PEOPLES FINANCIAL CORP /MS/
Form 10-Q
May 09, 2007

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SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549
FORM 10-Q

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

For the quarterly period ended March 31, 2007

or

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

Commission File Number 0-30050

PEOPLES FINANCIAL CORPORATION

(Exact name of registrant as specified in its charter)

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

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

Large accelerated filer o Accelerated filer þ Non-accelerated filer o

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

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 April 30, 2007, there were 15,000,000 shares of $1 par value common stock authorized, and 5,548,199 shares issued and outstanding.

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PART I
FINANCIAL INFORMATION
PEOPLES FINANCIAL CORPORATION AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF CONDITION

March 31, December 31, and March 31,	(Unaudited) 2007	(Audited) 2006	(Unaudited) 2006
Assets			
Cash and due from banks	$ 40,476,666	$ 37,793,493	$ 64,765,168
Federal funds sold	4,440,000	6,400,000	23,870,000
Held to maturity securities, market value of $43,798,000 - March 31, 2007; $85,519,000 - December 31, 2006; $209,672,000 - March 31, 2006	43,822,161	85,574,260	209,973,869
Available for sale securities, at market value	438,434,671	397,207,489	204,959,326
Federal Home Loan Bank stock, at cost	1,143,200	1,128,500	1,089,800
Loans	422,702,259	401,194,010	354,706,547
Less: Allowance for loan losses	10,854,058	10,841,367	10,975,126
Loans, net	411,848,201	390,352,643	343,731,421
Bank premises and equipment, net of accumulated depreciation	20,961,878	19,658,585	19,453,383
Accrued interest receivable	7,547,823	8,142,230	4,358,496
Other assets	18,087,037	17,765,868	19,073,435
Total assets	$ 986,761,637	$ 964,023,068	$ 891,274,898

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PEOPLES FINANCIAL CORPORATION AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF CONDITION (Continued)

March 31, December 31, and March 31,	(Unaudited) 2007	(Audited) 2006	(Unaudited) 2006
Liabilities & Shareholders Equity			
Liabilities:			
Deposits:			
Demand, non-interest bearing	$ 148,453,991	$ 148,455,754	$ 181,777,595
Savings and demand, interest bearing	277,213,793	271,331,272	319,689,203
Time, $100,000 or more	137,112,142	132,846,509	62,405,284
Other time deposits	59,685,277	60,536,259	65,540,357
Total deposits	622,465,203	613,169,794	629,412,439
Federal funds purchased and securities sold under agreements to repurchase	238,264,001	226,032,370	155,434,163
Borrowings from Federal Home Loan Bank	7,224,546	7,267,349	7,310,139
Other liabilities	17,648,310	19,320,860	9,314,809
Total liabilities	885,602,060	865,790,373	801,471,550
Shareholders Equity:			
Common Stock, $1 par value, 15,000,000 shares authorized, 5,548,199, 5,548,199 and 5,548,399 shares issued and outstanding at March 31, 2007, December 31, 2006 and March 31, 2006, respectively	5,548,199	5,548,199	5,548,399
Surplus	65,780,254	65,780,254	65,780,254
Undivided profits	31,969,148	29,253,825	21,464,032
Accumulated other comprehensive income	(2,138,024)	(2,349,583)	(2,989,337)
Total shareholders equity	101,159,577	98,232,695	89,803,348

Total liabilities and shareholders equity	$ 986,761,637	$ 964,023,068	$ 891,274,898

See Selected Notes to Consolidated Financial Statements.

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PEOPLES FINANCIAL CORPORATION AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF INCOME
(Unaudited)

For the Quarter Ended March 31,	2007	2006
Interest income:		
Interest and fees on loans	$ 7,789,889	$ 6,183,077
Interest and dividends on investments:		
U. S. Treasury	1,315,311	1,828,082
U. S. Government agencies and corporations	4,271,533	1,758,533
States and political subdivisions	223,162	208,601
Other investments	143,548	85,974
Interest on federal funds sold	51,109	440,490
Total interest income	13,794,552	10,504,757
Interest expense:		
Deposits	3,526,334	2,218,270
Borrowings from Federal Home Loan Bank	114,543	115,866
Federal funds purchased and securities sold under agreements to repurchase	2,725,052	663,245
Total interest expense	6,365,929	2,997,381
Net interest income	7,428,623	7,507,376
Provision for losses on loans	49,000	35,000
Net interest income after provision for losses on loans	$ 7,379,623	$ 7,472,376

