PEOPLES BANCORP INC
Form 10-Q/A
August 14, 2003

FORM 10-Q/A
(Amendment No. 1)

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

(Mark One)

[X] QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d)
OF THE SECURITIES EXCHANGE ACT OF 1934
For the quarterly period ended June 30, 2003

OR

[ ] TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d)
OF THE SECURITIES EXCHANGE ACT OF 1934
For the transition period from ____ to ____

Commission file number 0-16772

PEOPLES BANCORP INC.
(Exact name of Registrant as specified in its charter)

Ohio
(State or other jurisdiction of incorporation or organization)

31-0987416
(I.R.S. Employer Identification No.)

138 Putnam Street, P. O. Box 738, Marietta, Ohio	45750
(Address of principal executive offices)	(Zip Code)

Registrant's telephone number, including area code: (740) 373-3155

Not Applicable
(Former name, former address and former fiscal year, if changed since last report)

Indicate by check mark whether the registrant (1) has filed all reports required 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 is an accelerated filer (as defined in Rule 12b-2 of the Exchange Act).

Yes X No

Indicate the number of shares outstanding of each of the issuer's classes of Common Stock, at August 7, 2003: 10,164,001.

PEOPLES BANCORP INC.
QUARTERLY REPORT ON FORM 10-Q/A
FOR THE QUARTERLY PERIOD ENDED JUNE 30, 2003

EXPLANATORY NOTE

The purpose of this Form 10-Q/A ("Form 10-Q/A") is to amend Item 2 of Part I of the Quarterly Report on Form 10-Q of Peoples Bancorp Inc. for the quarterly period ended June 30, 2003 ("Peoples' June 30, 2003 Form 10-Q"), to correct an inversion of the labels in the first column of the table in the "Interest Rate Sensitivity and Liquidity" section of Management's Discussion and Analysis of Financial Condition and Results of Operations. There have been no additional changes to any other section of Item 2 of Part I of Peoples' June 30, 2003 Form 10-Q.

This amendment does not reflect events occurring after the original filing of the Quarterly Report on August 11, 2003, or modify or update those disclosures as presented in the original Form 10-Q, except to reflect the amendment described above.

PART I - FINANCIAL INFORMATION

ITEM 2: MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS \OF OPERATIONS

SELECTED FINANCIAL DATA

The following data should be read in conjunction with the unaudited consolidated financial statements and the management discussion and analysis that follows:

	At or For the Three Months Ended June 30,	
SIGNIFICANT RATIOS	2003	2002
Return on average equity	12.92 %	18.85 %
Return on average assets	1.25 %	1.54 %
Net interest margin (a)	3.64 %	4.54 %
Non-interest income leverage ratio (b)	46.54 %	43.06 %
Efficiency ratio (c)	51.10 %	50.97 %
Average stockholders' equity to average assets	9.67 %	8.16 %
Average loans to average deposits	86.70 %	93.40 %

Cash dividends to net income		30.04 %		25.24 %	
ASSET QUALITY RATIOS (end of period)					
Nonperforming loans as a percent of total loans (d)		0.62 %		0.87 %	
Nonperforming assets as a percent of total assets (e)		0.35 %		0.57 %	
Allowance for loan losses to loans net of unearned interest		1.54 %		1.44 %	
CAPITAL RATIOS (end of period)					
Tier I capital ratio		13.87 %		11.26 %	
Risk-based capital ratio		15.34 %		12.62 %	
Leverage ratio		8.80 %		8.42 %	
PER SHARE DATA					
Net income per share - basic	$	0.55	$	0.60	$
Net income per share - diluted		0.54		0.59	
Cash dividends per share		0.16		0.15	
Book value per share (end of period)		17.56		13.30	
Tangible book value per share (end of period) (f)	$	12.75	$	9.71	$
Weighted average shares outstanding - Basic		9,905,403		7,873,795	
Weighted average shares outstanding - Diluted		10,094,114		8,102,047	

Introduction

The following discussion and analysis of the Consolidated Financial Statements of Peoples is presented to provide insight into management's assessment of the financial condition and results of operations. Peoples' subsidiaries are Peoples Bank, National Association ("Peoples Bank"), Peoples Investment Company, PEBO Capital Trust I and PEBO Capital Trust II. Peoples Bank also operates Peoples Insurance Agency, Inc. ("Peoples Insurance"), which offers a full range of life, property, and casualty insurance products to customers in Peoples' markets, and Peoples Loan Services, Inc., which invests in certain loans originated in Peoples' markets. Peoples Investment Company also owns Peoples Capital Corporation.

Peoples Bank is a member of the Federal Reserve System and subject to regulation, supervision, and examination by the Office of the Comptroller of the Currency. Peoples Bank offers complete financial products and services through 50 financial service locations and 33 ATMs in Ohio, West Virginia, and Kentucky. Peoples Bank's e-banking service, Peoples OnLine Connection, can be found on the Internet at www.peoplesbancorp.com (this uniform resource locator (URL) is an inactive, textual reference only). Peoples Bank provides an array of financial products and services to customers that include traditional banking products such as deposit accounts, lending products, credit and debit cards, corporate and personal trust services, and safe deposit rental facilities. Peoples provides services through ordinary walk-in offices and automobile drive-in facilities, automated teller machines, banking by phone, and the Internet.

Peoples Bank also makes available other financial services through Peoples

Financial Advisors, which provides customer-tailored services for fiduciary needs, investment alternatives, financial planning, retirement plans, and other asset management needs. Brokerage services are offered exclusively through Raymond James Financial Services, member NASD/SIPC and an independent broker/dealer, located at Peoples Bank offices.

Peoples Investment Company and Peoples Capital Corporation were formed in 2001 to allow management to better deploy investable funds and provide new opportunities to make investments, including, but not limited to, low-income housing tax credit funds, that are either limited or restricted at the bank level.

This discussion and analysis should be read in conjunction with the audited Consolidated Financial Statements for the year ended December 31, 2002, and notes thereto, as well as the ratios, statistics and discussions contained elsewhere in this Form 10-Q.

References will be found in this Form 10-Q to the following significant transactions that have impacted or will impact Peoples' results of operations:

- As discussed in Note 1 of Notes to the Consolidated Unaudited Financial Statements, on May 9, 2003, Peoples Bancorp completed its acquisition of Kentucky Bancshares Incorporated ("Kentucky Bancshares"), the holding company of Kentucky Bank & Trust. In addition, Peoples Bank closed an office at 404 Ferry Street in Russell, Kentucky concurrent with this acquisition. Peoples Bank also plans to close its Catlettsburg, Kentucky office in October 2003 due to the proximity of the acquired Ashland, Kentucky office.

- On March 13, 2003, Peoples announced the authorization to repurchase up to 300,000, or approximately 3%, of Peoples' outstanding common shares from time to time in open market or privately negotiated transactions ("2003 Stock Repurchase Program"). The common shares repurchased will be used for projected stock option exercises granted under Peoples' stock option plans, a portion of the consideration to be paid in acquisitions, and other general corporate purposes. The timing of the purchases and the actual number of common shares purchased will depend on market conditions and limitations imposed by applicable federal securities laws. The 2003 Stock Repurchase Program will expire on December 31, 2003.

- On December 19, 2002, Peoples Bancorp Inc. completed the sale of 1,440,000 common shares through a firm commitment underwritten offering and on January 3, 2003, sold an additional 216,000 common shares in conjunction with the option granted to the underwriters to cover over-allotments (collectively, the "Common Stock Offering"). The Common Stock Offering generated new capital totaling $36.9 million after offering expenses. In January 2003, Peoples Bancorp used $16 million of the net proceeds to increase Peoples Bank's capital position. Peoples intends to use the remaining net proceeds for general corporate purposes, which may include the repayment of outstanding indebtedness, mergers and acquisitions, such as the Kentucky Bancshares acquisition, or other strategic investments.

- In December 2002, Peoples initiated an investment growth strategy to offset the dilutive impact of the Common Stock Offering, thereby leveraging Peoples' increased capital levels ("Investment Growth Strategy"). As a result of this Investment Growth Strategy, total earning assets, particularly mortgage-backed investment securities, increased by $260 million in January 2003 compared to the year-end 2002 balance. Peoples funded the investment purchases using $187 million of wholesale market repurchase agreements at an average cost of 2.92%, $58 million of FHLB advances at an average cost of 2.15% and $15 million from the Common Stock Offering. In March 2003, Peoples purchased an additional $20 of million mortgage-backed investment securities as part of this strategy. This purchase was funded using an $18.6 million wholesale market repurchase agreement at a rate of 2.09%, with the remainder from available corporate funds.

o On April 10, 2002, Peoples issued $7.0 million of LIBOR based floating rate trust preferred securities through a newly-formed subsidiary, PEBO Capital Trust II, which participated in a pooled offering. PEBO Capital Trust II used the proceeds from the issuance to purchase floating rate junior subordinated debt securities due April 22, 2032 (the "Debentures"). Peoples has used the net proceeds from the sale of the Debentures for general corporate purposes and management of corporate liquidity.

The impact of these transactions, where significant, is discussed in the applicable sections of this management's discussion and analysis.

Critical Accounting Policies

The accounting and reporting policies of Peoples conform to accounting principles generally accepted in the United States ("US GAAP") and to general practices within the banking industry. The preparation of the financial statements in conformity with US GAAP requires management to make estimates and assumptions that affect the amounts reported in the financial statements and accompanying notes. Actual results could differ from those estimates. Management has identified the accounting policies described below as those that, due to the judgments, estimates and assumptions inherent in those policies, are critical to an understanding of Peoples' consolidated financial statements and management's discussion and analysis.

Income Recognition

Peoples recognizes interest income by methods that conform to US GAAP that include general accounting practices within the banking industry. In the event management believes collection of all or a portion of contractual interest on a loan has become doubtful, which generally occurs after the loan is 90 days past due, Peoples discontinues the accrual of interest. In addition, previously accrued interest deemed uncollectible that was recognized in income in the current year is reversed, while amounts recognized in income in the prior year are charged against the allowance for loan losses. Interest received on nonaccrual loans is included in income only if principal recovery is reasonably assured. A nonaccrual loan is restored to accrual status when it is brought current or has performed in accordance with contractual terms for a reasonable period of time, and the collectibility of the total contractual principal and interest is no longer in doubt.

