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LETTER FROM THE PRESIDENT



CHARTING THE COURSE FOR THE FUTURE

DEAR SHAREHOLDERS:

In some important ways, 2003 was a year of seeming contradiction: Peoples Financial Corporation stayed the course of our strategic plan, yet at the same time we charted new directions for the future.

In practice, these actions were not incompatible. And they were quite successful: the company enjoyed its most profitable year since 1999, with net income increasing 57% over 2002 to \$5,018,000. Moreover, we were able to raise the dividend not once but twice during 2003, a total increase of 25%, from \$.12 a share at the beginning of 2003 to \$.15 a share at the start of 2004.

So how did we stay the course and chart new directions at the same time? First, we stayed the course of our strategic plan to continue pursuing expansion in the face of difficult economic conditions. We started the year with the opening of our new branch in Gautier in January, 2003, then dedicated a new, larger facility in Long Beach near the end of the year. In December, we began work on the renovation of our Bay St. Louis branch to accommodate the growth of our business in Hancock County.

On the financial side of our business, we aggressively tackled the challenge of shrinking interest margins by repricing deposits, while simultaneously addressing loan portfolio issues. As we start 2004, I'm comfortable that all our problem loans have been dealt with, and we can look forward to pursuing business on the loan side once again.

At the same time, during 2003 we began charting new directions to position The Peoples Bank for more growth in the future. Specifically, we engaged the services of a respected management consulting firm to analyze our entire organizational structure and suggest changes to take us seamlessly to another level of asset size.

During the second half of 2003, we began to implement the report's recommendations. Most notably, we have clearly defined the responsibilities of the members of our senior management team, and they in turn have begun to build their respective employee groups to implement their own strategic plans. The result, we are confident, will be a more efficient operation that provides more responsive service to our customers.

Throughout this year of change, we have been blessed with a group of employees whose dedication has been unwavering. Their contribution to the success of The Peoples Bank is incalculable. Whether they are on the front line directly serving customers or in the back office keeping our systems running smoothly, our team members represent the engine that drives The Peoples Bank. I want to acknowledge and salute their splendid performance through turbulent times.

I also want to pay special tribute to our board of directors, who have demonstrated their leadership in charting this new direction for Peoples Financial Corporation while supporting our management team to stay the course of our strategic plan. Our directors' combination of vision and determination represents a great source of strength on which I am personally grateful to depend.

Finally, I offer my gratitude to our stockholders who have entrusted our team with the management and operation of this institution. We never forget that our stockholders are our owners; we strive to earn your trust and generate a fair return on your investment every day.

Sincerely,

A handwritten signature in black ink that reads "Chevis C. Swetman". The signature is fluid and cursive.

Chevis C. Swetman
Chairman of the Board, Chief Executive Officer

THE YEAR IN
REVIEW



PROFITS RISE, DIVIDEND RAISED TWICE

Financial performance in 2003 reversed the course of the last three years of economic difficulty, with net income rising 57% over the year before, totaling \$5,018,000, compared to \$3,191,000 for 2002. The 2002 performance was impacted by a \$1,500,000 addition to loan loss reserves caused by a single credit.

However, exclusive of the loss provision, 2003 results exceeded 2002 by nearly 9%, largely on the strength of an 8% increase in net interest income to more than \$19,000,000. The increase in net interest income was the result of stabilizing interest rates and our ability to reprice loans and deposits to bring interest rates margins back to acceptable levels.

As a result of the steady rise in earnings, the Board of Directors voted to increase the dividend paid on the common stock of Peoples Financial Corporation twice during 2003. In June, the Board voted to increase the dividend by 16.7%, from \$.12 to \$.14 a share. At the end of the year, the Board voted to raise the dividend another 7.1% to \$.15 a common share.



Combined, the two dividend raises increased the dividend 25% above the level it stood at the end of 2002. The current dividend represents a distribution of about 32% of earnings, very near the target of 35% set by the board a year earlier. The latest dividend increase was the fifth in the last six years, making the current \$.30 annualized dividend 76% higher than the 1998 payout of \$.17 per share.

Meanwhile, The Peoples Bank capital ratios continued to improve during the year. Primary capital to average assets finished 2003 at 15.84%,

compared to 15.39% at the end of 2002. Our strong capital base gives us the ability to continue our expansion program, even during difficult economic conditions.



TWO NEW BRANCHES OPEN, RENOVATION OF ANOTHER BRANCH ANNOUNCED

In a continuation of our program of physical and geographic expansion, 2003 saw the grand opening of two new branches of the Peoples Bank. We opened our new branch in Gautier in January to serve our growing customer base in Jackson County. Later in the fall, we dedicated a new facility in Long Beach that replaced an older branch two blocks away. The new, full-service Long Beach branch provides a total of 2,000 square feet of banking space to customers, including a night drop, safe deposit boxes, two drive-up lanes and an ATM.