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PEOPLES FINANCIAL CORPORATION AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF INCOME (Continued)
(Unaudited)

For the Quarter Ended March 31,	2007	2006
Other operating income:		
Trust department income and fees	$ 448,620	$ 356,017
Service charges on deposit accounts	1,671,861	1,060,487
Other service charges, commissions and fees	57,530	74,507
Other income	471,960	179,529
Total other operating income	2,649,971	1,670,540
Other operating expense:		
Salaries and employee benefits	3,387,175	3,033,019
Net occupancy	377,705	343,002
Equipment rentals, depreciation and maintenance	783,670	661,205
Other expense	1,477,721	1,282,240
Total other operating expense	6,026,271	5,319,466
Income before income taxes	4,003,323	3,823,450
Income taxes	1,288,000	1,290,000
Net income	$ 2,715,323	$ 2,533,450
Basic and diluted earnings per share	$ .49	$ .46

See Selected Notes to Consolidated Financial Statements.

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PEOPLES FINANCIAL CORPORATION AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF SHAREHOLDERS EQUITY

	# of Common Shares	Common Stock	Surplus	Undivided Profits	Accumu -lated Other Compre -hensive Income	Compre -hensive Income	Total
Balance, January 1, 2006	5,549,128	$ 5,549,128	$ 65,780,254	$ 18,942,855	$ (2,769,106)		$ 87,503,131
Comprehensive Income:							
Net income				2,533,450		$ 2,533,450	2,533,450
Net unrealized loss on available for sale securities, net of tax					(220,231)	(220,231)	(220,231)
Total comprehensive income						$ 2,313,219	
Retirement of common stock	(729)	(729)		(12,273)			(13,002)
Balance, March 31, 2006	5,548,399	$ 5,548,399	$ 65,780,254	$ 21,464,032	$ (2,989,337)		$ 89,803,348

Note: Balances as of January 1, 2006 were audited.

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PEOPLES FINANCIAL CORPORATION AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF SHAREHOLDERS EQUITY (Continued)

	# of Common Shares	Common Stock	Surplus	Undivided Profits	Accumulated Other Comprehensive Income	Comprehensive Income	Total
Balance, January 1, 2007	5,548,199	$ 5,548,199	$ 65,780,254	$ 29,253,825	$ (2,349,583)		$ 98,232,695
Comprehensive Income:							
Net income				2,715,323		$ 2,715,323	2,715,323
Net unrealized gain on available for sale securities, net of tax					199,490	199,490	199,490
Reclassification adjustment for available for sale securities called or sold in current year, net of tax					12,069	12,069	12,069
Total comprehensive income						$ 2,926,882	
Balance, March 31, 2007	5,548,199	$ 5,548,199	$ 65,780,254	$ 31,969,148	$ (2,138,024)		$ 101,159,577

Note: Balances as of January 1, 2007 were audited.
See Selected Notes to Consolidated Financial Statements.

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PEOPLES FINANCIAL CORPORATION AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF CASH FLOWS
(Unaudited)

For the Quarter Ended March 31,	2007	2006
Cash flows from operating activities:		
Net income	$ 2,715,323	$ 2,533,450
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation	435,000	369,000
Provision for losses on loans	49,000	35,000
Gain on sale of Other Real Estate	(10,470)	
Loss on sales, calls and liquidation of securities	15,993	
Changes in assets and liabilities:		
Accrued interest receivable	594,407	(43,138)
Other assets	(319,586)	(241,443)
Other liabilities	(400,414)	1,439,831
Net cash provided by operating activities	3,079,253	4,092,700
Cash flows from investing activities:		
Proceeds from maturities and calls of held to maturity securities	47,090,000	62,000,000
Proceeds from maturities, sales and calls of available for sale securities	43,077,975	3,100,292
Purchases of investments in held to maturity securities	(5,337,901)	(137,926,910)
Purchases of investments in available for sale securities	(83,995,457)	(29,999,197)
Purchases of investments in Federal Home Loan Bank	(14,700)	(13,200)
Proceeds from sales of other real estate	55,000	6,000
Loans, net increase	(21,544,558)	(5,386,103)

Acquisition of premises and equipment	(1,738,294)	(1,934,476)
Other assets	(156,296)	(118,278)
Net cash used in investing activities	$ (22,564,231)	$ (110,271,872)

