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TAYLOR CALVIN B BANKSHARES INC

Form 10-Q

November 05, 2001

SECURITIES AND EXCHANGE COMMISSION
Washington, DC 20549

FORM 10-Q

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

FOR THE QUARTER ENDED SEPTEMBER 30, 2001

Commission File Number: 0001003986

CALVIN B. TAYLOR BANKSHARES, INC.

I.R.S. Employer Identification No.: 52-1948274
State of incorporation: Maryland

Address of principal executive offices: 24 North Main
Street, Berlin, Maryland 21811
Issuer's telephone number: (410) 641-1700

Indicate by check mark whether the registrant (1) has
filed all reports required to be filed by Section 13 or
15(d) of the Exchange Act 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

State the number of shares outstanding of each of the
issuer's classes of common equity, as of the latest
practicable date: The registrant had 3,240,000 shares
of common stock (\$1.00 par) outstanding as of October
31, 2001.

Calvin B. Taylor Bankshares, Inc. and Subsidiaries
Form 10-Q
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Calvin B. Taylor Bankshares, Inc. and Subsidiaries
Part I - Financial Information
Consolidated Statements of Condition

	(unaudited)	
	September 30	December 31
	2001	2000
Assets		
Cash and due from banks	16,956,191	13,332,279
Federal funds sold	50,130,391	18,167,527
Interest-bearing deposits	784,000	784,000
Investment securities available for sale	3,634,477	4,052,934
Investment securities held to maturity (approximate fair value of \$89,113,635 and \$76,610,933)	86,354,239	76,273,558
Loans, less allowance for credit losses of \$2,177,132 and \$2,192,755	167,865,919	168,571,199
Premises and equipment	5,920,941	5,620,478
Accrued interest income	1,734,334	1,948,199
Deferred income taxes	119,615	107,227
Other assets	296,736	190,610
	333,796,843	289,048,011
Liabilities and Stockholders' Equity		
Deposits		
Noninterest-bearing	64,466,220	49,674,943
Interest-bearing	206,061,017	182,251,249
	270,527,237	231,926,192
Securities sold under agreements to repurchase		
	5,109,388	3,113,671
Accrued interest payable	560,378	503,519
Note payable	219,745	231,517
Accrued income taxes	57,132	103,818
Other liabilities	8,182	84,085
	276,482,062	235,962,802
Stockholders' equity		
Common stock, par value \$1 per share authorized 10,000,000 shares, issued and outstanding 3,240,000 shares	3,240,000	3,240,000
Additional paid in capital	17,290,000	17,290,000
Retained earnings	36,307,758	32,058,498
	56,837,758	52,588,498
Net unrealized gain on securities available for sale		
	477,023	496,711
	57,314,781	53,085,209
	333,796,843	289,048,011

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Calvin B. Taylor Bankshares, Inc. and Subsidiaries
Consolidated Statements of Income (unaudited)

	For the three months ended	
	September	
	2001	2000
Interest and dividend revenue		
Loans, including fees	3,526,900	3,388,391
U.S. Treasury and Agency securities	894,005	971,672
State and municipal securities	74,748	102,288
Federal funds sold	490,283	580,011
Deposits with banks	11,622	10,792
Equity securities	6,314	3,289
Total interest and dividend revenue	5,003,872	5,056,443
Interest expense		
Deposit interest	1,602,832	1,487,745
Other	23,843	10,994
Total interest expense	1,626,675	1,498,739
Net interest income	3,377,197	3,557,704
Provision for credit losses	-	23,000
Net interest income after provision for credit losses	3,377,197	3,534,704
Other operating revenue		
Service charges on deposit accounts	199,001	177,679
Miscellaneous revenue	131,250	119,726
Total other operating revenue	330,251	297,405
Other expenses		
Salaries and employee benefits	856,231	752,985
Occupancy	128,106	162,591
Furniture and equipment	155,494	67,566
Other operating	388,292	427,226
Total other expenses	1,528,123	1,410,368
Income before income taxes	2,179,325	2,421,741
Income taxes	778,413	837,824
Net income	1,400,912	1,583,917
Basic earnings per share	0.43	0.49

