811	7,522,811
Cash surrender value of life insurance	16,513,580			16,513,580	16,513,580
Financial Liabilities:					
Deposits:					
Non-interest bearing	114,738,363	114,738,363			114,738,363
Interest bearing	366,830,140		367,546,286		367,546,286
Federal funds purchased and securities sold under agreements to repurchase	161,987,702	161,987,702			161,987,702
Borrowings from Federal Home Loan Bank	83,017,894		84,912,241		84,912,241
December 31, 2011:					
Financial Assets:					
Cash and due from banks	$ 36,928,657	$ 36,928,657	$	$	$ 36,928,657
Available for sale securities	278,918,481		278,918,481		278,918,481
Held to maturity securities	1,428,887		1,492,374		1,492,374
Other investments	3,930,300	3,930,300			3,930,300
Federal Home Loan Bank stock	2,580,700		2,580,700		2,580,700
Loans, net	424,271,664			427,880,554	427,880,554
Other real estate	6,153,238			6,153,238	6,153,238
Cash surrender value of life insurance	16,196,368			16,196,368	16,196,368
Financial Liabilities:					
Deposits:					
Non-interest bearing	97,581,073	97,581,073			97,581,073
Interest bearing	370,858,009		372,018,592		372,018,592
Federal funds purchased and securities sold under agreements to repurchase	157,600,967	157,600,967			157,600,967
Borrowings from Federal Home Loan Bank	53,323,568		55,013,522		55,013,522

10. Reclassifications:

Certain reclassifications, which had no effect on prior year net income, have been made to prior period statements to conform to current year presentation.

Item 2: Management s Discussion and Analysis of Financial Condition and Results of Operations
GENERAL

The Company is a one-bank holding company headquartered in Biloxi, Mississippi. It has two operating subsidiaries, PFC Service Corp., an inactive company, and The Peoples Bank, Biloxi, Mississippi (the Bank). The Bank provides a full range of banking, financial and trust services to state, county and local government entities and individuals and small and commercial businesses operating in its trade area.

The following presents Management s discussion and analysis of the consolidated financial condition and results of operations of Peoples Financial Corporation and Subsidiaries. These comments should be considered in combination with the Consolidated Financial Statements and Notes to Consolidated Financial Statements included in this report on Form 10-Q and the Consolidated Financial Statements, Notes to Consolidated Financial Statements and Management s Discussion and Analysis included in the Company s Form 10-K for the year ended December 31, 2011.

Forward-Looking Information

Congress passed the Private Securities Litigation Act of 1995 in an effort to encourage corporations to provide information about a company s anticipated future financial performance. This act provides a safe harbor for such disclosure which protects the companies from unwarranted litigation if actual results are different from management expectations. This report contains forward-looking statements and reflects industry conditions, company performance and financial results. These forward-looking statements are subject to a number of factors and uncertainties which could cause the Company s actual results and experience to differ from the anticipated results and expectations expressed in such forward-looking statements. Such factors and uncertainties include, but are not limited to: changes in interest rates and market prices, changes in local economic and business conditions, increased competition for deposits and loans, a deviation in actual experience from the underlying assumptions used to determine and establish the allowance for loan losses, changes in the availability of funds resulting from reduced liquidity, changes in government regulations and acts of terrorism, weather or other events beyond the Company s control.

New Accounting Pronouncements

There were no new accounting standards updates issued during the six months ended June 30, 2012. The Company did implement the disclosure requirements relating to the presentation of comprehensive income as set forth in Accounting Standards Update 2011 5.

Critical Accounting Policies

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America (GAAP) requires Management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. The Company evaluates these estimates and assumptions on an on-going basis using historical experience and other factors, including the current economic environment. We adjust such estimates and assumptions when facts and circumstances dictate. Certain critical accounting policies affect the more significant estimates and assumptions used in the preparation of the consolidated financial statements.

Allowance for loan losses:

The Company s most critical accounting policy relates to its allowance for loan losses (ALL), which reflects the estimated losses resulting from the inability of its borrowers to make loan payments. The ALL is established and maintained at an amount sufficient to cover the estimated loss associated with the loan portfolio of the Company as of the date of determination. Credit losses arise not only from credit risk, but also from other risks inherent in the lending process including, but not limited to, collateral risk, operation risk, concentration risk and economic risk. As such, all related risks of lending are considered when assessing the adequacy of the ALL. On a quarterly basis, Management estimates the probable level of losses to determine whether the allowance is adequate to absorb reasonably foreseeable, anticipated losses in the existing portfolio based on our past loan loss experience, known and inherent risk in the portfolio, adverse situations that may affect the borrowers ability to repay and the estimated value of any underlying collateral and current economic conditions. Management believes that the ALL is adequate and appropriate for all periods presented in these financial statements. If there was a deterioration of any of the factors considered by Management in evaluating the ALL, the estimate of loss would be updated, and additional provisions for loan losses may be required. The analysis divides the portfolio into two segments: a pool analysis of loans based upon a five year average loss history which is updated on a quarterly basis and which may be adjusted by qualitative factors by loan type and a specific reserve analysis for those loans considered impaired under generally accepted accounting principles. All credit relationships with an outstanding balance of $100,000 or greater that are included in Management s loan watch list are individually reviewed for impairment. All losses are charged to the ALL when the loss actually occurs or when a determination is made that a loss is likely to occur; recoveries are credited to the ALL at the time of receipt.