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PEOPLES FINANCIAL CORPORATION AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF CASH FLOWS (Continued)
(Unaudited)

For the Quarter Ended March 31,	2007	2006
Cash flows from financing activities:		
Demand and savings deposits, net increase	$ 5,880,758	$ 23,786,863
Time deposits, net increase	3,414,651	13,408,234
Borrowings from Federal Home Loan Bank	4,150,000	4,600,000
Repayments to Federal Home Loan Bank	(4,192,803)	(4,641,866)
Retirement of common stock		(13,002)
Cash dividends	(1,276,086)	(1,109,826)
Federal funds purchased and securities sold under agreements to repurchase, net increase	12,231,631	6,166,413
Net cash provided by financing activities	20,208,151	42,196,816
Net increase (decrease) in cash and cash equivalents	723,173	(63,982,356)
Cash and cash equivalents, beginning of period	44,193,493	152,617,524
Cash and cash equivalents, end of period	$ 44,916,666	$ 88,635,168

See Selected Notes to Consolidated Financial Statements.

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PEOPLES FINANCIAL CORPORATION AND SUBSIDIARIES
SELECTED NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
For the Quarters Ended March 31, 2007 and 2006

1. Basis of Presentation:

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, the financial position of the Company and its subsidiaries as of March 31, 2007 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 2006 Annual Report.

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

The results of operations for the quarter ended March 31, 2007, are not necessarily indicative of the results to be expected for the full year.

2. Earnings Per Share:

Per share data is based on the weighted average shares of common stock outstanding of 5,548,199 and 5,548,609 for the quarters ended March 31, 2007 and 2006, respectively.

3. Statements of Cash Flows:

The Company has defined cash and cash equivalents to include cash and due from banks and federal funds sold. The Company paid $6,428,000 and $2,747,000 for the quarters ended March 31, 2007 and 2006, respectively, and $18,445,000 for the year ended December 31, 2006, for interest on deposits and borrowings. Income tax payments of $509,000 were made during the quarter ended March 31, 2007 and $5,310,000 for the year ended December 31, 2006. There were no loans transferred to other real estate during the quarters ended March 31, 2007 and 2006 and loans transferred to other real estate were $144,000 for the year ended December 31, 2006.

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4. Investments:

Securities with gross unrealized losses at March 31, 2007 and 2006, aggregated by investment category and length of time that individual securities have been in a continuous loss position are as follows (in 000 s):

	Less Than Twelve Months		Over Twelve Months		Total	
March 31, 2007:	Fair Value	Gross Unrealized Loss	Fair Value	Gross Unrealized Loss	Fair Value	Gross Unrealized Loss
U. S. Treasury	$ 28,794	$ 30	$ 31,719	$ 259	$ 60,513	$ 289
U. S. Govt. Agencies	99,887	280	117,020	1,463	216,907	1,743
States and political subdivisions	3,780	41	8,028	177	11,808	218
Mortgage backed securities	9,735	44			9,735	44
FHLMC preferred stock			2,459	616	2,459	616
Total	$ 142,196	$ 395	$ 159,226	$ 2,515	$ 301,422	$ 2,910

	Less Than Twelve Months		Over Twelve Months		Total	
March 31, 2006:	Fair Value	Gross Unrealized Loss	Fair Value	Gross Unrealized Loss	Fair Value	Gross Unrealized Loss
U. S. Treasury	$ 157,410	$ 382	$ 22,564	$ 413	$ 179,974	$ 795
U. S. Govt. Agencies	127,089	887	75,191	2,286	202,280	3,173
States and political subdivisions	6,297	64	5,717	219	12,014	283
FHLMC preferred stock			2,276	799	2,276	799
Total	$ 290,796	$ 1,333	$ 105,748	$ 3,717	$ 396,544	$ 5,050

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Management evaluates securities for other-than-temporary impairment on a monthly basis. Consideration is given to 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, the cause of the decline in value, the intent and ability of the Company to hold these securities until maturity and that the Company has traditionally held virtually all of its securities, including those classified as available for sale, until maturity. Any sales of available for sale securities, which have been infrequent and immaterial, have been for liquidity purposes. As a result of this evaluation, the Company has determined that the declines summarized in the table above are not deemed to be other-than-temporary.