Calvin B. Taylor Bankshares, Inc. and Subsidiaries
Consolidated Statements of Income (unaudited)

For the nine months ended

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	September	
	2001	2000
Interest and dividend revenue		
Loans, including fees	10,725,442	10,038,406
U.S. Treasury and Agency securities	2,589,108	2,724,551
State and municipal securities	261,696	304,950
Federal funds sold	1,103,534	1,260,948
Deposits with banks	35,670	33,130
Equity securities	25,786	18,104
Total interest and dividend revenue	14,741,236	14,380,089
Interest expense		
Deposit interest	4,642,570	4,313,238
Other	55,687	19,491
Total interest expense	4,698,257	4,332,729
Net interest income	10,042,979	10,047,360
Provision for credit losses	-	106,080
Net interest income after provision for credit losses	10,042,979	9,941,280
Other operating revenue		
Service charges on deposit accounts	608,122	539,752
Miscellaneous revenue	374,577	313,135
Total other operating revenue	982,699	852,887
Other expenses		
Salaries and employee benefits	2,508,625	2,296,553
Occupancy	332,793	473,213
Furniture and equipment	445,651	398,115
Other operating	1,200,524	1,221,279
Total other expenses	4,487,593	4,389,160
Income before income taxes	6,538,085	6,405,007
Income taxes	2,288,825	2,218,638
Net income	4,249,260	4,186,369
Basic earnings per share	1.31	1.29

Calvin B. Taylor Bankshares, Inc. and Subsidiaries
Consolidated Statements of Cash Flows (unaudited)

	For the nine months ended	
	September	
	2001	2000
Cash flows from operating activities		
Interest received	14,847,228	14,583,888
Fees and commissions received	1,021,867	868,831
Interest paid	(4,641,398)	(4,276,398)
Cash paid to suppliers and employees	(4,276,194)	(4,012,433)
Income taxes paid	(2,335,511)	(2,149,480)
	4,615,992	5,014,408

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Cash flows from investing activities		
Proceeds from maturities of investment securities	47,747,000	45,935,000
Purchase of investment securities held to maturity	(57,333,426)	(35,162,275)
Certificates of deposit purchased, net of redemptions	199,000	
Purchases of premises, equipment, and intangibles	(750,060)	(420,042)
Loans made, net of principal collected	705,280	(10,388,035)
Proceeds from sales of equipment	17,000	423
	(9,614,206)	164,071
Cash flows from financing activities		
Net change in time deposits	14,054,954	2,909,579
Net change in other deposits	24,546,091	2,297,033
Net change in repurchase agreements	1,995,717	4,432,764
Payment on mortgage obligation	(11,772)	(14,675)
Dividend paid	-	-
	40,584,990	9,624,701
Net increase (decrease) in cash	35,586,776	14,803,180
Cash and equivalents at beginning of period	31,499,806	34,423,959
Cash and equivalents at end of period	67,086,582	49,227,139
Reconciliation of net income to net cash provided from operating activities		
Net income	4,249,260	4,186,369
Adjustments		
Depreciation and amortization	380,284	367,366
Deferred income tax	-	
Provision for loan losses	-	106,080
Security discount accretion, net of premium amortization	(107,873)	(37,170)
(Gain) loss on disposition of assets	(13,933)	-
Decrease (increase) in accrued interest receivable and other assets	173,984	256,913
Increase (decrease) in accrued interest payable and other liabilities	(65,730)	134,850
	4,615,992	5,014,408

Calvin B. Taylor Bankshares, Inc. and Subsidiaries
Notes to Financial Statements

1. Basis of Presentation

The accompanying unaudited consolidated financial statements have been prepared in accordance with generally accepted accounting principles for interim financial information and with the instructions to Form 10-Q. Accordingly, they do not include all the information and footnotes required by generally accepted accounting principles for complete financial statements. In the opinion of management, all adjustments considered necessary for a fair presentation have been made. These adjustments are of a normal recurring nature. Results of operations for the nine months ended September 30, 2001 are not necessarily indicative of the results that may be expected for the year ending December 31, 2001. For

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further information, refer to the audited consolidated financial statements and related footnotes for the Registrant's fiscal period ended December 31, 2000.