Allowance for Loan Losses

In general, determining the amount of the allowance for loan losses requires significant judgment and the use of estimates by management. Peoples maintains an allowance for loan losses to absorb probable losses in the loan portfolio based on a quarterly analysis of the portfolio. This formal analysis determines an appropriate level and allocation of the allowance for loan losses among loan types and resulting provision for loan losses by considering factors affecting loan losses, including specific losses, levels and trends in impaired and nonperforming loans, historical loan loss experience, current national and local economic conditions, volume, growth and composition of the portfolio, regulatory guidance and other relevant factors. Management continually monitors the loan portfolio through its Loan Review Department and Loan Loss Committee to evaluate the adequacy of the allowance. The provision expense could increase or decrease each quarter based upon the results of management's formal analysis.

The amount of the allowance for the various loan types represents management's estimate of expected losses from existing loans based upon specific allocations for individual lending relationships and historical loss experience for each category of homogeneous loans. The allowance for loan losses related to impaired loans is based on discounted cash flows using the loan's initial effective interest rate or the fair value of the collateral for certain collateral dependent loans. This evaluation requires management to make estimates of the amounts and timing of future cash flows on impaired loans, which consists primarily of nonaccrual and restructured loans. While allocations are made to specific loans and pools of loans, the allowance is available for all loan losses.

Individual loan reviews are based upon specific quantitative and qualitative criteria, including the size of the loan, loan quality ratings, value of collateral, repayment ability of borrowers, and historical experience factors. The historical experience factors utilized are based upon past loss experience, trends in losses and delinquencies, the growth of loans in particular markets and industries, and known changes in economic conditions in the particular lending markets. Allowances for homogeneous loans (such as residential mortgage loans, credit cards, personal loans, etc.) are evaluated based upon historical loss experience, trends in losses and delinquencies, growth of loans in particular markets, and known changes in economic conditions in each particular lending market. Consistent with the evaluation of allowances for homogenous loans, allowances relating to the Overdraft Privilege program are based upon management's monthly analysis of accounts in the program. This analysis considers factors that could affect future losses on existing accounts, including historical loss experience and length of overdraft.

There can be no assurance that the allowance for loan losses will be adequate to cover all losses, but management believes the allowance for loan losses of $14.2 million at June 30, 2003, was adequate to provide for probable losses from existing loans based on information currently available. While management uses available information to provide for loan losses, the ultimate collectibility of a substantial portion of the loan portfolio and the need for future additions to the allowance will be based on changes in economic conditions and other relevant factors. As a result of a slowdown in economic activity that could adversely affect cash flows for both commercial and individual borrowers, Peoples could experience increases in problem assets, delinquencies and losses on loans.

Investment Securities

Investment securities are recorded at cost, which includes premiums and discounts if purchased at other than par or face value. Peoples amortizes premiums and accretes discounts as an adjustment to interest income using the effective interest method over the estimated life of the security. The cost of investment securities sold, and any resulting gain or loss, is based on the specific identification method.

Management determines the appropriate classification of investment securities at the time of purchase. Held-to-maturity securities are those securities that Peoples has the positive intent and ability to hold to maturity and are recorded at amortized cost. Available-for-sale securities are those securities that would be available to be sold in the future in response to Peoples' liquidity needs, changes in market interest rates, and asset-liability management strategies, among others. Available-for-sale securities are reported at fair value, with unrealized holding gains and losses reported in stockholders' equity as a separate component of other comprehensive income, net of applicable deferred income taxes.

Presently, Peoples classifies its entire investment portfolio as available-for-sale. As a result, both the investment and equity sections of Peoples' balance sheet are more sensitive to changes in the overall market value of the investment portfolio, due to changes in market interest rates, investor confidence and other factors affecting market values, than if the investment portfolio was classified as held-to-maturity.

Management systematically evaluates investment securities for other-than-temporary declines in fair value on a quarterly basis. Declines in fair value of individual investment securities below their amortized cost that are deemed to be other-than-temporary will be written down to current market value and included in earnings as realized losses. There were no investment securities identified by management to be other-than-temporarily impaired for the six months ended June 30, 2003. If the financial markets experience deterioration and investments decline in fair value, charges to income could occur in future periods.

Goodwill and Other Intangible Assets

Statement of Financial Accounting Standards No. 142, "Accounting for Goodwill and Other Intangible Assets" ("SFAS 142"), establishes standards for the amortization of acquired intangible assets and the non-amortization and impairment assessment of goodwill. In addition, Statement of Financial Accounting Standards No. 147, "Acquisitions of Certain Financial Institutions" ("SFAS 147"), establishes standards for unidentifiable intangible assets acquired specifically in branch purchases that qualify as business combinations. At June 30, 2003, Peoples had $7.8 million of core deposit and trust relation intangible assets, subject to amortization, and $40.8 million of goodwill, not subject to periodic amortization.

Goodwill arising from business combinations represents the value attributable to unidentifiable intangible elements in the business acquired. Goodwill recorded by Peoples in connection with its acquisitions relates to the value inherent in the banking business and the value is dependent upon Peoples' ability to provide quality, cost effective services in a competitive market place. As such, goodwill value is supported ultimately by revenue that is driven by the volume of business transacted. A decline in earnings as a result of a lack of growth or the inability to deliver cost effective services over sustained periods can lead to impairment of goodwill that could adversely impact earnings in future periods.

Under US GAAP in effect through December 31, 2001, Peoples amortized goodwill on a straight-line basis over periods ranging from ten to fifteen years. Effective January 1, 2002, Peoples was no longer required to amortize previously recorded goodwill as a result of adopting SFAS 142 and SFAS 147.

Peoples has reviewed its goodwill assets and has concluded the recorded value of goodwill was not impaired as of June 30, 2003. There are many assumptions and estimates underlying the determination of impairment and using different, but still reasonable, assumptions could produce a significantly different result. Additionally, future events could cause management to conclude impairment indicators exist and Peoples' goodwill is impaired, which would result in Peoples' recording an impairment loss. Any resulting impairment loss could have a material, adverse impact on Peoples' financial condition and results of operations.

Overview of the Income Statement

In the second quarter of 2003, net income totaled $5,439,000, up 14% from $4,763,000 a year ago and up 8% from $5,014,000 for the first quarter of 2003.

Diluted earnings per share were $0.54 for the second quarter of 2003 versus $0.59 for the same period last year and $0.51 the first quarter of 2003. For the six months ended June 30, 2003, net income totaled $10,453,000, representing an 11% increase over the $9,456,000 earned a year ago. Earnings per diluted share were $1.05 for the six months ended June 30, 2003, versus $1.18 for the first six months of 2002.

Peoples' increased net income in 2003 is due in large part to additional net interest income resulting from the Investment Growth Strategy implemented in the first quarter of 2003 and an overall increase in net revenues attributable to the Kentucky Bancshares acquisitions. The lower earnings per share is attributable to higher average common shares outstanding, due to the issuance of approximately 593,000 common shares in the second quarter of 2003 as partial consideration in the Kentucky Bancshares acquisition and 1.7 million shares in the Common Stock Offering. However, the Investment Growth Strategy offset most of the dilutive effect of the Common Stock Offering. Peoples also recognized merger-related costs of approximately $215,000 after-tax (or $0.02 per share) relating to the Kentucky Bancshares acquisition.

Net interest income grew to $14,161,000 for the three months ended June 30, 2003, from $13,643,000 last quarter and $12,511,000 a year ago. Net interest margin was 3.64% in the second quarter of 2003 versus 3.87% and 4.54% for the first quarter of 2003 and second quarter of 2002, respectively. For the six months ended June 30, 2003, net interest income totaled $27,804,000 and net interest margin was 3.74% compared to $24,670,000 and 4.53% for the same period in 2002. The Investment Growth Strategy accounted for a significant portion of the increase in net interest income in 2003, but also contributed to compression of net interest margin.

For the quarter ended June 30, 2003, non-interest income was $4,282,000, compared to $3,626,000 for the same period last year. On a year-to-date basis, non-interest income totaled $8,217,000 through June 30, 2003, compared to $7,584,000 last year. Peoples' enhanced non-interest income was primarily the result of higher deposit service charge income, with revenues from Peoples' e-banking services, mortgage banking income and fiduciary activities also contributing to the increase. Non-interest expense was $10,042,000 in the second quarter of 2003, up 17% compared to $8,549,000 for the same period in 2002. On a year-to-date basis, non-interest expense totaled $19,746,000 and $17,227,000 through June 30, 2003 and 2002, respectively. These increases are largely the result of acquisitions and strategic initiatives, which caused Peoples to incur additional expenses in 2003.

Interest Income and Expense

Peoples derives a majority of its interest income from loans and investment securities and incurs interest expense on interest-bearing deposits and borrowed funds. Net interest income, the amount by which interest income exceeds interest expense, remains Peoples' largest source of revenue. Management periodically adjusts the mix of assets and liabilities in an attempt to manage and improve net interest income; however, factors that influence market interest rates, such as interest rate changes by the Federal Reserve Open Market Committee and Peoples' competitors, may have a greater impact on net interest income than adjustments made by management. Consequently, a volatile rate environment can make it extremely difficult to manage net interest margin and income in the short term, much less anticipate and position the balance sheet for future changes.

In the second quarter of 2003, net interest income totaled $14,161,000, up 13% compared to $12,511,000 for 2002's second quarter. Interest income increased $3,180,000 (or 16%) from last year, totaling $23,492,000 in the second quarter of 2003, while interest expense was up $1,530,000 (or 20%), totaling $9,331,000 for the three months ended June 30, 2003. Compared to the first quarter of 2003, net interest income grew 4% in the second quarter of 2003. On a year-to-date basis through June 30, 2003, net interest income totaled $27,804,000 compared to $24,670,000, an increase of $3,134,000 (or 13%). For the same period, total interest income grew 14% to $46,269,000, while interest expense was up 16% to $18,465,000. These increases are primarily the result of the Investment Growth Strategy, while acquisitions also fueled some of the growth.

Peoples derives a portion of its interest income from loans to and investments issued by states and political subdivisions. Since these revenues generally are not subject to income taxes, management believes it is more meaningful to analyze net interest income on a fully-tax equivalent ("FTE") basis, which adjusts interest income by converting tax-exempt income to the pre-tax equivalent of taxable income using an effective tax rate of 35%. For the three months ended June 30, 2003, interest income was increased by $416,000 for the impact of the tax-equivalent adjustment, resulting in FTE net interest income of $14,577,000, up $1,657,000 (or 13%) from $12,920,000 for the same period in 2002, and up $524,000 (or 4%) from $14,053,000 for the first quarter of 2003. The FTE yield on Peoples' earning assets was 5.96% for quarter ended June 30, 2003, versus 6.41% and 7.29% for the first quarter of 2003 and second quarter of 2002, respectively, while the cost of interest-bearing liabilities was 2.65%, 2.91% and 3.12% for the same periods, respectively. On a year-to-date basis, FTE net interest income was $28,630,000 through June 30, 2003, compared to $25,430,000 for the first half of 2002, an increase of $3,200,000 (or 13%). For the six months ended June 30, 2003, the FTE yield on earning assets was 6.17% and cost of interest-bearing liabilities was 2.77% versus 7.39% and 3.24%, respectively, for the same period last year.