5. Past Due and Impaired Loans:

Loans past due ninety days or more and still accruing were $3,205,000 and $1,882,000 at March 31, 2007 and 2006, respectively. Nonaccrual loans amounted to approximately $2,268,000 and $410,000 at March 31, 2007 and 2006, respectively.

At March 31, 2007 and 2006, the Company s other individually evaluated impaired loans included performing loans and totaled $11,217,000 and $15,448,000. The average recorded investment in impaired loans amounted to approximately $13,562,000 and $16,765,000 at March 31, 2007 and 2006, respectively. The Company had $5,219,000 and $5,788,000 of specific allowance related to impaired loans at March 31, 2007 and 2006, respectively. Interest income recognized on impaired loans was $251,000 and $313,000 during the quarters ended March 31, 2007 and 2006, respectively. Interest income recognized on impaired loans if the Company had used the cash-basis method of accounting would have approximated $161,000 and $341,000 during the quarters ended March 31, 2007 and 2006, respectively.

6. Allowance for Loan Losses:

Transactions in the allowance for loan losses were as follows:

	For the Quarter Ended March 31, 2007	For the Year Ended December 31, 2006	For the Quarter Ended March 31, 2006
Balance, beginning of period	$ 10,841,367	$ 10,966,022	$ 10,966,022
Provision for loan losses	49,000	141,000	35,000
Recoveries	64,159	463,345	122,250
Loans charged off	(100,468)	(729,000)	(148,146)
Balance, end of period	$ 10,854,058	$ 10,841,367	$ 10,975,126

7. Other Comprehensive Income:

The income tax effect on the accumulated other comprehensive income was $109,000 and ($113,000) at March 31, 2007 and 2006, respectively.

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8. Federal Funds Purchased and Securities Sold Under Agreements to Repurchase:
On April 25, 2007, the Board of Directors authorized the Company to establish an additional $10,000,000 unsecured line of credit. As a result, the Company now has facilities in place to purchase federal funds up to $98,000,000 under established credit arrangements in order to meet its liquidity needs.

9. Income Taxes:
The Financial Accounting Standards Board (the FASB) issued FASB Interpretation No. 48, Accounting for Uncertainty in Income Taxes An Interpretation of FASB Statement No. 109 (FIN 48). This interpretation clarifies the accounting and disclosure for uncertainty in income tax positions and is effective for the Company for the year beginning January 1, 2007. The Company has considered the recognition and measurement requirements of FIN 48 of the benefits recorded in its financial statements for tax positions taken or expected to be taken in its tax returns. Based on its evaluation of these tax positions for open tax years 2003 2006, the unrecognized tax benefit, including applicable interest and penalties, is not material to the financial position of the Company as of January 1, 2007.

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.

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

The following presents Management s discussion and analysis of the consolidated financial condition and results of operations of Peoples Financial Corporation and Subsidiaries (the Company) for the quarters ended March 31, 2007 and 2006. These comments highlight the significant events and should be considered in combination with the Consolidated Financial Statements included in this report on Form 10-Q.

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.

Overview

Net income for the first quarter of 2007 was $2,715,000 as compared with $2,533,000 for the first quarter of 2006. This positive result was primarily due to the increase in ATM and NSF fee income during 2007 as compared with 2006. Net interest income decreased from $7,507,000 for the first quarter of 2006 to $7,429,000 for the first quarter of 2007 as a result of the increase in the cost of funds exceeding the increase in interest income.

Total assets reached $987,000,000 at March 31, 2007 as compared with $891,000,000 at March 31, 2006. Strong deposit and non-deposit growth during the last year continues to fund loan demand with excess funds invested in U.S. Government and Agency securities.

Below are the financial highlights for the quarters ended March 31, 2007 and 2006:

For the quarters ended March 31,	2007	2006
Net income per share	$ .49	$ .46
Book value per share	$ 18.23	$ 16.19
Return on average total assets	1.10%	1.15%
Return on average shareholders equity	10.89%	8.85%
Allowance for loan losses as a % of loans, net of unearned discount	2.57%	3.09%

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Financial Condition

Held to Maturity Securities

Held to maturity securities decreased $166,152,000 at March 31, 2007, compared with March 31, 2006. The significant increase in the balances of deposits and non-deposits product after Hurricane Katrina in August 2005 outpaced loan demand during the last eighteen months. These funds were initially invested in short term U. S. Treasury securities and classified as held to maturity. Proceeds from the maturity of these investments are now primarily funding the purchase of U. S. Agency securities with longer maturities and which are being classified as available for sale. The Company continues to monitor its investment in bonds issued by municipalities which have been affected by Hurricane Katrina. At March 31, 2007, Management has determined that no provision for loss on these investments is required.