Consolidation has resulted in the elimination of all significant intercompany accounts and transactions.

Cash Flows

For purposes of reporting cash flows, cash and cash equivalents include cash on hand, amounts due from banks and overnight investments in federal funds sold.

Per share data

Earnings per common share and dividends per common share are determined by dividing net income and dividends by the 3,240,000 shares outstanding, giving retroactive effect to stock dividends distributed.

2. Comprehensive Income

Comprehensive income consists of:

	Nine months ended September 30,	
	2001	2000
Net income	\$4,249,260	\$4,186,369
Unrealized gain (loss) on investment securities available for sale, net of income taxes	(19,688)	152,623
Comprehensive income	\$4,229,572	\$4,338,992

Calvin B. Taylor Bankshares, Inc. and Subsidiaries
Part I. Financial Information
Item 2. Management's Discussion and Analysis of
Financial Condition and Results of Operations

The following discussion contains certain forward-looking statements within the meaning of and made pursuant to the safe harbor provisions of the Private Litigation Securities Reform Act of 1995.

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The following discussion of the financial condition and results of operations of the Registrant (the Company) should be read in conjunction with the Company's financial statements and related notes and other statistical information included elsewhere herein.

General

Calvin B. Taylor Bankshares, Inc. (the "Company") was incorporated as a Maryland corporation on October 31, 1995. The Company owns all of the stock of two banks. Calvin B. Taylor Banking Company (the "Maryland bank") is a commercial bank that was established in 1890 and incorporated under the laws of the State of Maryland on December 17, 1907. This bank operates nine banking offices in Worcester County with the Bank's main office located in Berlin, Maryland. It is engaged in a general commercial and retail banking business serving individuals, businesses, and governmental units in Worcester County, Maryland and neighboring counties.

Calvin B. Taylor Bank of Delaware (the "Delaware bank") was incorporated in the state of Delaware in 1997. This one-branch Delaware bank, which offers the same services as the Maryland bank, opened late in the second quarter of 1998. The Company currently engages in no business other than owning and managing the Banks.

Financial Condition

Total assets of the Company increased \$44.7 million from December 31, 2000 to September 30, 2001. Combined deposits and customer repurchase agreements increased \$40.6 million during the same period. During the first quarter of the year, the banks typically experience a decline in deposits since business customers are using their deposits to meet cash flow needs. Generally, this situation reverses late in the second quarter of the year as the banks receive loan repayments from seasonal business customers, and deposits from summer residents and tourists. Late in the third quarter, seasonal deposits decline. Management believes that adverse conditions in the national stock markets, which have been amplified by the terrorist attacks of September 11, 2001, are contributing to the sustained high level of deposits in the banks as of September 30, 2001.

During the first nine months of 2001, the banks' loan portfolios have decreased \$721 thousand. As market rates have declined, the banks have faced aggressive competition for low rate loans.

The allowance for credit losses represents a reserve for potential losses in the loan portfolio. The adequacy of the allowance for credit losses is evaluated periodically based on a review of all significant loans, with a particular emphasis on non-accruing, past due, and other loans that management believes require attention. The determination of the

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reserve level rests upon management's judgment about factors affecting loan quality and anticipated changes in the composition and size of the portfolio, as well as assumptions about the economy. Historically, the Company has low loan charge-offs. The banks' target levels for their allowances as a percentage of gross loans range from approximately 1.00% to 1.27%. Based on a review of the consolidated loan portfolio, the Company determined that an allowance of 1.28% of gross loans was adequate as of September 30, 2001. At December 31, 2000, the allowance was 1.28% of gross loans. At September 30, 2001, one loan of \$175,000 was nonaccruing, representing .10% of the portfolio, and accruing loans of \$137,587 or .08% of the portfolio were delinquent ninety days or more.

Liquidity

The company's major sources of liquidity arise from loan repayments, short-term investments, including federal funds sold, and an increase in core deposits. Throughout the first quarter of the year, when the banks typically experience a decline in deposits, federal funds sold and investment securities are primary sources of liquidity. During the second quarter of the year, additional sources of liquidity become more readily available as business borrowers start repaying loans, and the banks receive seasonal deposits. Throughout the second and third quarters the banks maintain a high liquidity level.