Net interest margin, calculated by dividing FTE net interest income by average interest-earning assets, serves as an important measurement of the net revenue stream generated by the mix and pricing of Peoples' earning assets and interest-bearing liabilities. In the second quarter of 2003, net interest margin was 3.64% versus 3.87% last quarter and 4.54% a year ago. For the six months ended June 30, 2003, net interest margin was 3.74%, down from 4.53% for the first six months of 2002. The lower net interest margin in 2003 is largely the result of high volumes of prepayments in both the loan and investment portfolios, which were reinvested at significantly lower rates due to the current interest rate environment. In addition, a full quarter's impact of the Investment Growth Strategy contributed to compression of net interest margin.

Earning assets averaged $1.61 billion in the second quarter of 2003, up $151.1 million (or 10%) compared to $1.46 billion last quarter, and up $467.9 million (or 41%) from $1.14 billion for the second quarter of 2002. Net loans accounted for the largest portion of earning assets, averaging $881.6 million for three months ended June 30, 2003, compared to average net loans of $837.6 million and $784.3 million for the first quarter of 2003 and second quarter of 2002, respectively. Loans acquired in acquisitions accounted for a majority of the loan growth. Investment securities averaged $703.6 million for the second quarter of 2003 compared to $608.0 million for the prior quarter and $351.9 for 2002's second quarter, with the increases largely attributable to the Investment Growth Strategy. The FTE yield on net loans was 7.14% for the quarter ended June 30, 2003, versus 7.40% for the first quarter of 2003 and 7.76% for the three months of June 30, 2002, while the FTE yield on investments was 4.63%, 5.13% and 6.27% for the same periods, respectively. Declining yields on both loans and investment securities were a result of lower market interest rates.

On a year-to-date basis, average earning assets were $1.53 billion in 2003 compared to $1.12 million in 2002. Net loan balances increased $84.7 million (or 11%), averaging $859.7 million for the six months ended June 30, 2003, versus $775.0 million a year ago. Through six months in 2003, the FTE yield on loans dropped 62 basis points from 7.88% to 7.26%. Average investment securities totaled $656.1 million in the first half of 2003 versus $347.4 million for the first six months of 2002, while the FTE yield on investments was 4.86% and 6.34% for the same periods, respectively. Both the higher average balance and lower yield were principally the result of the Investment Growth Strategy implemented during the first quarter of 2003.

In the second quarter of 2003, Peoples' average interest-bearing liabilities totaled $1.41 billion, up from $1.27 billion in the first quarter of 2003 and $1.00 billion a year ago. For the six months ended June 30, 2003, average interest-bearing liabilities were $1.34 billion, up from $992.1 million a year ago. Traditional deposits comprise the majority of Peoples' interest-bearing liabilities, averaging $906.9 million for the three months ended June 30, 2003 compared to $843.2 million and $755.5 million for the first quarter of 2003 and second quarter of 2002, respectively. Through six months of 2003, traditional deposits averaged $875.2 million compared to $740.6 million last year, an increase of $134.6 million (or 18%). These increases were due largely to deposits acquired as part of acquisitions. In the second quarter of 2003, cost of funds from interest-bearing deposits was 2.17%, down from 2.50% in the prior quarter and 2.74% in second quarter of 2002. The cost of funds from interest-bearing deposits was 2.33% for the first half of 2003, down 58 basis points from 2.91% for the same period in 2002. The lower rates paid on interest-bearing deposit accounts were a result of market rates remaining at low levels. However, management continues to price Peoples' longer-term certificates of deposit competitively as part of a strategy to shift to longer-term funding.

Peoples also utilizes a variety of borrowings as complementary funding sources to traditional deposits. Total borrowed funds averaged $499.9 million for the three months ended June 30, 2003, up from $429.2 million in the first quarter of 2003 and up from $246.8 million a year ago. The majority of these increases are attributable to borrowed funds used in the Investment Growth Strategy. The interest cost of Peoples' borrowed funds was 3.53% in second quarter of 2003, down from 3.70% last quarter and 4.29% for the same period in 2002. For the six months ended June 30, 2003, borrowed funds averaged $464.7 million compared to $251.6 million for the first half of 2002, while the average cost was 3.61% and 4.21% for the same periods, respectively.

Peoples' main sources of borrowed funds are short- and long-term advances from the FHLB. Short-term FHLB advances are primarily variable rate, LIBOR based advances that are used to balance Peoples' daily liquidity needs and may be repaid at any time without a penalty. The long-term FHLB advances consist largely of 10-year borrowings requiring monthly interest payments, with principal due at maturity. The rate on these advances are fixed for initial periods ranging from two to four years, depending on the specific advance. After the initial fixed rate period, the FHLB has the option to convert each advance to a LIBOR based, variable rate advance; however, Peoples may repay the advance, without a penalty, if the FHLB exercises its option.

Short-term FHLB borrowings averaged $23.0 million for the quarter ended June 30, 2003, compared to $12.9 million a year ago, with an average cost of 1.59% and 1.83% for the same periods, respectively. This increase was attributable to short-term advances used in the Investment Growth Strategy. Average long-term FHLB borrowings were up $27.0 million (or 14%) compared to the second quarter of 2002, totaling $223.0 million for the three months ended June 30, 2003, while the average cost dropped to 4.64% from 4.85%. The increase in long-term FHLB advances was mainly due to management's efforts to secure longer-term funding during this period of low rates. A portion of the new long-term FHLB advances are fixed rate advances that require monthly principal and interest payments and may not be repaid prior to maturity without a penalty. Management intends to continue using a variety of FHLB borrowings to fund asset growth and manage interest rate sensitivity, as deemed appropriate. For the six months ended June 30, 2002, short-term FHLB borrowings averaged $19.5 million versus $22.7 million a year ago, while the average cost was 1.53% and 1.82% for the same periods, respectively. Average long-term FHLB borrowings were $223.5 million through six months of 2003, at an average cost of 4.67%, versus $194.4 million and average cost of 4.86% a year ago.

In addition to FHLB borrowings, Peoples also accesses national market repurchase agreements to diversify funding sources. Typically, these repurchase agreements are for terms of 90 days or less. However, Peoples utilized repurchase agreements with terms ranging from 2 to 5 years as part of the Investment Growth Strategy in an effort to match the term of the funding sources with the initial estimated life of the investments. As a result, wholesale market term repurchase agreements averaged $216.3 million at an average cost of 2.91%, up from $150.5 million and average cost of 2.96% in the prior quarter and $9.1 million and average cost of 3.69% a year ago. On a year-to-date basis, wholesale market repurchase agreements averaged $183.5 million, at an average cost of 2.93%, through June 30, 2003, compared to $7.7 million and average cost of 3.65% a year ago.

Peoples offers cash management services to its business customers, which also provide short-term funding in the form of overnight repurchase agreements. For the three months ended June 30, 2003, overnight repurchase agreements, excluding balances of wholesale market term repurchase agreements, averaged $20.7 million, down from $21.6 million last quarter and $23.8 million a year ago. The average rate paid on overnight repurchase agreements was 0.87% in second quarter of 2003, compared to 0.86% in the prior quarter and 1.40% in the second quarter of 2002. Average overnight repurchase agreements totaled $21.1 for the six months ended June 30, 2003, compared to $23.3 million a year ago, while the average cost dropped 60 basis points from 1.46% to 0.86%.

Late in the second quarter of 2003, management initiated a plan to improve the performance of Peoples' investment securities portfolio in response to the high rate of prepayments on mortgage-backed securities and the corresponding downward pressure on yields due to accelerated amortization of bond premiums. As part of this plan, Peoples sold $48.6 million of lower yielding mortgage-backed securities resulting in a net loss of $37,000. Management sold additional lower yielding securities experiencing increased prepayment speeds subsequent to quarter end and reinvested the proceeds into higher yielding instruments. Peoples expects the repositioning to improve both the yields and the timing of cash flows from these securities.

On July 1, 2003, Peoples adopted the reporting requirements of SFAS 150, as required. This adoption resulted in Peoples reclassifying its Trust Preferred Securities, presented on the balance sheet as "Guaranteed preferred beneficial interest in junior subordinated debentures", to the liabilities section of the balance sheet. In addition, Peoples will recognize approximately $1.2 million of interest expense on its Trust Preferred Securities in the final six months of 2003 that would have otherwise been recognized as non-interest expense had SFAS 150 not been in effect. Had SFAS 150 been in effect for the first six months of 2003, net interest margin would have been 3.59% versus the 3.74% reported.

As is the case with most financial institutions, Peoples continues to experience net interest margin compression due to interest rates remaining at historically low levels. Significant volumes of assets continue to reprice downward with limited flexibility for a corresponding decrease in rates paid on interest-bearing liabilities. In addition, a weak economy and other factors are suppressing loan growth. While these conditions challenge Peoples' ability to enhance net interest income and margin in the short-term, current asset-liability simulations indicate a sustained increase in interest rates could cause net interest income to increase modestly based on Peoples' interest rate risk position at June 30, 2003. Even though management continues to focus on minimizing the impact of future rate changes on Peoples' earnings, Peoples' net interest margin and income remain difficult to predict, and to manage, since changes in market interest rates remain uncertain.

Provision for Loan Losses

In the second quarter of 2003, Peoples' provision for loan losses was $935,000, up from $831,000 in the prior quarter and down from $980,000 a year ago. The changes in the quarterly provision amounts reflected the changes in the provision related to the Overdraft Privilege program, which totaled $185,000, $81,000 and $230,000 for the same periods, respectively. On a year-to-date basis through June 30, 2003, the provision for loan losses was $1,766,000 versus $1,841,000 in 2002, of which $266,000 and $391,000, respectively, related to the Overdraft Privilege program.

When expressed as a percentage of average loans, the provision was 0.10% in both the first and second quarters of 2003 and 0.12% in the second quarter of 2002. For the six months ended June 30, the provision was 0.20% of average loans in 2003 versus 0.23% in 2002. Management believes the provisions were appropriate for the overall quality, inherent risk and volume concentrations of Peoples' loan portfolio.

Gains and/or Losses on Securities Transactions

Peoples recognized net losses on securities transactions of $29,000 for the quarter ended June 30, 2003, versus no gains or losses in 2002's second quarter. The net losses on securities transactions in 2003 were largely the result of Peoples selling $48.6 million as part of the plan to improve the performance of Peoples' investment securities portfolio. In the first half of 2003, Peoples recognized net losses of $27,000, versus net gains of $51,000 a year ago.