Gross unrealized gains for held to maturity securities were $49,000 and $78,000 at March 31, 2007 and 2006, respectively. Gross unrealized losses for held to maturity securities were $73,000 and $380,000 at March 31, 2007 and 2006, respectively. The following schedule reflects the mix of the held to maturity investment portfolio at March 31, 2007 and 2006:

March 31,	2007 Amount	%	2006 Amount	%
U. S. Treasury	$ 4,997,361	11%	$ 134,819,398	64%
U. S. Government agencies	10,000,000	23%	69,000,000	33%
State and political subdivisions	28,824,800	66%	6,154,471	3%
Totals	$ 43,822,161	100%	$ 209,973,869	100%

Available for Sale Securities

Available for sale securities increased $233,475,000 at March 31, 2007, compared with March 31, 2006, in the management of the Company s liquidity position as discussed above. The Company continues to monitor its investment in bonds issued by municipalities which have been affected by Hurricane Katrina. At March 31, 2007, Management has determined that no provision for loss on these investments is required.

Gross unrealized gains were $743,000 and $140,000 and gross unrealized losses were $2,836,000 and $4,670,000 at March 31, 2007 and 2006, respectively. The schedule on page 16 reflects the mix of available for sale securities at March 31, 2007 and 2006:

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March 31,	2007 Amount	%	2006 Amount	%
U. S. Treasury	$ 82,883,488	19%	$ 47,320,217	23%
U. S. Government agencies	322,783,121	74%	140,451,521	69%
State and political subdivisions	18,758,816	4%	14,095,381	7%
Mortgage back securities	9,734,834	2%		
Other securities	4,274,412	1%	3,092,207	1%
Totals	$ 438,434,671	100%	$ 204,959,326	100%

Loans

Loans increased $67,996,000 at March 31, 2007, as compared with March 31, 2006. Minimal loan growth can be attributed to the on-going recovery of the Mississippi Gulf Coast since Hurricane Katrina in August 2005. The Company has supplemented its loan portfolio with out of area and syndicated national casino credits as loan demand fluctuates in its trade area. With the large increase in deposits since Hurricane Katrina far exceeding local loan demand, out of area loans and syndicated national casino loans have been more aggressively pursued and such loans increased $14,000,000 and $21,000,000, respectively, at March 31, 2007 as compared with March 31, 2006.

Bank Premises and Equipment

Bank premises and equipment increased $1,508,000 at March 31, 2007, as compared with March 31, 2006, primarily as a result of construction projects including the expansion at the Main Office and renovations at our Orange Grove Branch.

Accrued Interest Receivable

Accrued interest receivable increased $3,189,000 at March 31, 2007 as compared with March 31, 2006 due to an increase in interest earning assets and the rates earned on those assets.

Other Assets

Other assets decreased $986,000 at March 31, 2007, as compared with March 31, 2006 due to deferred taxes on deferred gains on the sale and retirement of bank premises during the last quarter of 2006.

Deposits

Total deposits decreased $6,947,000 at March 31, 2007, as compared with March 31, 2006. 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 gaming/casino industry and county and municipal areas reallocate their resources periodically. Since Hurricane Katrina in August 2005, the Company has realized a significant increase in demand

and savings deposits and jumbo CD s as municipal customers receive federal and state funding and commercial and personal customers receive insurance proceeds, SBA loans, block grants and other forms of assistance. Based on previous post-hurricane experience and expectations with respect to the time frame for reconstruction, the Company anticipates that deposits will continue at or near their present level throughout the remaining quarters of 2007.

The Company has managed its funds including structuring the maturity of investment securities and the classification of investments as well as utilizing other funding sources and structuring their maturity to manage the potential volatility of its deposits.

Federal Funds Purchased and Securities Sold Under Agreements to Repurchase

Federal funds purchased and securities sold under agreements to repurchase increased $82,830,000 at March 31, 2007, as compared with March 31, 2006, primarily as the result of the reallocation of funds by certain customers between deposit products and non-deposit products.