Funds from seasonal deposits are generally invested in short-term U.S. Treasury Bills and overnight federal funds. Average liquid assets (cash and amounts due from banks, interest bearing deposits in other banks, federal funds sold, and investment securities) compared to average deposits were 56.66% for the third quarter of 2001 as compared to 48.05% for the second quarter of 2001 and 53.20% for the third quarter of 2000.

Results of Operations

Net income for the three months ended September 30, 2001, was \$1,400,912 or \$.43 per share, compared to \$1,583,917 or \$.49 per share for the third quarter of 2000. This represents a decrease of \$183,005 or 11.55% from the prior year. Year to date net income increased \$62,891 or \$.02 per share from \$4,186,369 or \$1.29 per share in 2000 to \$4,249,260 or \$1.31 per share in 2001. Significant reasons for the year to date increase in net income are increased non-interest income and a reduction of the provision for credit losses, offset in part by a decrease in net interest income and increased operating expenses.

Net interest income decreased \$4,381 in the first nine months of 2001 as compared to the first nine months of 2000. Net interest income decreased \$180,507 in the three months ended September 30, 2001 as compared to the three months ended September 30, 2000. This decrease, both year-to-date and for the most recent quarter, is attributable to the overall

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reduction of rates on earning assets, and the growth of interest-bearing deposits which are invested in U. S. treasury securities and low yielding overnight federal funds. Management views the influx of deposits as temporary and has chosen not to invest in longer term investment vehicles. The Company's net interest income is one of the most important factors in evaluating its financial performance. Management uses interest sensitivity analysis to determine the effect of rate changes. Net interest income is projected over a one-year period to determine the effect of an increase or decrease in the prime rate of 100 basis points. If prime were to decrease one hundred basis points, and all assets and liabilities maturing within that period were fully adjusted for the rate change, the Company would experience a decrease of less than six percent in net interest income. The sensitivity analysis does not consider the likelihood of these rate changes nor whether management's reaction to this rate change would be to reprice its loans or deposits.

No provision for loan losses was made in the three quarters of 2001, versus a \$106,080 provision in same period in 2000. Net charge-offs during the third quarter of 2001, and the year-to-date, were \$10,143 and \$15,623, respectively.

Other operating revenue, including service charges on deposit accounts, increased \$33 thousand from third quarter 2000 to third quarter 2001. For the year to date, other operating revenue has increased \$130 thousand from 2000 to 2001. Revenue increases are primarily due to deposit services charges assessed against a larger deposit base, and fees related to increased ATM and VISA debit card use.

Personnel expenses are higher for the nine months ended September 30, 2001 compared to the same period in 2000 due to general increases in salaries and the addition of two new positions, as well as increased health care costs. The banks employed 98 full time equivalent employees as of September 30, 2001. The Maryland bank hires seasonal employees during the summer. The Company has no employees other than those hired by the banks.

The Company's occupancy expense decreased \$140 thousand from first three quarters of 2000 to 2001. Of this, \$39 thousand was due to the relocation, in 2000, of vehicular access to a branch, which was necessary due to road construction. Also in 2000, the Maryland bank consolidated two branches in Pocomoke Maryland, and incurred cost to move and otherwise dispose of assets from the abandoned branch. In 2001, the banks changed their accounting for real property taxes from cash basis to amortizing the cost throughout the year.

Furniture and fixture expenses increased \$48 thousand from the first three quarters of 2000 to 2001. Depreciation associated with the replacement and upgrade of the banks' computer equipment comprises most of the increase. Although the Company's current data

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processing equipment meets the needs of the banks, it is nearing the end of its economic life. The Company expects to replace its core processing system in the fourth quarter of 2001 and expects related depreciation, maintenance costs, and software amortization expense to increase with this replacement. Prior to the installation of the new processing system, improved data storage, networking, and Internet banking systems are planned. It is anticipated that these, too, will cause an increase in related costs.