Employee Benefit Plans:

Employee benefit plan liabilities and pension costs are determined utilizing actuarially determined present value calculations. The valuation of the benefit obligation and net periodic expense is considered critical, as it requires Management and its actuaries to make estimates regarding the amount and timing of expected cash outflows including assumptions about mortality, expected service periods and the rate of compensation increases.

Income Taxes:

GAAP requires the asset and liability approach for financial accounting and reporting for deferred income taxes. We use the asset and liability method of accounting for deferred income taxes and provide deferred income taxes for all significant income tax temporary differences. As part of the process of preparing our consolidated financial statements, the Company is required to estimate our income taxes in each of the jurisdictions in which we operate. This process involves estimating our actual current tax exposure together with assessing temporary differences resulting from differing treatment of items, such as the provision for loan losses, for tax and financial reporting purposes.

These differences result in deferred tax assets and liabilities that are included in our consolidated statement of condition. We must also assess the likelihood that our deferred tax assets will be recovered from future taxable income, and to the extent we believe that recovery is not likely, we must establish a valuation allowance. Significant management judgment is required in determining our provision for income taxes, our deferred tax assets and liabilities and any valuation allowance recorded against our net deferred tax assets. To the extent the Company establishes a valuation allowance or adjusts this allowance in a period, we must include an expense within the tax provisions in the statement of income.

OVERVIEW

The Company is a community bank serving the financial and trust needs of its customers in its trade area of south Mississippi, southeast Louisiana and southwest Alabama. Maintaining a strong core deposit base and providing commercial and real estate lending in our trade area are the traditional focuses of the Company. Growth has largely been achieved through de novo branching activity, and it is expected that these strategies will continue to be emphasized in the future.

Net income for the second quarter of 2012 was $561,753 compared with $809,873 for the second quarter of 2011 and for the first half of 2012 was $1,066,509 as compared with $1,247,417 for the first half of 2011. Current year results for the second quarter and first half included a reduction in net interest income, an increase in the provision for loan losses, gains on sales and calls of securities, a decrease in salaries and benefit costs and an increase in data processing expenses as compared with 2011 results. Prior year results included a gain from the redemption of life insurance of $389,119.

Net interest income increased $10,512 for the second quarter of 2012 as compared with the second quarter of 2011 and decreased $262,671 for the first half of 2012 as compared with the first half of 2011. Interest income on loans continues to be negatively impacted by the large balance of the loan portfolio on nonaccrual and the charge off of accrued interest on loans placed on nonaccrual. The yield on U.S. Agencies, our primary investment choice, continues to decline.

Monitoring asset quality, estimating potential losses in our loan portfolio and addressing non-performing loans continue to be emphasized during these difficult economic times. Borrowers ability to repay has been significantly impacted by these conditions, which has resulted in nonaccrual loans totaling $54,968,213 and $57,592,715 at June 30, 2012 and December 31, 2011, respectively. Most of these loans are collateral-dependent, and the Company has rigorously evaluated the value of its collateral to determine potential losses. During the second quarter of 2012, the Company increased the specific reserve on one credit relationship by $800,000 as well as a number of other smaller adjustments in specific reserves to other loans. As a result, the provision for loan losses increased to $1,290,000 for the second quarter of 2012 from $546,000 for the second quarter of 2011 and to $1,830,000 for the first half of 2012 from $1,187,000 for the first half of 2011.

The Company realized gains of $859,942 in the second quarter of 2012 as compared with $7,174 in the second quarter of 2011 and $964,175 in the first half of 2012 as compared with $7,174 in the first half of 2011 from the sale and call of securities. The voluntary early retirement program offered in the fourth quarter of 2011 resulted in a net decrease in salaries and employee benefit costs of $347,414 for the second quarter of 2012 as compared with 2011 and $451,990 for the first half of 2012 as compared with the first half of 2011. In June 2011, the Company outsourced its data processing operations, which resulted in increased costs for the second quarter of 2012 of $216,346 as compared with the second quarter of 2011 and $443,729 for the first half of 2012 as compared with the first half of 2011.