Other Liabilities

Other liabilities increased $8,334,000 at March 31, 2007, as compared with March 31, 2006, primarily as a result of an increase in the liability for the Company s retiree health plan of $1,158,000 due to the adoption of SFAS 158 and the accrual of $5,000,000 for investments not yet settled at March 31, 2007.

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. One measure of capital adequacy is the primary capital ratio which was 11.36% at March 31, 2007, as compared with 11.41% at March 31, 2006. These ratios are 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 minium requirement for classification as being well-capitalized by the banking regulatory authorities.

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 earning assets and interest-bearing liabilities combined with changes in market rates of interest greatly affect net interest income.

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The Company s net interest margin on a tax-equivalent basis, which is net income as a percentage of average earning assets, was 3.39% at March 31, 2007, down 62 basis points from 4.01% at March 31, 2006. The table that follows this discussion analyzes the changes in tax-equivalent net interest income for the two quarters ended March 31, 2007 and 2006.

Average earning assets increased $131,852,000, or 17%, from $759,023,000 in March 2006 to $890,875,000 in March 2007. The average yield on earning assets improved 66 basis points, from 5.59% at March 31, 2006 to 6.25% at March 31, 2007. The increase in the yield is attributable to increase in prime rate during the second quarter of 2006. The large increase in funds during the last eighteen months has funded the increase in loan demand and the remaining funds have been invested in U.S. Treasury and Agency securities and classified as held to maturity in 2006 and as available for sale in 2007. The loan portfolio generally has a 40%/60% blend of fixed/floating rate term. This fact, coupled with the relatively shorter term duration of investment maturities results in the Company being more asset sensitive to changes in market interest rates.

Average interesting bearing liabilities increased $145,582,000, or 25%, from $576,491,000 in March 2006 to $722,073,000 in March 2007. The average rate paid on interest bearing liabilities increased 145 basis points, from 2.08% in March 2006 to 3.53% in March 2007. This significant increase, as well as the decrease in the net tax-equivalent yield on earning assets, is the result of rates paid on funds management accounts, a non-deposit product classified as federal funds purchased and securities sold under agreement to repurchase.

Analysis of Average Balances, Interest Earned/Paid and Yield
(In Thousands)

	For the Quarter Ended March 31, 2007			For the Quarter Ended March 31, 2006		
	Average Balance	Interest Earned/ Paid	Yield	Average Balance	Interest Earned/ Paid	Yield
INTEREST INCOME:						
Loans (2)(3)	$403,773	$ 7,790	7.72%	$348,251	$ 6,183	7.10%
Federal funds sold	3,750	51	5.44%	35,623	440	4.94%
Held to maturity:						
Taxable	54,407	685	5.04%	179,996	1,953	4.34%
Non-taxable (1)	5,029	80	6.36%	6,152	110	7.15%
Available for sale:						
Taxable	400,995	4,901	4.89%	170,776	1,634	3.83%
Non-taxable (1)	17,520	258	5.89%	14,188	206	5.81%
Other	5,401	144	10.66%	4,037	86	8.52%
Total	$890,875	$13,909	6.25%	$759,023	$10,612	5.59%
INTEREST EXPENSE:						
Savings and demand, interest bearing	$287,874	$ 1,438	2.00%	$317,422	$ 1,262	1.59%
Time deposits	195,716	2,088	4.27%	121,827	956	3.14%
Federal funds purchased and securities sold under agreements to repurchase	231,234	2,725	4.71%	129,192	663	2.05%
Borrowings from FHLB	7,249	115	6.35%	8,050	116	5.76%
Total	$722,073	$ 6,366	3.53%	$576,491	$ 2,997	2.08%

Net tax-equivalent yield on earnings assets	3.39%	4.01%

(1) All interest earned is reported on a taxable equivalent basis using a tax rate of 34% in 2007 and 2006.

(2) Loan fees of $159 and $143 for 2007 and 2006, respectively, are included in these figures.

(3) Includes nonaccrual loans.

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Provision for Loan Losses

Management continuously monitors the Company s relationships with its loan customers, especially those in concentrated industries such as gaming/casino and hotel/motel, as well as the exposure for out of area loans, and their direct and indirect impact on its operations. A thorough analysis of current economic conditions and the quality of the loan portfolio is conducted on a quarterly basis. Management utilized these analyses, with special emphasis on the impact of Hurricane Katrina on the loan portfolio and underlying collateral, in determining the adequacy of its allowance for loan losses at March 31, 2007. In determining potential loan losses as a result of Hurricane Katrina since August 2005, the Company has evaluated its commercial and residential loan portfolios separately. Management continues its evaluation in recognition of the extraordinary impact of Katrina on its entire trade area, attempting to quantify potential losses in accordance with the Company s established methodology. Loan delinquencies and deposit overdrafts are closely monitored in order to identify developing problems as early as possible.