Plans of Operation

The banks conduct general commercial banking businesses in their service areas, of Worcester County, Maryland and Sussex County, Delaware, while also emphasizing the banking needs of individuals and small- to medium-sized businesses and professional concerns. The banks offer a full range of federally insured deposit services that are typically available in most banks and savings and loan associations, including checking accounts, NOW accounts, savings accounts and other time deposits of various types ranging from daily money market accounts to longer-term certificates of deposit.

The Company, through its banks, offers a full range of short- to medium-term commercial and personal loans, and originates mortgage loans, including real estate construction and acquisition loans. The banks have the intent and the ability to hold loans that they originate in their portfolios.

Other bank services include cash management services, safe deposit boxes, travelers checks, direct deposit of payroll and social security checks, debit cards, and automatic drafts for various accounts. The Company is associated with the MAC network of automated teller machines that may be used by customers throughout Maryland, Delaware and other regions. The Company offers credit card services through a correspondent bank.

Capital Resources and Adequacy

Total stockholders' equity increased \$4,229,572 from December 31, 2000 to September 30, 2001. This increase is attributable to the comprehensive income recorded during the period, as detailed in Note 2 of the Notes to Financial Statements.

Under the capital guidelines of the Federal Reserve Board and the FDIC, the Company and its banks are currently required to maintain a minimum risk-based total capital ratio of 8%, with at least 4% being Tier 1 capital. Tier 1 capital consists of common shareholders' equity, qualifying perpetual preferred stock, and minority interests in equity accounts of consolidated subsidiaries, less certain intangibles. In addition, the Company and the banks must maintain a

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minimum Tier 1 leverage ratio (Tier 1 capital to total assets) of at least 3%, but this minimum ratio is increased by 100 to 200 basis points for other than the highest-rated institutions.

Tier one risk-based capital ratios of the Company as of September 30, 2001 and 2000 were 32.31% and 36.53%, respectively. Both are substantially in excess of regulatory minimum requirements.

Item 3. Quantitative and Qualitative Disclosures About Market Risk

The Company's principal market risk exposure relates to interest rates on interest-earning assets and interest-bearing liabilities. Unlike most industrial companies, the assets and liabilities of financial institutions such as the Company and the banks are primarily monetary in nature. Therefore, interest rates have a more significant effect on the Company's performance than do the effects of changes in the general rate of inflation and change in prices. In addition, interest rates do not necessarily move in the same direction or in the same magnitude as the prices of goods and services. As discussed previously, management monitors and seeks to manage the relationships between interest sensitive assets and liabilities in order to protect against wide interest rate fluctuations, including those resulting from inflation.

At September 30, 2001, the Company's interest rate sensitivity, as measured by gap analysis, showed the Company was asset-sensitive with a one-year cumulative gap of 23.48%, as a percentage of interest-earning assets. Generally asset-sensitivity indicates that assets reprice more quickly than liabilities and in a rising rate environment net interest income typically increases. Conversely, if interest rates decrease, net interest income would decline. Both banks have classified their demand mortgage and commercial loans as immediately repricing. Unlike loans tied to prime, these rates do not necessarily change as prime changes since the decision to call the loans and change the rates rests with management.

Calvin B. Taylor Bankshares, Inc. and Subsidiaries Part II. Other Information

Item 1 Legal Proceedings
Not applicable

Item 2 Changes in Securities and Use of Proceeds
Not applicable

Item 3 Defaults Upon Senior Securities

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Not applicable

Item 4 Submission of Matters to a Vote of Security
Holders

Not applicable

Item 5 Other information

Not applicable.

Item 6 Exhibits and Reports on Form 8-K

a) Exhibits

2. Proxy Statement dated March 7, 2001, is
incorporated by reference.

b) Reports on Form 8-K

There were no reports on Form 8-K filed for
the quarter ended September 30, 2001.

SIGNATURES

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

Calvin B. Taylor Bankshares, Inc.

Date: November 01, 2001 By: /s/ Reese F. Cropper, Jr.
Reese F. Cropper, Jr.
President and Chief
Executive Officer

Date: November 01, 2001 By: /s/ William H. Mitchell
William H. Mitchell
Chief Financial Officer