Non-Interest Income

Peoples generates non-interest income from six primary sources: deposit account service charges, fiduciary activities, investment and insurance commissions, electronic banking, mortgage banking and business owned life insurance ("BOLI"). For the quarter ended June 30, 2003, non-interest income was $4,282,000, up $656,000 (or 18%) from $3,626,000 for the same period last year. On a year-to-date basis, non-interest income totaled $8,217,000 through June 30, 2003, compared to $7,584,000 last year, an increase of $633,000 (or 8%). Peoples' enhanced non-interest income was primarily the result of higher deposit service charge income, with revenues from Peoples' e-banking services, mortgage banking and fiduciary activities also contributing to the increase. Compared to the first quarter of 2003, non-interest income grew $347,000 (or 9%) in the second quarter of 2003.

Peoples largest source of non-interest revenue remains service charges and other fees on deposit accounts, which are based on the recovery of costs associated with services provided. In the second quarter of 2003, deposit account service charges grew $377,000 (or 23%) to $2,052,000, from $1,675,000 in 2002's second quarter. This increase was primarily the result of higher volumes of overdraft and non-sufficient funds fees, which were up $256,000 (or 24%) and $98,000 (or 37%), respectively. An increased number of checking accounts from acquisitions and Peoples' Free Checking campaign also contributed to the increase. For the six months ended June 30, 2003, deposit account service charges totaled $3,777,000 versus $3,041,000 for the same period last year, an increase of $736,000 (or 24%), as overdraft and non-sufficient funds fees grew $504,000 (or 27%) and $201,000 (or 45%), respectively. Due in part to the Kentucky Bancshares acquisition, deposit account service charges were up $327,000 (or 19%) in the second quarter of 2003 compared to $1,725,000 in the first three months of 2003.

Peoples utilizes various electronic banking services, including ATM and debit cards, direct deposit services and Internet banking, as alternative delivery channels to traditional sales offices for providing services to clients. Peoples' electronic banking services generated revenues of $529,000 for the quarter ended June 30, 2003, up $115,000 (or 28%) from $414,000 a year ago and up $75,000 (or 17%) from $454,000 in the first quarter of 2003. These increased revenues were the result of customers using Peoples' debit cards to complete more of their payment transactions. In the second quarter of 2003, Peoples' customers used their debit cards to complete over $14 million of transactions, up from $12 million last quarter and $10 million in 2002's second quarter. For the six months ended June 30, 2003, e-banking revenues totaled $983,000, an increase of $201,000 (or 26%) compared to $782,000 in 2002, as debit card transactions exceeded $26 million in 2003 versus $19 million a year ago. Further information regarding Peoples' anticipated future electronic banking revenues can be found later in this discussion under "Future Outlook."

Starting in the second half of 2002, Peoples began selling long-term, fixed rate real estate loans into the secondary market. As a result of continuing this program during the current year, Peoples recognized mortgage banking income of $337,000 for quarter ended June 30, 2003, up from $230,000 in the prior quarter. Through six months of 2003, mortgage banking produced revenue of $567,000 versus no income in the same period last year. Prior to the third quarter of 2002, Peoples primarily originated one- to five-year adjustable rate, fully amortizing real estate loans rather than long-term, fixed rate loans due to the associated interest rate risk and, as a result, did not recognize any mortgage banking income in first six months of 2002.

Peoples' fiduciary fees totaled $858,000 in the second quarter of 2003, compared to $586,000 in the prior quarter and $640,000 in the second quarter of 2002. On a year-to-date basis, fiduciary revenues grew $188,000 (or 15%) to $1,444,000, from $1,256,000 in 2002. While the sluggish equity markets, upon which a significant portion of fiduciary fees are based, continue to challenge Peoples' fiduciary revenues, the addition of trust assets through the Kentucky Bancshares acquisition accounted for the majority of the increased revenue in the second quarter.

Insurance and investment commissions totaled $320,000 in the second quarter of 2003 compared to $462,000 a year ago, a decrease of $142,000 (or 31%). Compared to the first quarter of 2003, insurance and investment commissions were down $122,000 (or 28%) in the second quarter, from $442,000. For the six months ended June 30, insurance and investment commissions were $762,000 in 2003 versus $986,000 in 2002, a decline of $224,000 (or 23%). The lower level of insurance and investment income is largely attributable to lower volumes of fixed annuity sales and related commission income. The following table details Peoples' insurance and investment commissions for the periods indicated:

	Three Months Ended June 30,		Six Months Ended June 30,	
(Dollars in thousands)	2003	2002	2003	2002
Property and casualty insurance	$112	$93	$203	$178
Fixed annuities	77	222	294	502
Brokerage	50	61	94	128
Life and health insurance	42	30	101	83
Credit life and A&H insurance	39	56	70	95
Total	$320	$462	$762	$986

Peoples' BOLI investment enhances operating efficiency by offsetting rising employee benefit costs. In the second quarter of 2003, BOLI income totaled $353,000 versus $365,000 last quarter and $376,000 a year ago. For the six months ended June 30, 2003, BOLI produced income of $718,000 compared to $701,000 for the same period in 2002.

Non-Interest Expense

In the second quarter of 2003, non-interest expense totaled $10,042,000, up $1,493,000 (or 17%) from $8,549,000 a year ago, due largely to acquisitions and strategic investments in technology. Compared to the first quarter of 2003, non-interest expense increased $338,000 (or 3%) in the second quarter, from $9,704,000. The majority of this increase was due to higher levels of salaries and benefits and marketing costs, which were both up $103,000.

Salaries and benefits remain Peoples' largest non-interest expense, which is inherent in a service-based industry such as financial services. For the quarter ended June 30, 2003, salaries and benefits totaled $4,827,000 compared to $4,346,000 the prior year and $4,724,000 for the first quarter of 2003, increases of $481,000 (or 11%) and $103,000 (or 2%), respectively. In the first half of 2003, salaries and benefits grew $721,000 (or 8%) to $9,551,000, from $8,830,000 for the first six months of 2002. The majority of these increases were due to the addition of new associates in conjunction with acquisitions. At June 30, 2003, Peoples had 486 full-time equivalent associates, up from 451 at March 31, 2003 and 447 a year ago. Management will continue to leverage Peoples' resources in an effort to optimize customer service and produce additional future revenue streams.

Net occupancy and equipment expenses increased $168,000 (or 18%) in the second quarter of 2003, totaling $1,108,000 versus $940,000 last year. For the six months ended June 30, 2003, net occupancy and equipment expenses totaled $2,206,000, up $340,000 (or 18%) from $1,866,000 a year ago. Recent investments in technology and acquisitions produced additional expenses, including depreciation expense. The continued investment in technology has enhanced Peoples' ability to serve clients and satisfy their financial needs, while acquisitions have allowed Peoples to expand its customer base. Compared to the first quarter of 2003, net occupancy and equipment expense was virtually unchanged.

Professional fees, which include fees for accounting, legal and other professional services, totaled $499,000 in the second quarter of 2003, down $83,000 (or 14%) compared to last year but up $57,000 (or 13%) from $442,000 last quarter. In the second quarter of 2003, Peoples incurred additional legal expenses, due in part to management implementing various provisions of the Sarbanes-Oxley Act of 2002. These additional costs were offset by a reduction in the consulting fees Peoples paid during the quarter for the implementation of the Overdraft Privilege program. These fees, which are based on the net improvement in overdraft fees, were $112,000 in the second quarter of 2003 versus $155,000 in the second quarter of 2002 and $152,000 in the first quarter of 2003, as the percentage paid was reduced beginning in March 2003. Through six months of 2003, professional fees were $941,000 compared to $883,000 for the first half of 2002, an increase of $58,000 (or 7%).

Marketing expense was $379,000 for the three months ended June 30, 2003, compared to $150,000 for the same period in 2002, an increase of $229,000 (or 153%). Compared to the first quarter of 2003, marketing expense grew $103,000 (or 37%) in the second quarter, from $276,000. In the first half of 2003, Peoples advertised its newly created Peoples Financial Advisors division and Freedom Checking product. While these initiatives resulted in higher marketing expenses, management believes they will allow Peoples to attract many new clients and, as a result, improve revenues.

In the second quarter of 2003, intangible amortization expense was up $159,000 (or 142%) to $271,000, from $112,000 last year. Compared to the prior quarter, intangible amortization was up $70,000 (or 35%) from $201,000. For the six months ended June 30, intangible amortization was $472,000 in 2003 versus

$223,000 in 2002. These increases were due to recent acquisitions. Intangible amortization expense for the three and six months ended June 30, 2002, also reflects the adoption of SFAS 147 and restatement of goodwill relating to qualifying branch acquisitions.

State franchise taxes totaled $272,000 in the second quarter of 2003, up $94,000 (or 53%) from $178,000 a year ago. On a year-to-date basis, franchise taxes increased $169,000 (or 47%) in 2003, totaling $529,000 versus $360,000 in first half of 2002. These increases were a result of additional equity at Peoples Bank, the primary basis for these taxes.

Management uses the non-interest income leverage ratio as a measurement of non-interest expense leverage. The ratio, defined as non-interest income as a percentage of operating expenses, excludes gains and losses on securities transactions and asset disposals, as well as intangible asset amortization. For the six months ended June 30, 2003, the non-interest income leverage ratio was 44.0% compared to 40.7% a year ago. In the second quarter of 2003, the non-interest income leverage ratio improved to 46.5% from 41.4% for the prior quarter and 43.1% for 2002's second quarter. Peoples' sales associates will strive to generate new revenues and leverage operating expenses through a needs-based selling approach in order to achieve a long-term target non-interest income leverage ratio of 50%.

As a result of Peoples adopting the reporting requirements of SFAS 150 on July 1, 2003, as required, Peoples will recognize approximately $1.2 million of interest expense on its Trust Preferred Securities in the final six months of 2003 that would have otherwise been recognized as non-interest expense had SFAS 150 not been in effect. Had SFAS 150 been in effect for the first six months of 2003, Peoples' non-interest leverage and efficiency ratios would have been 46.9% and 50.4%, respectively, versus 44.0% and 51.9% actually reported.

Return on Equity

In the second quarter of 2003, Peoples' return on equity ("ROE") was 12.92% versus 13.00% last quarter and 18.85% a year ago. On a year-to-date basis, ROE was 12.95% in 2003, down from 19.10% in the first half of 2002. The lower ROE is primarily the result of higher average equity generated by the Common Stock Offering, the Kentucky Bancshares acquisition, increased earnings and improvements in the net unrealized value of Peoples' available-for-sale investment securities portfolio. While ROE remains a key part of the evaluation of Peoples' long-term performance, management believes earnings per share ("EPS") serves as a more meaningful measurement of short-term performance due to the impact of changing market valuations in the investment portfolio.