Additionally, Management has considered the historical data available from the impact of other natural disasters on the Mississippi Gulf Coast and other coastal communities, including the length of time between the storm s landfall and identification of all losses. Past bank experience with hurricanes and FDIC research have shown that the actual loss position may not be known until 24 months after the event.

Although more than eighteen months have passed, much uncertainty remains regarding the impact of federal and state assistance, settlement of insurance claims, the availability and affordability of windstorm insurance and the rate and pace of recovery in the Company s trade area. Commercial and personal customers are still assessing their resources and making decisions about their future plans. Meanwhile, construction costs continue to escalate, further impacting recovery efforts. The ability of customers to service their debt must be carefully considered.

We are starting to realize the full impact of Hurricane Katrina on insurance coverage going forward. Several carriers have announced their intention to restrict coverage in our trade area. For those carriers continuing to write policies on the Gulf Coast, premiums are increasing significantly. Commercial development has already been negatively impacted by the ability to obtain insurance coverage. Ultimately, the effect of the insurance uncertainty may pose a potential risk to a large portion of our loan portfolio.

The Company has identified no additional significant potential losses as a result of Hurricane Katrina since its initial evaluation in September 2005. In fact, some loans which were thought to pose a potential loss during the initial evaluation have shown positive developments. It is also very possible that potential losses, despite the best efforts of the Company, have not yet been identified. Management believes that it is reasonably possible that the actual amount of potential losses as a result of Hurricane Katrina may be less that what was estimated in September 2005, but as a result of the factors discussed above, this amount cannot be reasonably estimated at this time and no provision or negative provision for losses on loans was recorded for the quarter ended March 31, 2007.

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The Company recorded a provision of $49,000 during the first quarter of 2007 relating to potential losses on overdrawn deposit accounts.

Trust Department Income and Fees

Trust department income and fees increased $93,000 for the quarter ended March 31, 2007 as compared with the quarter ended March 31, 2006, as a result of an increase in cash management accounts funded with insurance and other proceeds.

Service Charges on Deposit Accounts

Service charges on deposit accounts increased $611,000 for the quarter ended March 31, 2007, as compared with the quarter ended March 31, 2006. This increase is the result of an increase of ATM fee income as transactions at casino ATMs have significantly increased during this period and an increase in NSF fee income due to an increase in the fee charged.

Other Income

Other income increased $292,000 for the quarter ended March 31, 2007 as compared with the quarter ended March 31, 2006, as the result of a gain on the sale of bank premises.

Salaries and Employee Benefits

Salaries and employee benefits increased $354,000 for the quarter ended March 31, 2007, as compared with the quarter ended March 31, 2006. The Company increased salaries and incentives to its employees in order to reward performance and retain personnel within the local competitive employment environment.

Net Occupancy

Net occupancy increased $35,000 for the quarter ended March 31, 2007, as compared with the quarter ended March 31, 2006, as a result of an increase in costs associated with insurance coverage.

Equipment Rentals, Depreciation and Maintenance

Equipment rentals, depreciation and maintenance increased $123,000 for the quarter ended March 31, 2007, as compared with the quarter ended March 31, 2006 due to an increase in repair and maintenance costs. For several quarters after Hurricane Katrina hit in August 2005, repairs and maintenance were covered by the Company s insurance. Since mid 2006, however, such costs are once again borne by the Company.

Other Expense

Other expense increased $195,000 for the quarter ended March 31, 2007, as compared with the quarter ended March 31, 2006, as ATM surcharge expense increased based on the increase in the number of ATM transactions during the first quarter of 2007 as compared with the first quarter of 2006.

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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. 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.

Since Hurricane Katrina, the Company s deposits and non-deposit accounts have increased significantly as discussed previously. Management carefully monitors its liquidity needs, particularly relating to these potentially volatile deposits. The Company is currently investing its excess funds in short-term U. S. Treasury and Agency Securities. It is anticipated that loan demand will be funded in future quarters from the maturity of these investments. Federal funds sold and federal funds purchased are utilized by the Company to manage its daily liquidity position.