Total assets at June 30, 2012 increased $48,455,504 as compared with December 31, 2011. During the first half of 2012, two public fund relationships increased their balances in a non-deposit product with the Bank by more than $80,000,000. These balances were included in federal funds purchased and securities sold under agreements to repurchase. These proceeds funded the purchase of available for sale securities, which were pledged against these public funds as required by law. While these entities began to reallocate their funds to other institutions during the first quarter of 2012, the securities pledging the accounts were still in place. Funds were borrowed from the Federal Home Loan Bank to fund the decrease in the public fund balances.

RESULTS OF OPERATIONS

Net Interest Income

Net interest income, the amount by which interest income on loans, investments and other interest earning assets exceeds interest expense on deposits and other borrowed funds, is the single largest component of the Company s income. Management s objective is to provide the largest possible amount of income while balancing interest rate, credit, liquidity and capital risk. Changes in the volume and mix of interest earning assets and interest-bearing liabilities combined with changes in market rates of interest directly affect net interest income.

Quarter Ended June 30, 2012 as Compared with Quarter Ended June 30, 2011

The Company s average interest earning assets increased approximately $39,720,000, or 5%, from approximately $734,761,000 for the second quarter of 2011 to approximately $774,481,000 for the second quarter of 2012. The Company s average balance sheet increased as new loans have outpaced principal payments, maturities, charge-offs and foreclosures relating to existing loans.

The average yield on earning assets decreased by 34 basis points, from 3.68% for the second quarter of 2011 to 3.34% for the second quarter of 2012, with the biggest impact to the yield on taxable available for sale securities. The Company s investment and liquidity strategy has been to invest most of the proceeds from sales, calls and maturities of securities in similar securities. As a result, the yield on taxable available for sale securities decreased from 2.40% for the second quarter of 2011 to 1.89% for the second quarter of 2012. The Company has more recently purchased securities with maturities of up to fifteen years, with call provisions, to improve its yield on these assets. Future security purchases may be of shorter duration in anticipation of rising rates in 2014. The yield on loans has decreased due to the increase in loans on nonaccrual during the last quarter of 2011 and the first half of 2012.

Average interest bearing liabilities increased approximately $28,861,000, or 5%, from approximately $602,757,000 for the second quarter of 2011 to approximately $631,618,000 for the second quarter of 2012. The increase was primarily related to borrowing from the Federal Home Loan Bank, which increased due to the liquidity needs of the bank subsidiary.

The average rate paid on interest bearing liabilities decreased 21 basis points, from .57% for the second quarter of 2011 to .36% for the second quarter of 2012. Rates paid on deposit accounts and non-deposit accounts, which are reported as federal funds purchased and securities sold under agreements to repurchase, have decreased in 2012. The current unprecedented low rate environment which exists on a national and local level has caused customers to tolerate lower interest rates in return for less risk. The Company believes that it is unlikely that its cost of funds can be materially reduced further; however, any opportunity to do so will be considered.

The Company s net interest margin on a tax-equivalent basis, which is net income as a percentage of average earning assets, was 3.04% for the quarter ended June 30, 2012, down 16 basis points from 3.20% for the quarter ended June 30, 2011.

Six Months Ended June 30, 2012 as Compared with Six Months Ended June 30, 2011

The Company s average interest earning assets increased approximately $46,977,000, or 7%, from approximately $720,795,000 for the first half of 2011 to approximately $767,772,000 for the first half of 2012. The Company s average loan balance increased as new loans have outpaced principal payments, maturities, charge-offs and foreclosures relating to existing loans.

The average yield on earning assets decreased by 47 basis points, from 3.82% for the first half of 2011 to 3.35% for the first half of 2012, with the biggest impact to the yield on taxable available for sale securities. The Company s investment and liquidity strategy has been to invest most of the proceeds from sales, calls and maturities of securities in similar securities. As a result, the yield on taxable available for sale securities decreased from 2.38% for the first half of 2011 to 1.79% for the first half of 2012. The Company has more recently purchased securities with maturities of up to fifteen years, with call provisions, to improve its yield on these assets. Future security purchases may be of shorter duration in anticipation of rising rates in 2014. The yield on loans has decreased due to the increase in loans on nonaccrual during the last quarter of 2011 and the first half of 2012.

Average interest bearing liabilities increased approximately $39,596,000, or 7%, from approximately $588,905,000 for the first half of 2011 to approximately $628,501,000 for the first half of 2012.

The average rate paid on interest bearing liabilities decreased 23 basis points, from .61% for the first half of 2011 to .38% for the first half of 2012. Rates paid on deposit accounts and non-deposit accounts, which are reported as federal funds purchased and securities sold under agreements to repurchase, have decreased in 2012. The current unprecedented low rate environment which exists on a national and local level has caused customers to tolerate lower interest rates in return for less risk. The Company believes that it is unlikely that its cost of funds can be materially reduced further; however, any opportunity to do so will be considered.