Return on Assets

Return on assets ("ROA") was 1.25% for the quarter ended June 30, 2003, compared to 1.27% and 1.54% for the first quarter of 2003 and second quarter of 2002, respectively. Through six months of 2003, ROA was 1.26% versus 1.55% for the same period in 2002. The reduction in ROA is due to the increase in total average assets resulting from the Investment Growth Strategy and acquisitions. In recent years, Peoples' primary focus has shifted to EPS enhancement and ROE while reducing the emphasis on ROA as a key performance indicator. However, management continues to monitor ROA and considers it a measurement of Peoples' asset utilization.

Income Tax Expense

Peoples' effective tax rate was 28.0% for the six months ended June 30, 2003, compared to 28.3% for the same period in 2002. Peoples continues to make tax-advantaged investments in order to manage its effective tax rate and overall tax burden. At June 30, 2003, the amount of tax-advantaged investments included in Other Assets totaled $29.8 million compared to $28.5 million at June 30, 2002. Depending on economic and regulatory conditions, Peoples may make additional investments in various tax credit pools and other tax-advantaged assets.

FINANCIAL CONDITION

Overview of Balance Sheet

At June 30, 2003, total assets were $1.86 billion compared to $1.39 billion at year-end 2002, an increase of $465.7 million (or 34%). During the second quarter of 2003, total assets grew $191.4 million (or 11%), due primarily to the Kentucky Bancshares acquisition. The Investment Growth Strategy contributed to the increase in assets since the prior year-end, as investment securities totaled $689.7 million at June 30, 2003, up $277.6 million (or 67%) since December 31, 2002. Gross loans were $916.6 million June 30, 2003, up $65.7 million (or 8%) since December 31, 2002.

Total liabilities were $1.65 billion at June 30, 2003, compared to $1.22 billion at year-end 2002, an increase of $434.5 million (or 36%). At June 30, 2003, deposits totaled $1.14 billion versus $955.9 million at year-end, an increase of $187.5 million (or 20%). This increase was primarily the result of deposits acquired in the Kentucky Bancshares acquisition. Borrowed funds totaled $499.0 million at June 30, 2003, up from $252.0 million at December 31, 2002 due to additional borrowings which funded the Investment Growth Strategy.

Stockholders' equity totaled $178.3 million at June 30, 2003, versus $147.2 million at December 31, 2002, an increase of $31.1 million (or 21%). The majority of this increase is due to common shares issued in conjunction with the Kentucky Bancshares acquisition and Common Stock Offering, which increased equity by $19.1 million, while Peoples' earnings, net of dividends paid, was also a significant contributor.

Cash and Cash Equivalents

Peoples considers cash and cash equivalents to consist of Federal funds sold, cash and balances due from banks, interest-bearing balances in other institutions and other short-term investments that are readily liquid. The amount of cash and cash equivalents fluctuates on a daily basis due to client activity and Peoples' liquidity needs. At June 30, 2003, cash and cash equivalents totaled $155.2 million, up $99.6 million (or 179%) compared to $55.6 million at December 31, 2002, attributable to a higher level of Federal funds sold. At June 30, 2003, Peoples had Federal funds sold of $93.5 million, compared to $20.5 million at December 31, 2002, an increase of $73.0 million. This increase was the result of Peoples holding $60 million of funds at quarter-end relating to the liquidation of a trust relationship associated with the Kentucky Bancshares acquisition. In early July, these funds were transferred to another fiduciary by the customer, resulting in cash and cash equivalents to return to normal levels. A further discussion of this transaction can be found later in this discussion under "Funding Sources."

Management believes the current balance of cash and cash equivalents, along with the availability of other funding sources, should allow Peoples to meet cash obligations, special needs and off-balance sheet commitments, specifically undrawn lines of credit, construction loans and letters of credit, as they come due. Peoples will actively manage the principal runoff from the investment and loan portfolios and seek to reinvest those funds appropriately, based on loan demand and investment opportunities, while maintaining adequate liquidity. Further information regarding Peoples' liquidity can be found later in this discussion under "Interest Rate Sensitivity and Liquidity."

Investment Securities

At June 30, 2003, the amortized cost of Peoples' investment securities totaled $671.8 million compared to $402.0 million at year-end 2002, while the market value of the investment portfolio was $689.7 million at June 30, 2003, up from $412.1 million at December 31, 2002. These increases were primarily the result of the Investment Growth Strategy initiated in December 2002 and implemented in the first quarter of 2003.

The difference in amortized cost and market value at June 30, 2003, resulted in unrealized appreciation in the investment portfolio of $17.9 million and a corresponding increase in Peoples' equity of $11.5 million, net of deferred taxes. In comparison, the difference in amortized cost and market value at December 31, 2002, resulted in unrealized appreciation of $10.1 million and an increase in equity of $6.4 million, net of deferred taxes.

Since December 31, 2002, Peoples' investment in US treasury securities and obligations of US government agencies and corporations has grown $38.1 million (or 133%), as management reinvested a portion of the runoff from the investment portfolio to maintain diversity within the portfolio. In addition, Peoples' investment in mortgage-backed securities has grown significantly compared to year-end 2002 due to the Investment Growth Strategy. The following table details Peoples' investment portfolio, at estimated fair value:

(Dollars in thousands)	June 30, 2003	March 31, 2003	December 31, 2002	June 200
US Treasury securities and obligations of US government agencies and corporations	$ 66,714	$ 41,638	$ 28,647	$ 33,5
Obligations of states and political subdivisions	68,841	67,088	67,806	67,2
Mortgage-backed securities	493,556	522,469	259,811	214,7
Other securities	60,569	57,155	55,836	51,8
Total available-for-sale securities	$ 689,680	$ 688,350	$ 412,100	$ 367,4

Management monitors the earnings performance and liquidity of the investment portfolio on a regular basis through Asset/Liability Committee ("ALCO") meetings. The ALCO also monitors net interest income, sets deposit pricing and maturity guidelines, and manages Peoples' interest rate risk. Through active management of the balance sheet and investment portfolio, Peoples seeks to maintain sufficient liquidity to satisfy depositor demand, other company liquidity requirements and various credit needs of its customers.

Loans

Peoples Bank originates various types of loans, including commercial, financial and agricultural loans ("commercial loans"), real estate loans (both commercial and residential) and consumer loans, focusing primarily on lending opportunities in central and southeastern Ohio, northwestern West Virginia, and northeastern Kentucky markets. At June 30, 2003, gross loans totaled $916.6 million, up $65.7 million since year-end 2002. While this increase is primarily attributable to loans acquired in the Kentucky Bancshares acquisition, Peoples also experienced internally generated commercial loan growth, which partially offset declines in real estate and consumer loan balances. The following table details total outstanding loans:

(Dollars in thousands)	June 30, 2003	March 31, 2003	December 31, 2002	June 30, 2002
Commercial, financial, and agricultural	$ 475,600	$ 422,782	$ 392,528	$ 379,243
Real estate, construction	10,339	10,523	16,231	15,782
Real estate, mortgage	329,708	324,877	331,948	345,795
Consumer	94,549	96,857	103,635	115,398
Credit cards	6,407	6,065	6,549	6,159
Total loans	$ 916,603	$ 861,104	$ 850,891	$ 862,377

Commercial loan balances, including loans secured by commercial real estate, totaled $475.6 million at June 30, 2003, up $83.1 million (or 21%) from $392.5 million at year-end 2002. While the majority of the increase in commercial loans is attributable to acquiring $49 million of loans in the Kentucky Bancshares acquisition, Peoples also experienced internally generated growth from lending opportunities within Peoples' existing markets. Commercial loans continued to represent the largest portion of Peoples' total loan portfolio, comprising 51.9% and 46.1% of total loans at June 30, 2003 and December 31, 2002, respectively. The portion of commercial loan balances secured by commercial real estate, excluding construction loans, was $353.8 million at June 30, 2003, up from $289.6 million at December 31, 2002. Future commercial lending activities will be dependent on economic and related conditions, such as general demand for loans in Peoples' primary markets, interest rates offered by Peoples and normal underwriting requirements. In addition to in-market opportunities, Peoples will continue to selectively lend to creditworthy customers outside its primary markets.

Real estate loans, which include construction loans but exclude loans secured by commercial real estate, totaled $340.0 million at the end of the second quarter of 2003 compared to $348.2 million at December 31, 2002, a decrease of $8.2 million (or 2%). Real estate loan balances have declined in response to customer demand for long-term, fixed-rate mortgages, which are sold in the secondary market with servicing rights retained. Peoples acquired $21 million of real estate loans in the Kentucky Bancshares acquisition, partially offsetting the decline resulting from Peoples' increased secondary market activity. Real estate loans comprised 37.1% of Peoples' total loan portfolio at June 30, 2003, versus 40.9% at year-end 2002. Included in real estate loans are home equity credit line ("Equiline") balances of $29.1 million at June 30, 2003, up from $28.5 million at December 31, 2002. Management believes Equiline loans are a relationship product with an acceptable return on investment after risk considerations. Residential real estate loans continued to represent a major focus of Peoples' lending due to the lower risk factors associated with this type of loan, and the opportunity to provide additional products and services to these consumers.

Excluding credit card balances, consumer loans decreased $9.1 million (or 9%) since year-end 2002, totaling $94.5 million at June 30, 2003. Excluding loans acquired as part of the Kentucky Bancshares acquisition, consumer loan balances were down $13.8 million (or 13%) since December 31, 2002. The indirect lending area represented the majority of Peoples' consumer loans, with balances of $46.9 million and $56.2 million at June 30, 2003 and December 31, 2002, respectively. While sluggish economic conditions and strong competition for loans, particularly automobile loans, have challenged the performance and growth of Peoples' consumer loan portfolio, management remains committed to sound lending practices and continues to emphasize appropriate discipline in loan pricing and loan underwriting practices more than loan growth.

At June 30, 2003, Peoples' credit card balances totaled $6.4 million, down slightly since December 31, 2002. Peoples' ability to grow credit card balances is impacted by fierce competition for customers. Since management does not intend to subject Peoples to additional and/or unnecessary risk merely for such growth, Peoples continues to market its credit card as a complementary product offering for client relationships.

Loan Concentration

Peoples' largest concentration of commercial loans are credits to assisted living facilities and nursing homes, which comprised 12.2% of Peoples' outstanding commercial loans at June 30, 2003, versus 13.4% at year-end 2002. Loans to lodging and lodging-related companies also represented a significant portion of Peoples' commercial loans comprising approximately 11.8% of Peoples' outstanding commercial loans at quarter-end, compared to 11.2% at December 31, 2002.