Item 4: Controls and Procedures

As of March 31, 2007, 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 March 31, 2007 that have materially affected, or are reasonably likely to materially affect, the Company s internal control over financial reporting.

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PART II
OTHER INFORMATION

Item 1 Legal Proceedings

The Company s bank subsidiary (the Bank) filed suit again USF&G in 1998 to recover damages for USF&G s bad faith failure to defend and indemnify the Bank in connection with a lawsuit filed against the Bank in 1996. The Bank obtained legal representation from a local plaintiff s attorney and customer (Attorney) on a contingent basis.

In December 2000, the case was transferred from the judge to whom it was originally assigned to a second judge (the Judge). The Judge had previously handled some discovery matters in the case.

The Bank had made a routine loan to the Judge in November 1998, which was guaranteed by the Attorney. The loan was repaid in February 2000 by someone other than the Judge, apparently at the request of the Attorney. Neither the Attorney nor the Judge disclosed the loan or the repayment to USF&G or its counsel.

During the course of the case, the Bank and USF&G filed competing motions for summary judgment. The Judge granted summary judgment in the Bank s favor on the issue of liability and subsequently presided over a settlement conference in which he expressed his opinion about the value of the case in monetary terms. The case was settled on December 24, 2001, for $1.5 million

In 2003, the Attorney, the Judge and other parties were indicted for alleged fraud, bribery, etc. involving various events, including allegations concerning the Bank v. USF&G lawsuit. Neither the Bank nor any Bank employee was indicted. Following the indictments, USF&G filed a civil action against the Attorney, the Judge and the Bank alleging fraud in connection with the outcome of the Bank v. USF&G lawsuit. The complaint demands $2.5 million in compensatory damages and $10 million in punitive damages, prejudgment interest and attorneys fees, etc. The USF&G v. Bank suit was stayed until 30 days following the completion of the criminal case. There has been no discovery.

The criminal case against the Attorney, the Judge and other parties concluded on August 12, 2005. No guilty verdicts were returned. The defendants received not guilty verdicts on several counts and there was no verdict (mistrial) on a number of other counts, including the Bank v. USF&G matter. On September 16, 2005, the U. S. Attorney s office announced that it would retry the Attorney, the Judge and other parties on fraud and bribery charges related to the Bank v. USF&G matter. The new trial began on February 7, 2007. On March 31, 2007, guilty verdicts on counts of bribery, conspiracy, mail fraud/honest services fraud and racketeer influenced corrupt organizations (RICO) violations were returned against the Attorney, the Judge and other parties. The Attorney, the Judge and other parties have indicated that they plan to appeal the guilty verdicts. Despite the verdicts in the criminal case, the USF&G v. Bank suit remains subject to the stay order until the stay order is lifted by the judge in that case.

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Item 4 Submission of Matters to a Vote of Security Holders
(a) The Annual Meeting of Shareholders of the Company was held on April 18, 2007.
(b) The following five directors were elected at the meeting to hold office for a term of one year:

	Approve	Disapprove
Drew Allen	4,994,210.750	335.685
Rex E. Kelly	4,994,210.750	335.685
Dan Magruder	4,994,210.750	335.685
Lyle M. Page	4,860,615.750	133,930.685
Chevis C. Swetman	4,613,582.750	381,963.685

Of the 5,548,199 shares outstanding and eligible to vote on April 18, shares not voted amounted to 539,705.863 and there were 13,946.702 abstentions.

Item 5 Other Information
(a) On February 28, 2007, the Board of Directors re-appointed the following officers of the Company:

President and CEO	Chevis C. Swetman
Executive Vice President	A. Wes Fulmer
First Vice President	Thomas J. Sliman
Second Vice President	Jeannette E. Romero
Vice President	Robert M. Tucei
Vice President and Secretary	Ann F. Guice
Chief Financial Officer	Lauri A. Wood

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

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(b) Reports on Form 8-K
A Form 8-K was filed on January 23, 2007 and April 16, 2007.

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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: May 9, 2007

By: /s/ Chevis C. Swetman

Chevis C. Swetman
Chairman, President and Chief Executive Officer

Date: May 9, 2007

By: /s/ Lauri A. Wood

Lauri A. Wood
Chief Financial Officer and Controller
(principal financial and accounting officer)