The Company s net interest margin on a tax-equivalent basis, which is net income as a percentage of average earning assets, was 3.04% for the six months ended June 30, 2012, down 27 basis points from 3.31% for the six months ended June 30, 2011.

The tables on the following pages analyze the changes in tax-equivalent net interest income for the quarters ended June 30, 2012 and 2011 and the six months ended June 30, 2012 and 2011.

Analysis of Average Balances, Interest Earned/Paid and Yield

(In Thousands)

	Three Months Ended June 30, 2012			Three Months Ended June 30, 2011		
	Average Balance	Interest Earned/Paid	Rate	Average Balance	Interest Earned/Paid	Rate
Loans (2)(3)	$ 428,951	$ 4,511	4.21%	$ 391,346	$ 4,381	4.48%
Federal Funds Sold	3,841	3	0.31%	2,318	4	0.69%
HTM:						
Non taxable (1)	4,109	43	4.19%	1,916	31	6.47%
AFS:						
Taxable	292,811	1,384	1.89%	295,317	1,770	2.40%
Non taxable (1)	39,914	527	5.28%	40,913	568	5.55%
Other	4,855	1	0.80%	2,951	3	0.41%
Total	$ 774,481	$ 6,469	3.34%	$ 734,761	$ 6,757	3.68%
Savings & interest-bearing DDA	$ 238,344	$ 157	0.26%	$ 249,035	$ 265	0.43%
CD s	148,536	252	0.68%	169,899	386	0.91%
Federal funds purchased	161,933	98	0.24%	147,997	170	0.46%
FHLB advances	82,805	69	0.33%	35,826	45	0.50%
Total	$ 631,618	$ 576	0.36%	$ 602,757	$ 866	0.57%
Net tax-equivalent margin on earning assets			3.04%			3.20%

(1) All interest earned is reported on a taxable equivalent basis using a tax rate of 34% in 2012 and 2011.
(2) Loan fees of $145 and $197 for 2012 and 2011, respectively, are included in these figures.
(3) Includes nonaccrual loans.

Analysis of Average Balances, Interest Earned/Paid and Yield

(In Thousands)

	Six Months Ended June 30, 2012				Six Months Ended June 30, 2011			
	Average Balance	Interest Earned/Paid		Rate	Average Balance	Interest Earned/Paid		Rate
Loans (2)(3)	$ 428,276	$	9,153	4.27%	$ 399,497	$	9,288	4.65%
Federal Funds Sold	6,609		9	0.27%	3,730		5	0.27%
HTM:								
Non taxable (1)	2,944		64	4.35%	1,916		59	6.16%
AFS:								
Taxable	285,818		2,560	1.79%	271,379		3,232	2.38%
Non taxable (1)	40,046		1,056	5.27%	41,266		1,163	5.64%
Other	4,079		5	0.24%	3,007		9	0.60%
Total	$ 767,772	$	12,847	3.35%	$ 720,795	$	13,756	3.82%
Savings & interest-bearing DDA	$ 231,928	$	301	0.26%	$ 233,294	$	525	0.45%
CD s	152,624		543	0.71%	175,304		829	0.95%
Federal funds purchased	177,614		217	0.24%	141,819		342	0.48%
FHLB advances	66,335		119	0.36%	38,488		95	0.49%
Total	$ 628,501	$	1,180	0.38%	$ 588,905	$	1,791	0.61%
Net tax-equivalent margin on earning assets				3.04%				3.31%

(1) All interest earned is reported on a taxable equivalent basis using a tax rate of 34% in 2012 and 2011.
(2) Loan fees of $389 and $363 for 2012 and 2011, respectively, are included in these figures.
(3) Includes nonaccrual loans.

Analysis of Changes in Interest Income and Interest Expense

(In Thousands)

	For the Quarter Ended June 30, 2012 compared with June 30, 2011			
	Volume	Rate	Rate/Volume	Total
Interest earned on:				
Loans	$ 421	$ (266)	$ (25)	$ 130
Federal funds sold	2	(2)	(1)	(1)
Held to maturity securities:				
Non taxable	35	(10)	(13)	12
Available for sale securities:				
Taxable	(15)	(374)	3	(386)
Non taxable	(14)	(28)	1	(41)
Other	2	(2)	(2)	(2)
Total	$ 431	$ (682)	$ (37)	$ (288)
Interest paid on:				
Savings & interest-bearing deposits	$ (11)	$ (101)	$ 4	$ (108)
CD s	(49)	(98)	13	(134)
Federal funds purchased	16	(80)	(8)	(72)
FHLB advances	59	(15)	(20)	24
Total	$ 15	$ (294)	$ (11)	$ (290)