These lending opportunities have arisen due to the growth of these industries in markets served by Peoples or contiguous areas, as well as sales associates' efforts to develop these lending relationships. Management believes Peoples' loans to assisted living facilities and nursing homes, as well as loans to lodging and lodging-related companies, do not pose abnormal risk when compared to risk assumed in other types of lending since these credits have been subjected to Peoples' normal underwriting standards. In addition, a sizeable portion of the loans to lodging and lodging-related companies are spread over various geographic areas and are guaranteed by principals with substantial net worth. Peoples also requires the owners in these business relationships to possess market expertise and experience.

Allowance for Loan Losses

Peoples' allowance for loan losses totaled $14.2 million, or 1.54% of total loans, at June 30, 2003, compared to $13.1 million, or 1.54%, at year-end 2002. The following table presents changes in Peoples' allowance for loan losses:

	Three Months Ended June 30,		Six Months Ended June 30,	
(Dollars in thousands)	2003	2002	2003	2002
Balance, beginning of period	$ 13,363	$ 12,426	$ 13,086	$ 12,
Chargeoffs	(955)	(1,147)	(1,740)	(2,
Recoveries	235	164	466	
Net chargeoffs	(720)	(983)	(1,274)	(1,
Provision for loan losses	935	980	1,766	1,
Allowance for loan losses acquired	573	-	573	
Balance, end of period	$ 14,151	$ 12,423	$ 14,151	$ 12,

The allowance is allocated among the loan categories based upon the consistent, quarterly procedural discipline described in the "Critical Accounting Policies" section of this discussion. However, the entire allowance for loan losses is available to absorb future loan losses in any loan category. The following details the allocation of the allowance for loan losses:

(Dollars in thousands)	June 30, 2003	December 31, 2002	June 30, 2002
Commercial	$ 10,387	$ 8,846	$ 7,5
Consumer	1,820	2,075	2,5
Real estate	1,482	1,617	1,7
Credit cards	256	342	4
Overdrafts	206	206	1
Total allowance for loan losses	$ 14,151	$ 13,086	$ 12,4

The allowance allocated to commercial loans has increased in recent periods, reflecting the higher credit risk associated with this type of lending and the continued growth in this portfolio. The allowance allocated to the real estate and consumer loan portfolios is based upon Peoples' allowance methodology for homogeneous loans, which includes a consideration of changes in total balances in those portfolios.

In the second quarter of 2003, net loan chargeoffs were $720,000 compared to $983,000 a year ago and $554,000 in the first quarter of 2003. While commercial and consumer loans, including overdraft chargeoffs, comprise the largest portion of net chargeoffs, the lower level of chargeoffs in the second quarter of 2003 is attributable to fewer troubled commercial loans. In addition, commercial loan chargeoffs were impacted by Peoples charging down a group of loans in single client relationship totaling $697,000 and $341,000 in the second and first quarters of 2002, respectively. The following table details Peoples' net chargeoffs:

	Three Months Ended June 30,		Six Months Ended June 30,	
(Dollars in thousands)	2003	2002	2003	2002
Commercial	$ 210	$ 690	$ 396	$ 1,
Consumer	189	68	389	
Overdrafts	150	147	267	
Real estate	128	41	136	
Credit card	43	37	86	
Total	720	983	1,274	1,
As a percent of average loans	$ 0.08%	$ 0.12%	$ 0.15%	$ 0.

Asset quality remains a key focus, as management continues to stress quality rather than growth. Since December 31, 2002, Peoples' asset quality has improved due to the combination of a lower level of nonperforming loans and an increase in assets. The following table details Peoples' nonperforming assets:

(Dollars in thousands)	June 30, 2003	March 31, 2003	December 2002
Loans 90+ days past due and accruing	$ 569	$ 337	$
Renegotiated loans	685	685	
Nonaccrual loans	4,389	3,741	
Total nonperforming loans	5,643	4,763	
Other real estate owned	960	924	
Total nonperforming assets	$ 6,603	$ 5,687	$
Nonperforming loans as a percent of total loans	0.62%	0.55%	
Nonperforming assets as a percent of total assets	0.35%	0.34%	

In the first half of 2003, the balance of nonperforming loans declined as a large commercial loan, comprising the entire amount of renegotiated loans at December 31, 2002, moved to performing status. In addition, a large commercial loan on nonaccrual status moved into other real estate owned ("OREO") in the first quarter of 2003, which also accounted for the majority of the increase in OREO. Nonperforming assets comprise a smaller percentage of total assets at June 30, 2003, as a result of an increase in assets largely attributable to the completion of the Investment Growth Strategy and the Kentucky Bancshares acquisition. While the increase in nonperforming loans in the second quarter of 2003 was due mainly to loans acquired in the Kentucky Bancshares acquisition, Peoples has recorded valuation reserves to absorb any probable losses from these acquired loans.

A loan is considered impaired when, based on current information and events, it is probable that Peoples will be unable to collect the scheduled payments of principal or interest according to the contractual terms of the loan agreement. The measurement of potential impaired loan losses is generally based on the present value of expected future cash flows discounted at the loan's historical effective interest rate, or the fair value of the collateral if the loan is collateral dependent. If foreclosure is probable, impairment loss is measured based on the fair value of the collateral.

At June 30, 2003, the recorded investment in loans that were considered to be impaired was $12.9 million, of which $10.1 million were accruing interest, and $2.8 million were nonaccrual loans. Included in this amount were $2.3 million of impaired loans for which the related allowance for loan losses was $794,000. The remaining impaired loan balances do not have a related allocation of the allowance for loan losses because the loans have been previously written-down, are well secured, or possess characteristics indicative of the ability to repay the loan. For the six months ended June 30, 2003, Peoples' average recorded investment in impaired loans was approximately $11.1 million and interest income of $332,000 was recognized on impaired loans during the period, representing 0.7% of Peoples' total interest income.

Funding Sources

Peoples considers a number of sources when evaluating funding needs, including but not limited to deposits, short-term borrowings, and long-term borrowings. Deposits, both interest-bearing and non-interest bearing, continue to be the most significant source of funds for Peoples, totaling $1.14 billion, or 70% of total funding sources, at June 30, 2003.

Non-interest bearing deposits serve as a core funding source. At June 30, 2003, non-interest bearing deposit balances totaled $196.6 million, up $80.7 million (or 70%) compared to the prior year-end, with the Kentucky Bancshares acquisition accounting for $19 million of the increase. In addition, Peoples also acquired a trust relationship in this merger that was in the process of being transferred to a successor fiduciary at the direction of the client. The timing of the liquidation resulted in Peoples holding $60 million of non-interest bearing deposits on June 30, 2003. On July 1, non-interest bearing deposits returned to normal levels as these trust funds were transferred to the new fiduciary. Since this transaction caused a temporary increase in balances at June 30, 2003, management believes a comparison of average balances to be a more meaningful reflection of the trend in non-interest bearing deposits. In the second quarter of 2003, non-interest bearing deposits averaged $125.9 million versus $108.3 million in the first quarter of 2003, an increase of $17.6 million (or 16%).

Interest-bearing deposits totaled $946.8 million at June 30, 2003, an increase of $106.8 million (or 13%) compared to $840.0 million at December 31, 2002. In the second quarter, Peoples acquired interest-bearing deposits of $95 million as part of the Kentucky Bancshares acquisition. The following details Peoples' interest-bearing deposits:

(Dollars in thousands)	June 30, 2003	March 31, 2003	December 31, 2002
Certificates of deposit	$ 479,068	$ 420,817	$ 422,715
Savings accounts	181,408	169,120	143,594
Interest-bearing transaction accounts	167,846	143,656	139,609
Money market deposit accounts	118,521	122,578	134,052
Total loans	$ 946,843	$ 856,171	$ 839,970

Peoples also accesses other funding sources, including short-term and long-term borrowings, to fund asset growth and satisfy liquidity needs. Peoples' short-term borrowings include overnight repurchase agreements and FHLB advances, while long-term borrowings include 10-year FHLB advances, a loan from an unrelated financial institution and term repurchase agreements. The majority of the long-term FHLB advances are convertible rate advances, with the initial rate fixed for periods ranging from two to four years, depending on the specific advance. After the initial fixed rate period, these advances have the opportunity, at the discretion of the FHLB, to convert to a LIBOR based, variable rate product. Peoples has the option to prepay any converted advance without penalty or allow the borrowing to reprice. In addition to these convertible rate advances, recent long-term FHLB advances have included fixed rate, amortizing advances, which have helped Peoples manage its interest rate sensitivity. Further information regarding Peoples' management of interest rate sensitivity can be found later in this discussion under "Interest Rate Sensitivity and Liquidity."

At June 30, 2003, long-term borrowings totaled $456.1 million, up $252.3 million (or 124%) from $203.8 million at December 31, 2002, with this increase largely the result of the Investment Growth Strategy. In addition, Peoples converted a $17 million short-term loan utilized to fund an acquisition in 2002 to a long-term loan with the same unaffiliated financial institution. As a result, short-term borrowings decreased $5.4 million to $42.8 million, compared to $48.2 million at year-end 2002.

Capital/Stockholders' Equity

At June 30, 2003, stockholders' equity was $178.3 million, versus $147.2 million at December 31, 2002, an increase of $31.1 million (or 21%). The majority of this increase is due to common shares issued in conjunction with the Kentucky Bancshares acquisition and Peoples' earnings, net of dividends paid, which accounted for $14.3 million and $7.4 million of the increase, respectively.

For the six months ended June 30, 2003, Peoples paid dividends of $3.1 million, representing a dividend payout ratio of 29.5% of earnings, compared to a ratio of 24.1% a year ago. While management anticipates Peoples continuing its 37-year history of consistent dividend growth in future periods, Peoples Bancorp's ability to pay dividends on its common shares is largely dependent upon dividends from Peoples Bank. Additionally, Peoples Bancorp has established two trust subsidiaries to issue preferred securities. If Peoples Bancorp suspends interest payments relating to the trust preferred securities issued by either of the two trust subsidiaries, Peoples will be prohibited from paying dividends on its common shares. Peoples Bancorp or Peoples Bank may decide to limit the payment of dividends, even when the legal ability to pay them exists, in order to retain earnings for other strategic purposes.

The adjustment for the net unrealized holding gains on available-for-sale securities, net of deferred income taxes, impacts Peoples' total equity. At June 30, 2003, net unrealized holding gains totaled $11.5 million versus $6.4 million at December 31, 2002, a change of $5.1 million. Since all the investment securities in Peoples' portfolio are classified as available-for-sale, both the investment and equity sections of Peoples' consolidated balance sheet are more sensitive to the changing market values of investments than if the investment portfolio was classified as held-to-maturity.