Analysis of Changes in Interest Income and Interest Expense

(In Thousands)

	For the Six Months Ended June 30, 2012 compared with June 30, 2011			
	Volume	Rate	Rate/Volume	Total
Interest earned on:				
Loans	$ 669	$ (750)	$ (54)	$ (135)
Federal funds sold	4	1	(1)	4
Held to maturity securities:				
Non taxable	32	(17)	(10)	5
Available for sale securities:				
Taxable	172	(801)	(43)	(672)
Non taxable	(34)	(75)	2	(107)
Other	3	(5)	(2)	(4)
Total	$ 846	$ (1,647)	$ (108)	$ (909)
Interest paid on:				
Savings & interest-bearing deposits	$ (3)	$ (222)	$ 1	$ (224)
CD s	(107)	(205)	26	(286)
Federal funds purchased	86	(169)	(42)	(125)
FHLB advances	69	(26)	(19)	24
Total	$ 45	$ (622)	$ (34)	$ (611)

Provision for Loan Losses

In the normal course of business, the Company assumes risk in extending credit to its customers. This credit risk is managed through compliance with the loan policy, which is approved by the Board of Directors. The policy establishes guidelines relating to underwriting standards, including but not limited to financial analysis, collateral valuation, lending limits, pricing considerations and loan grading. A loan review process further assists with evaluating credit quality and assessing potential performance issues. Loan delinquencies and deposit overdrafts are closely monitored in order to identify developing problems as early as possible. The Company monitors its relationships with its loan customers in concentrated industries such as gaming and hotel/motel, as well as the exposure for out of area, land, development, construction and commercial real estate loans, and their direct and indirect impact on its operations on a monthly basis. A watch list of credits which pose a potential loss to the Company is prepared based on the loan grading system. This list forms the foundation of the Company s allowance for loan loss computation.

Management relies on its guidelines and existing methodology to monitor the performance of its loan portfolio and identify and estimate potential losses based on the best available information. The potential effect resulting from the economic downturn on a national and local level, the decline in real estate values and actual losses incurred by the Company were key factors in our analysis. Much of the Company s loan portfolio is collateral-dependent, requiring careful consideration of changes in the value of the collateral.

The Company s on-going, systematic evaluation resulted in the Company recording a provision for loan losses of $1,290,000 and $546,000 for the second quarters of 2012 and 2011, respectively, and $1,830,000 and $1,187,000 for the first half of 2012 and 2011, respectively. The allowance for loan losses as a percentage of loans was 1.58% and 1.75% at June 30, 2012 and December 31, 2011, respectively. The Company s evaluation includes evaluating the current values of collateral securing all nonaccrual loans. Even though nonaccrual loans grew to $54,968,213 and $57,592,715 at June 30, 2012 and December 31, 2011, respectively, specific reserves of only $581,054 and $2,106,729, respectively, have been allocated to these loans as collateral values appear sufficient to cover loan losses or the loan balances have been charged down to their realizable value. The Company believes that its allowance for loan losses is appropriate as of June 30, 2012.

The allowance for loan losses is an estimate, and as such, events may occur in the future which may affect its accuracy. The Company anticipates that it is possible that additional information will be gathered in future quarters which may require an adjustment to the allowance for loan losses. Management will continue to closely monitor its portfolio and take such action as it deems appropriate to accurately report its financial condition and results of operations.

Non-interest income

Non-interest income increased $446,320 for the second quarter of 2012 as compared with the second quarter of 2011. During the second quarter of 2012, gains from sales and calls of securities increased $852,768 in comparison with the second quarter of 2011 as sales were executed when proceeds would be maximized. Gains from the redemption of life insurance were $389,119 for the second quarter of 2011.

Non-interest income increased $543,103 for the first half of 2012 as compared with the first half of 2011. During the first half of 2012, gains from sales and calls of securities increased $957,001 in comparison with the first half of 2011 as sales were executed when proceeds would be maximized. Gains from the redemption of life insurance were $389,119 for the first half of 2011. The Company experienced a loss on its investment in a low income housing partnership and other equity investments of $36,843 in 2012 as compared with a gain of $10,124 in 2011.

Non-interest expense

Total non-interest expense decreased $174,048 for the second quarter of 2012 as compared with the second quarter of 2011. Salaries and employee benefits decreased $347,414; equipment rentals, depreciation and maintenance decreased $74,851; data processing expenses increased $216,346 and other expenses increased $50,431 for the second quarter of 2012 as compared with the second quarter of 2011.

Salaries decreased $159,273 in the second quarter of 2012 as compared with the second quarter of 2011 as the employee census continues to decrease from attrition and the impact of the 2011 voluntary early retirement package. Expenses relating to the retiree health plan decreased $110,085 as a result of amendments made to the plan which require plan participants to utilize drug benefits and health insurance coverage available under Medicare. Costs associated with the Company s deferred compensation plans decreased $40,353 due to the 2011 voluntary early retirement package.

Equipment maintenance and servicing increased $25,543 in 2012 due to the timing of payment for these services. Depreciation costs have decreased by $103,500 in 2012, as computer and other equipment acquired after Hurricane Katrina in 2005 are now fully depreciated.

Data processing costs increased in 2012 as a result of the outsourcing of these activities during the second quarter of 2011.

Included in other expense are expenses relating to the ORE portfolio which increased $106,085 in 2012 a result of the write down of several of these properties to their fair value, less estimated cost to sell. The remaining net increase in other expense is primarily due to the timing of payments for various services.

Total non-interest expense decreased $377,660 for the first half of 2012 as compared with the first half of 2011. Salaries and employee benefits decreased $451,990; equipment rentals, depreciation and maintenance decreased $168,136; data processing expenses increased $443,729 and other expenses decreased $217,393 for the first half of 2012 as compared with the first half of 2011.

Salaries decreased $332,729 in the first half of 2012 as compared with the first half of 2011 as the employee census continues to decrease from attrition and the impact of the 2011 voluntary early retirement package. Expenses relating to the retiree health plan decreased $186,127 as a result of amendments made to the plan which require plan participants to utilize drug benefits and health insurance coverage available under Medicare. Costs associated with the Company s deferred compensation plans increased $96,593 due to the 2011 voluntary early retirement package.

Equipment maintenance and servicing decreased $55,861 in 2012 due to the timing of payment for these services. Depreciation costs have decreased by $139,500 in 2012, as computer and other equipment acquired after Hurricane Katrina in 2005 are now fully depreciated.

Data processing costs increased in 2012 as a result of the outsourcing of these activities during the second quarter of 2011.

Included in other expense are expenses relating to the ORE portfolio which increased $46,024 in 2012 a result of the write down of several of these properties to their fair value, less estimated cost to sell. The remaining net increase in other expense is primarily due to the timing of payments for various services.

Income Tax Benefit

Income taxes have been impacted by non-taxable income and federal tax credits during the quarters and six months ended June 30, 2012 and 2011, as follows:

	Quarters Ended June 30,			
	2012		2011	
	Tax	Rate	Tax	Rate
Taxes at statutory rate	$ 171,616	34	$ 210,077	34
Increase (decrease) resulting from:				
Tax-exempt interest income	(95,463)	(19)	(137,935)	(23)
Income from BOLI	(42,596)	(8)	(174,930)	(28)
Federal tax credits	(91,410)	(18)	(91,410)	(15)
Other	853	1	2,198	1
Total income taxes (benefit)	$ (57,000)	(10)	$ (192,000)	(31)

	Six Months Ended June 30,			
	2012		2011	
	Tax	Rate	Tax	Rate
Taxes at statutory rate	$ 312,633	34	$ 307,842	34
Increase (decrease) resulting from:				
Tax-exempt interest income	(200,504)	(22)	(263,429)	(29)
Income from BOLI	(83,869)	(9)	(219,912)	(24)
Federal tax credits	(182,820)	(20)	(182,820)	(20)
Other	7,560	1	16,319	1
Total income taxes (benefit)	$ (147,000)	(16)	$ (342,000)	(38)

FINANCIAL CONDITION

Available for sale securities increased $48,095,109 at June 30, 2012, compared with December 31, 2011, as a large increase in funds in a non-deposit product during the first quarter were invested in these securities.

Held to maturity securities increased $3,555,036 at June 30, 2012, compared with December 31, 2011, as the Company opted to classify some of its investment purchases during the second quarter as held to maturity.

The investment in Federal Home Loan Bank (FHLB) stock increased $1,678,700 at June 30, 2012 as compared with December 31, 2011 so that the Company could increase its borrowing capacity from the FHLB during the period.

Loans decreased $4,816,279 at June 30, 2012 as compared with December 31, 2011 as the result of charge-offs of $3,293,002 and transfers to Other Real Estate of $1,891,673.

Other real estate (ORE) increased $1,369,573 at June 30, 2012 as compared with December 31, 2011. Loans totaling $1,891,673 were transferred into ORE while $368,800 was sold for a loss of $24,739 and write downs of ORE to fair value of $153,300 were recorded during the first six months of 2012.

Prepaid FDIC assessments decreased by $817,331 at June 30, 2012 as compared with December 31, 2011 as a result of the amortization of these costs.