At June 30, 2003, Peoples had treasury stock totaling $1.1 million, unchanged from year-end 2002. In the first half of 2003, Peoples repurchased 40,000 common shares (or 13% of the total authorized), at an average price of $22.04 per share, under the 2003 Stock Repurchase Program and 1,923 common shares, at an average price of $23.94, as part of the deferred compensation plan for directors of Peoples Bancorp and Peoples Bank. The shares purchased under the 2003 Stock Repurchased Program were reissued in the Kentucky Bancshares acquisition and stock option exercises. Peoples anticipates repurchasing additional common shares under the 2003 Stock Repurchase Program and for the deferred compensation plan.

In addition to monitoring performance through traditional capital measurements (i.e., dividend payout ratios and ROE), Peoples has also complied with the capital adequacy standards mandated by the banking industry. Bank regulators have established "risk-based" capital requirements designed to measure capital adequacy. Risk-based capital ratios reflect the relative risks of various assets banks hold in their portfolios. A risk-weight category of 0% (lowest risk assets), 20%, 50% or 100% (highest risk assets) is assigned to each asset on the balance sheet. At June 30, 2003, Peoples' Total Capital, Tier 1 and Leverage ratios were 15.34%, 13.87% and 8.80%, respectively, exceeding the well-capitalized standards of 10%, 6% and 5%, respectively. In addition, all three risk-based capital ratios for Peoples Bank were also well above the minimum standards for a well-capitalized institution at June 30, 2003.

Interest Rate Sensitivity and Liquidity

While Peoples is exposed to various business risks, the risks relating to interest rate sensitivity and liquidity could materially impact its future results of operation and financial condition. The objective of Peoples' asset/liability management ("ALM") function is to measure and manage these risks in order to optimize net interest income within the constraints of prudent capital adequacy, liquidity and safety. This objective requires Peoples to focus on interest rate risk exposure and adequate liquidity as it manages the mix of assets and liabilities. Ultimately, the ALM function is intended to guide management in the acquisition of earning assets and selection of the appropriate funding sources.

Interest Rate Risk

Interest rate risk ("IRR") is one of the most significant risks for Peoples, and the entire financial services industry, primarily arising in the normal course of business of offering a wide array of financial products to its customers, including loans and deposits. IRR is the potential for economic loss due to future interest rate changes that can impact both the earnings stream as well as market values of financial assets and liabilities. Peoples' exposure to IRR is primarily due to differences in the maturity, or repricing, of earning assets and interest-bearing liabilities. In addition, other factors, such as prepayments of loans and investment securities or early withdrawal of deposits, can expose Peoples to IRR and increase interest costs or reduce revenue streams.

Peoples has charged the ALCO with the overall management of Peoples' balance sheet mix and off-balance sheet hedging transactions related to the management of IRR. It is the ALCO's responsibility to keep Peoples focused on the future by evaluating trends and potential future events, researching alternatives, then recommending and authorizing an appropriate course of action. To this end, the ALCO has established an IRR management policy that sets the minimum requirements and guidelines for monitoring and managing the level and amount of IRR. The objective of the IRR policy is to encourage management to adhere to sound fundamentals of banking while allowing sufficient flexibility to exercise the creativity and innovations necessary to meet the challenges and opportunities of changing markets. The ultimate goal of these policies is to optimize net interest income within the constraints of prudent capital adequacy, liquidity, and safety.

Peoples' ALCO relies on different methods of assessing IRR, including simulations to project future net interest income and to monitor the sensitivity of the net present market value of equity and the difference, or "gap", between maturing or rate-sensitive assets and liabilities over various time periods. Peoples uses these methods to monitor IRR for both the short- and long-term. The ALCO places emphasis on simulation modeling as the most beneficial measurement of IRR because it is a dynamic measure. By employing a simulation process that estimates the impact of potential changes in interest rates and balance sheet structures and by establishing limits on these estimated changes to net income and net market value, the ALCO is better able to evaluate interest rate risks and their potential impact to earnings and market value of equity.

The modeling process starts with a base case simulation using the current balance sheet and current interest rates held constant for the next twelve months. At least two alternative interest rate scenarios, one with higher interest rates and one with lower interest rates, assuming parallel, immediate and sustained changes are also prepared using the same balance sheet structure as the base scenario. Comparisons produced from the simulation data, showing the earnings variance from the base interest rate scenario, illustrate the risks associated with the current balance sheet structure. Additional simulations, when deemed appropriate, are prepared using different interest rate scenarios than those used with the base case simulation and/or possible changes in balance sheet structure. The additional simulations are used to better evaluate risks and highlight opportunities inherent in the modeled balance sheet. Comparisons showing the earnings and equity value variance from the base case are provided to the ALCO for review and discussion. The results from these model simulations are evaluated for indications of effectiveness of current IRR management strategies.

As part of the evaluation of IRR, the ALCO has established limits on changes in net interest income and the net value of the balance sheet. The ALCO limits the decrease in net interest income of Peoples Bank to 10% or less from base case for each 100 basis point shift in interest rates measured over a twelve-month period assuming a static balance sheet. The ALCO limits the negative impact on net equity value to 40% or less given an immediate and sustained 200 basis points shift in interest rates also assuming a static balance sheet. The ALCO also reviews static gap measures for specific time periods focusing on a one-year cumulative gap. At June 30, 2003, Peoples' one-year cumulative gap amount was positive 13.6% of earning assets, which represented $231.3 million more in assets than liabilities that may reprice during that period. Based on historical trends and performance, the ALCO has determined the ratio of the one-year cumulative gap should be within +/-15% of earning assets. Results that are greater than any of these limits will prompt a discussion by the ALCO of appropriate actions, if any, that should be taken.

The following table is provided to illustrate the estimated earnings at risk and value at risk positions of Peoples, on a pre-tax basis, at June 30, 2003 (dollars in thousands):

Immediate Interest Rate Increase (Decrease) in Basis Points	Estimated (Decrease) Increase In Net Interest Income		Estimated (Decrease) Increase in Economic Value of Equity	
300	$ 2,012	3.7 %	$ (66,567)	(27.6) %
200	1,436	2.6	(44,659)	(18.5)
100	748	1.4	(22,207)	(9.2)
(50)	$ (433)	(0.8) %	$ 12,929	5.4 %

The interest rate risk analysis shows that Peoples is asset sensitive, which means that increasing interest rates should favorably impact Peoples' net interest income while downward moving interest rates should negatively impact net interest income. Peoples' asset sensitivity increased in the second quarter of 2003 due to the Kentucky Bancshares acquisition; however, the ALCO believes it is to the long-term benefit of Peoples to maintain an asset sensitive position. The interest rate analysis also shows Peoples is within the established IRR policy limits for all simulations and all scenarios for the current period.

The ALCO has implemented hedge positions to help protect Peoples' net interest income streams in the event of rising rates which will complement the current slightly asset sensitive position. Peoples has a hedge position on a $17 million long-term, fixed-rate borrowing from the FHLB that may convert to a variable rate, at the FHLB's discretion. In addition, the ALCO may consider additional hedging options for Peoples' variable rate liabilities, including, but not limited to, the purchase of other interest rate hedge positions, as available and appropriate, that would provide net interest income protection in a rising rate environment.

Liquidity

In addition to IRR management, a primary objective of the ALCO is the maintenance of a sufficient level of liquidity. The ALCO defines liquidity as the ability to meet anticipated and unanticipated operating cash needs, loan demand, and deposit withdrawals, without incurring a sustained negative impact on profitability. The ALCO's liquidity management policy sets limits on the net liquidity position of Peoples and the concentration of non-core funding sources, both total wholesale funding and reliance on brokered deposits.

Typically, the main source of liquidity for Peoples is deposit growth. Liquidity is also provided from cash generated from earning assets such as maturities, calls, principal payments and income from loans and investment securities. In the first half of 2003, cash provided by financing activities totaled $319.0 million compared to $26.9 million a year ago, due largely to increased long-term borrowings used for the Investment Growth Strategy. Cash used in investing activities totaled $230.8 million versus $39.6 million last year, primarily due to increased investment securities purchases, net of maturities and sales.

When appropriate, Peoples takes advantage of external sources of funds, such as advances from the FHLB, national market repurchase agreements, and brokered funds. These external sources often provide attractive interest rates and flexible maturity dates that better enable Peoples to match funding dates and pricing characteristics with contractual maturity dates and pricing parameters of earning assets. At June 30, 2003, Peoples had available borrowing capacity of approximately $92 million through these external sources and unpledged securities in the investment portfolio of approximately $306 million that can be utilized as an additional source of liquidity.

The net liquidity position of Peoples is calculated by subtracting volatile funds from liquid assets. Peoples' volatile funds consist primarily of short-term growth in deposits, while liquid assets includes short-term investments and unpledged available-for-sale securities. At June 30, 2003, Peoples' net liquidity position was $298.2 million, or 16.0% of total assets, compared to $189.7 million, or 13.6% of total assets, at December 31, 2002. The increase in liquidity position as a percent of total assets was primarily the result of additional liquid assets from the higher level of cash and cash equivalents at quarter end. The liquidity position as of June 30, 2003, was within Peoples' policy limit of negative 10% of total assets. At June 30, 2003, total wholesale funding comprised 25.4% of total assets and brokered funds were 0.5% of total assets, which was within Peoples' policy limits of 30% and 10%, respectively.

Off-Balance Sheet Activities and Contractual Obligations

Peoples routinely engages in activities that involve, to varying degrees, elements of risk that are not reflected in whole or in part in the consolidated financial statements. These activities are part of Peoples' normal course of business and include traditional off-balance sheet credit-related financial instruments, interest rate contracts, operating leases, long-term debt and commitments to make additional capital contributions in low-income housing project investments.

Traditional off-balance sheet credit-related financial instruments are primarily commitments to extend credit, and standby letters of credit. These activities could require Peoples to make cash payments to third parties in the event certain specified future events occur. The contractual amounts represent the extent of Peoples' exposure in these off-balance sheet activities. However, since certain off-balance sheet commitments, particularly standby letters of credit, are expected to expire or be only partially used, the total amount of commitments does not necessarily represent future cash requirements. These activities are necessary to meet the financing needs of customers. The following table details the total contractual amount of loan commitments and standby letters of credit:

(Dollars in thousands)	June 30, 2003	March 31, 2003	December 31, 2002	June 30, 2002
Loan commitments	$ 119,316	$ 114,342	$ 103,462	$ 93,355
Standby letters of credit	9,606	7,799	7,632	7,570
Unused credit card limits	22,469	22,447	21,216	21,338

Peoples also enters into interest rate contracts where Peoples is required to either receive cash from or pay cash to counter parties depending on changes in interest rates. Peoples utilizes interest rate contracts to help manage the risk of changing interest rates.
At June 30, 2003, Peoples held interest rate contracts with notional amounts totaling $37 million and fair values totaling $288,000. Interest rate contracts are carried at fair value on the consolidated balance sheet, with the fair value representing the net present value of expected future cash receipts or payments based on market interest rates as of the balance sheet date. As a result, the amounts recorded on the balance sheet at June 30, 2003, do not represent the amounts that may ultimately be paid or received under these contracts.