Other assets increased $1,052,335 at June 30, 2012 as compared with December 31, 2011 primarily as income taxes receivable increased $715,000 due to overpayments during 2011.

Total deposits increased $13,129,421 at June 30, 2012, as compared with December 31, 2011. Typically, significant increases or decreases in total deposits and/or significant fluctuations among the different types of deposits from quarter to quarter are anticipated by Management as customers in the casino industry and county and municipal entities reallocate their resources periodically.

Federal funds purchased and securities sold under agreements to repurchase increased $4,386,735 at June 30, 2012 as compared with December 31, 2011 as several county and municipal entities increased their balances in a non-deposit account during the first half of 2012.

Borrowings from the FHLB increased $29,694,326 at June 30, 2012 as compared with December 31, 2011 based on the liquidity needs of the bank subsidiary.

Employee and director benefit plans liabilities increased $648,486 at June 30, 2012 as compared with December 31, 2011 due to the deferred compensation benefits earned by officers and directors during 2012.

Other liabilities decreased $679,207 at June 30, 2012 as compared with December 31, 2011 as a result of the payment of officer incentives and director fees which has been accrued at December 31, 2011.

SHAREHOLDERS EQUITY AND CAPITAL ADEQUACY

Strength, security and stability have been the hallmark of the Company since its founding in 1985 and of its bank subsidiary since its founding in 1896. A strong capital foundation is fundamental to the continuing prosperity of the Company and the security of its customers and shareholders.

The Company and the Bank are subject to regulatory capital adequacy requirements imposed by the federal banking agencies. Under capital adequacy guidelines and the regulatory framework for prompt corrective action, specific capital guidelines that involve quantitative measures of the bank subsidiary s assets and certain off-balance sheet items, adjusted for credit risk, as calculated under regulatory accounting practices must be met. The risk-based capital standards currently in effect are designed to make regulatory capital requirements more sensitive to differences in risk profiles among bank holding companies and banks and to account for off-balance sheet exposure. Quantitative measures established by regulation to ensure capital adequacy require the Company and Bank to maintain minimum amounts and ratios of Total and Tier 1 capital to risk-weighted assets, and Tier 1 capital to average assets.

As of June 30, 2012, the most recent notification from the Federal Deposit Insurance Corporation categorized the bank subsidiary as well capitalized under the regulatory framework for prompt corrective action. To be categorized as well capitalized, the bank subsidiary must have a Total risk-based capital ratio of 10.00% or greater, a Tier 1 risk-based capital ratio of 6.00% or greater and a Leverage capital ratio of 5.00% or greater. There are no conditions or events since that notification that Management believes have changed the bank subsidiary s category.

The actual capital amounts and ratios and required minimum capital amounts and ratios for the Company as of June 30, 2012 and December 31, 2011, are as follows (in thousands):

	Actual		For Capital Adequacy Purposes	
	Amount	Ratio	Amount	Ratio
June 30, 2012:				
Total Capital (to Risk Weighted Assets)	$ 111,924	20.60%	$ 43,466	8.00%
Tier 1 Capital (to Risk Weighted Assets)	105,181	19.36%	21,733	4.00%
Tier 1 Capital (to Average Assets)	105,181	12.00%	35,046	4.00%
December 31, 2011:				
Total Capital (to Risk Weighted Assets)	$ 110,762	20.86%	$ 42,475	8.00%
Tier 1 Capital (to Risk Weighted Assets)	104,116	19.61%	21,238	4.00%
Tier 1 Capital (to Average Assets)	104,116	12.84%	32,436	4.00%

The actual capital amounts and ratios and required minimum capital amounts and ratios for the Bank as of June 30, 2012 and December 31, 2011, are as follows (in thousands):

	Acutal		For Capital Adequacy Purposes		To Be Well Capitalized	
	Amount	Ratio	Amount	Ratio	Amount	Ratio
June 30, 2012:						
Total Capital (to Risk Weighted Assets)	$ 109,090	21.15%	$ 41,262	8.00%	$ 51,578	10.00%
Tier 1 Capital (to Risk Weighted Assets)	102,639	19.90%	20,631	4.00%	30,947	6.00%
Tier 1 Capital (to Average Assets)	102,639	12.03%	34,121	4.00%	42,652	5.00%
December 31, 2011:						
Total Capital (to Risk Weighted Assets)	$ 108,149	20.40%	$ 42,413	8.00%	$ 53,014	10.00%
Tier 1 Capital (to Risk Weighted Assets)	101,503	19.15%	21,207	4.00%	31,809	6.00%
Tier 1 Capital (to Average Assets)	101,503	12.56%	32,332	4.00%	40,407	5.00%

In addition to monitoring its risk-based capital ratios, the Company also determines the primary capital ratio on a quarterly basis. This ratio was 14.05% at June 30, 2012, which is well above the regulatory minimum of 6.00%. Management continues to emphasize the importance of maintaining the appropriate capital levels of the Company and has established the goal of maintaining its primary capital ratio at 8.00%, which is the minimum requirement for classification as being well-capitalized by the banking regulatory authorities.