Peoples also has commitments to make additional capital contributions in low-income housing tax funds, consisting of a pool of low-income housing projects. As a limited partner in these funds, Peoples receives Federal income tax benefits which assists Peoples in managing its overall tax burden. At June 30, 2003, these commitments approximated $9.7 million, with approximately $2.1 million expected to be paid over the next twelve months. Management may make additional investments in various tax credit funds.

Management does not anticipate Peoples' current off-balance sheet activities will have a material impact on future results of operations and financial condition.

Peoples continues to lease certain banking facilities and equipment under noncancelable operating leases with terms providing for fixed monthly payments over periods ranging from two to fifteen years. The majority of Peoples' leased banking facilities are inside retail shopping centers and, as a result, are not available for purchase. Management believes these leased facilities increase Peoples' visibility within its markets and afford sales associates additional access to current and potential clients.

Effects of Inflation on Financial Statements

Substantially all of Peoples' assets relate to banking and are monetary in nature. As a result, inflation does not impact Peoples to the same degree as companies in capital-intensive industries in a replacement cost environment. During a period of rising prices, a net monetary asset position results in a loss in purchasing power and conversely a net monetary liability position results in an increase in purchasing power. The opposite would be true during a period of decreasing prices. In the banking industry, typically monetary assets exceed monetary liabilities. The current monetary policy targeting low levels of inflation has resulted in relatively stable price levels. Therefore, inflation has had little impact on Peoples' net assets.

Future Outlook

Peoples' second quarter results reflect some earnings improvement from the first quarter despite the sustained low interest rate environment and uncertain economic conditions. In the final six months of 2003, management will focus to overcome short-term earnings challenges by enhancing revenues and controlling operating expenses. Peoples' overall focus remains long-term, and Peoples' current asset-liability position should minimize the impact of any future changes in interest rates on earnings. Management's commitment to sound underwriting discipline has produced asset quality that compares favorably to peer levels.

The expansion of Peoples' mortgage banking activities is an integral part of short-term earnings growth and is a key part of Peoples' long-term business strategy. In the first half of 2003, management took steps to improve Peoples' real estate lending operations to better satisfy the needs of customers. The refocusing of several Peoples Bank lenders to "Home Loan Specialists" has allowed mortgage banking income to become a major source of revenue in a relatively short period of time. Management believes the current interest rate environment provides opportunities for additional growth in the second half of 2003. Since real estate loans, as well as a basic checking account, are anchor products to successful long-term financial relationships with customers, management expects mortgage banking to remain a valuable part of Peoples' business even after rates start to increase.

While cost control remains a focus during this time of economic uncertainty, Peoples' continues to make strategic investments that are expected to provide long-term benefits for all stakeholders. For several months, management has been working to improve the integration of Peoples' customer data to allow associates to manage customer relationships more efficiently and effectively through the implementation of Customer Relationship Management ("CRM") and profitability systems. This $1.6 million investment will provide Peoples' associates with a comprehensive view of every customer, as well as allow them to offer an integrated sales package to potential customers. Beginning in the third quarter, Peoples will begin to implement these new systems, as well as amortize the project costs. Since the majority of the costs will be amortized over the expected useful life, management does not expect the CRM and profitability project to materially impact short-term earnings.

Management continues to review and rationalize Peoples' delivery channels, particularly its sales offices. As a result of the Kentucky Bancshares acquisition, Peoples' has had opportunities to improve operating efficiencies in the Kentucky markets. Concurrent with this acquisition, Peoples Bank consolidated its office at 404 Ferry Street in Russell, Kentucky with the newly acquired Russell office on Diederich Boulevard. In addition, Peoples Bank plans to close its existing Catlettsburg, Kentucky office and redirect customers to the nearby Ashland office acquired in the merger. Management believes these office consolidations allow Peoples to serve customers in these markets more efficiently and provide conveniences, such as drive-thru banking and ATMs needed in today's banking environment.

While the development and implementation of the Overdraft Privilege program has increased non-interest revenue, Peoples is obligated to pay professional fees to the consultant that assisted in the implementation of the process, based on revenue parameters, with that amount totaling approximately $115,000 in the second quarter of 2003 and $265,000 for the first half of 2003. Additional net revenues from Overdraft Privilege (i.e. after provision for bad debt) have more than offset the professional expenses associated with the new product. In March 2003, the percentage of revenues paid to the consultant decreased in accordance with the contract, which will have a positive impact on total professional fees in the final six months of 2003. In addition, the contract expires in February 2004, which should further enhance net revenues going forward, assuming Peoples maintains and/or grows total retail core deposits and volumes remain stable.

Mergers and acquisitions, such as the Kentucky Bancshares acquisition, have been an integral part of Peoples' efforts to expand its operations and scope of client services, while continuing to build client relationships and implement new products and services to enhance Peoples' earnings potential. Peoples' stronger regulatory capital ratios, as a result of the Common Stock Offering, afford management additional growth opportunities through mergers and acquisitions and market expansion. With a higher level of tangible equity to total assets, management believes Peoples is positioned to continue its disciplined acquisition strategy of the past decade and plans to dedicate more resources to develop and realize acquisition opportunities in and around Peoples' markets. However, the evaluation of future acquisitions will focus more on opportunities that complement Peoples' core competencies and strategic intent rather than geographic location or proximity to current markets.

In addition to mergers and acquisitions, Peoples routinely explores and evaluates opportunities to grow within existing markets. One such opportunity is the expansion of Peoples' operations in central Ohio by converting Peoples' loan production office in Lancaster, Ohio to a full-service business banking facility. The primary focus of the expanded office will remain business clients. However, the office will ultimately offer Peoples' complete line of products and services, including mortgage baking, insurance and investment services. The new office is planned to be completed in October 2003 and will offer deposit products for business clients in Ohio's Fairfield County and surrounding markets.

In recent years, Peoples' debit card, the Connect Card, has provided various benefits to customers while also generating fee income for Peoples based on a percentage of the transactions processed, known as interchange fees. However, MasterCard International and Visa USA have implemented new rules and changed business practices as part of agreements to settle claims brought against them in connection with the card associations' rules and fees relating to merchant acceptance of their branded cards. These changes are estimated to reduce Peoples' debit card revenues by about $70,000 before tax per quarter beginning in the third quarter of 2003, based on current volumes of debit card transactions. Management plans to partially offset this reduced income stream by continuing to grow core deposits, issuing additional debit cards, and encouraging Peoples' customers to use their debit cards as a convenient way to do their banking.

Peoples remains a service-oriented company with a sales focus that strives to satisfy clients through a relationship sales process. Through this process, sales associates work to anticipate, uncover, and solve their clients' every financial need, from insurance to banking to investments. In the third quarter of 2003, earnings catalysts include mortgage banking revenue growth, a full quarter of the Kentucky Bancshares acquisition and improved operating efficiencies. Management remains stakeholder-focused with four key long-term objectives: 7% to 10% EPS growth per year, ROE improvement, consistent dividend growth and revenue diversification.

Forward-Looking Statements

The statements in this Form 10-Q which are not historical fact are forward-looking statements within the meaning of Section 27A of the Securities Act of 1933, as amended, Section 21E of the Securities Exchange Act of 1934, as amended, and the Private Securities Litigation Reform Act of 1995. Although management believes Peoples' plans, intentions and expectations reflected in or suggested by these forward-looking statements are reasonable, Peoples cannot give any assurance that those plans, intentions or expectations will be achieved. The forward-looking statements involve a number of risks and uncertainties, including, but not limited to, the effect of changes in interest rates, the effect of federal and state banking and tax regulations, the effect of technological changes, the effect of economic conditions, the effect of competitive products and pricing, and other risks detailed in Peoples' Securities and Exchange Commission filings. All forward-looking statements are expressly qualified in their entirety by the cautionary statements. Although management believes the expectations in these forward-looking statements are based on reasonable assumptions within the bounds of management's knowledge of Peoples' business and operations, it is possible that actual results may differ materially from these projections.

SIGNATURES

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

PEOPLES BANCORP INC.

Date: August 14, 2003 By:/s/ ROBERT E. EVANS

Robert E. Evans
Chairman, President and Chief Executive Officer

Date: August 14, 2003 By:/s/ JOHN W. CONLON

John W. Conlon
Chief Financial Officer

EXHIBIT INDEX

PEOPLES BANCORP INC. QUARTERLY REPORT ON FORM 10-Q/A
FOR PERIOD ENDED JUNE 30, 2003

Exhibit Number	Description	Exhibit Loc
10(a)	Loan Agreement dated as of June 12, 2003, by and between Peoples Bancorp Inc. and First Tennessee Bank National Association.	Incorporated herein by Exhibit 10(a) to Peopl Inc.'s Quarterly Repor for the fiscal quarter 2003 (File No. 0-16772

10(b)	Promissory note executed by Peoples Bancorp Inc., as Maker in the principal amount of $17,000,000 dated June 12, 2003.	Incorporated herein by Exhibit 10(b) to Peopl Inc.'s Quarterly Repor for the fiscal quarter 2003 (File No. 0-16772
10(c)	Commercial Pledge Agreement dated as of June 12, 2003, by and between Peoples Bancorp Inc. and First Tennessee Bank National Association.	Incorporated herein by Exhibit 10(c) to Peopl Inc.'s Quarterly Repor for the fiscal quarter 2003 (File No. 0-16772
11	Computation of Earnings Per Share.	Incorporated herein by Exhibit 11 to Peoples Quarterly Report on Fo the fiscal quarter end 2003 (File No. 0-16772
12	Computation of Ratios.	Incorporated herein by Exhibit 12 to Peoples Quarterly Report on Fo the fiscal quarter end 2003 (File No. 0-16772
31(a)	CEO Certification Pursuant to Filed herewith Rule 13a-14(A)/15d-14(A)	Filed herewith
31(b)	CFO Certification Pursuant to Filed herewith Rule 13a-14(A)/15d-14(A)	Filed herewith
32	Certification Pursuant To Title 18, United States Code, Section 1350, As Adopted Pursuant To Section 906 Of The Sarbanes-Oxley Act Of 2002	Filed herewith