LIQUIDITY

Liquidity represents the Company s ability to adequately provide funds to satisfy demands from depositors, borrowers and other commitments by either converting assets to cash or accessing new or existing sources of funds. Management monitors these funds requirements in such a manner as to satisfy these demands and provide the maximum earnings on its earning assets. The Company manages and monitors its liquidity position through a number of methods, including through the computation of liquidity risk targets and the preparation of various analyses of its funding sources and utilization of those sources on a monthly basis. The Company also uses proforma liquidity projections which are updated on a monthly basis in the management of its liquidity needs and also conducts periodic contingency testing on its liquidity plan.

Deposits, payments of principal and interest on loans, proceeds from maturities of investment securities and earnings on investment securities are the principal sources of funds for the Company. Borrowings from the FHLB, federal funds sold and federal funds purchased are utilized by the Company to manage its daily liquidity position. The Company has also been approved to participate in the Federal Reserve Bank s Discount Window Primary Credit Program, which it intends to use only as a contingency.

REGULATORY MATTERS

During 2009, Management identified opportunities for improving risk management, addressing asset quality concerns, managing concentrations of credit risk and ensuring sufficient liquidity at the Bank as a result of its own investigation as well as examinations performed by certain bank regulatory agencies. In concert with the regulators, the Company and the Bank identified specific corrective steps and actions to enhance its risk management, asset quality and liquidity policies, controls and procedures. The Company and the Bank may not declare or pay any cash dividends without the prior written approval of their regulators.

Item 4: Controls and Procedures

As of June 30, 2012, an evaluation was performed under the supervision and with the participation of the Chief Executive Officer and Chief Financial Officer of the effectiveness of the Company s disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e)). Based on that evaluation, the Chief Executive Officer and the Chief Financial Officer have concluded that the Company s disclosure controls and procedures are effective to ensure that the information required to be disclosed by the Company in the reports it files or submits under the Securities Exchange Act of 1934 is recorded, processed, summarized and reported, within the time periods specified in the Securities and Exchange Commission s rules and forms.

There were no changes in the Company s internal control over financial reporting that occurred during the period ended June 30, 2012 that have materially affected, or are reasonably likely to materially affect, the Company s internal control over financial reporting.

PART II OTHER INFORMATION

Item 1: Legal Proceedings

The Bank is involved in various legal matters and claims which are being defended and handled in the ordinary course of business. None of these matters is expected, in the opinion of Management, to have a material adverse effect upon the financial position or results of operations of the Company.

Item 5: Other Information

None.

Item 6 Exhibits and Reports on Form 8-K

(a) Exhibits

Exhibit 31.1:	Certification of Chief Executive Officer Pursuant to Section 302 of the Sarbanes - Oxley Act of 2002
Exhibit 31.2:	Certification of Chief Financial Officer Pursuant to Section 302 of the Sarbanes - Oxley Act of 2002
Exhibit 32.1:	Certification of Chief Executive Officer Pursuant to 18 U.S.C. ss. 1350
Exhibit 32.2:	Certification of Chief Financial Officer Pursuant to 18 U.S.C. ss. 1350
Exhibit 101	The following materials from the Company s quarterly report on Form 10-Q for the quarter ended June 30, 2012, formatted in XBRL (Extensible Business Reporting Language): (i) Consolidated Statements of Condition at June 30, 2012 and December 31, 2011, (ii)Consolidated Statements of Income for the quarters and six months ended June 30, 2012 and 2011, (iii) Consolidated Statements of Comprehensive Income for the quarters and six months ended June 30, 2012 and 2011, (iv) Statement of Changes in Shareholders Equity for the six months ended June 30, 2012, (v) Consolidated Statements of Cash Flows for the six months ended June 30, 2012 and 2011 and (vi) Notes to the Unaudited Consolidated Financial Statements for the six months ended June 30, 2012 and 2011.

(b) Reports on Form 8-K
A Form 8-K was filed on April 25, 2012, April 27, 2012, July 25, 2012 and July 27, 2012.

SIGNATURES

Pursuant to the requirement of Section 13 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.

PEOPLES FINANCIAL CORPORATION

(Registrant)

Date: August 13, 2012

By: /s/ Chevis C. Swetman
Chevis C. Swetman

Chairman, President and Chief Executive Officer

(principal executive officer)

Date: August 13, 2012

By: /s/ Lauri A. Wood
Lauri A. Wood

Chief Financial Officer and Controller

(principal financial and accounting officer)