At the end of the year, The Peoples Bank also announced plans to renovate the Bay St. Louis branch to offer enhanced service to customers in the Bay-Waveland area.



Bay St. Louis branch manager Jeannie Deen and prominent business executive William Lady were featured in a television commercial that was part of a new advertising campaign launched in 2003. The campaign features employees from all departments and branches in a series of print ads that accompany the television and radio commercials.

THE PEOPLES BANK AND ITS PEOPLE GIVE BACK TO THE COMMUNITY



During 2003, The Peoples Bank continued its long-standing tradition of giving back to the community, with corporate and individual donations to non-profit groups serving the Mississippi Gulf Coast.

Two local charitable organizations—St. Vincent DePaul Pharmacy and the Junior Auxiliary of Biloxi—each received checks for \$8,266.50, raised through the efforts of Peoples Bank employees through charity golf and bowling tournaments during the year. The donation to the Junior Auxiliary is believed to be the largest single donation ever received by the organization, according to officials of the group.

In addition, bank employees selected Life of South Mississippi and Morning Star to receive corporate donations of \$5,000 each. Bank president Chevis Swetman presented the checks to representatives of the two organizations.

Once again, The Peoples Bank took an active role in the week-long Cruisin' the Coast event that has grown to nearly 6,000 registered participants. The annual Biloxi block party of the event was once again staged in front of the Main Branch of the bank. All staffers at the Main Branch, including president and CEO Chevis Swetman, supported the event by dressing in 50s outfits of blue jeans and poodle skirts.



Board of Directors

Peoples Financial Corporation

Chevis C. Swetman, Chairman of the Board

Dan Magruder, Vice Chairman; President, Rex Distributing Co., Inc.

Drew Allen, President, Allen Beverages, Inc.

Rex E. Kelly, Director of Corporate Communications, Mississippi Power Company

Lyle M. Page, Partner, Page, Mannino, Peresich & McDermott

Officers

Peoples Financial Corporation

Chevis C. Swetman, President and CEO

Thomas J. Sliman, First Vice-President

Jeannette E. Romero, Second Vice-President

Robert M. Tucei, Vice-President

A. Wes Fulmer, Vice-President and Secretary

M. O. Lawrence, III, Vice-President

Lauri A. Wood, Chief Financial Officer and Controller

Board of Directors

The Peoples Bank, Biloxi, Mississippi

Chevis C. Swetman, Chairman

Tyrone J. Gollott, Vice-Chairman; Secretary-Treasurer, Gollott & Sons Transfer & Storage, Inc.

Drew Allen, President, Allen Beverages, Inc.

Liz Corso Joachim, President, Frank P. Corso, Inc.

Rex E. Kelly, Director of Corporate Communications, Mississippi Power Company

Dan Magruder, President, Rex Distributing Co., Inc.

Jeffrey H. O'Keefe, President, Bradford-O'Keefe Funeral Homes, Inc.

Lyle M. Page, Partner, Page, Mannino, Peresich & McDermott

Officers

The Peoples Bank, Biloxi, Mississippi

Senior Management

Chevis C. Swetman, President and CEO

Thomas J. Sliman, Senior Vice-President

Jeannette E. Romero, Senior Vice-President

Robert M. Tucei, Senior Vice-President

Lauri A. Wood, Senior Vice-President and Cashier

A. Wes Fulmer, Senior Vice-President

M. O. Lawrence, III, Senior Vice-President

A. Wes Fulmer, Senior Vice-President and Chief Lending Officer

Lending

Brian J. Kozlowski, Assistant Vice-President

Andrew M. Welter, Assistant Vice-President

Stephanie D. Broussard, Loan Officer

Melanie L. Battise, Branch Manager

Diana T. Winland, Loan Officer

Pinky T. Walker, Administrative Officer

West Region

Jeannie M. Deen, Vice-President

Eric M. Chambless, Assistant Vice-President

William A. Aborn, Branch Manager

Debora T. Batchelor, Loan Officer

Shannon D. Garrett, Loan Officer

Central Region

John W. McKellar, Vice-President

Mark A. Chatham, Vice-President

Read H. Breeland, Assistant Vice-President

James P. Estrada, Assistant Vice-President

Brent G. Johnson, Assistant Vice-President

William S. Maddox, Assistant Vice-President

J. Denise Holmes, Branch Manager

East Region

Jerome D. Dodge, II, Vice-President

David A. Thompson, Assistant Vice-President

Henry N. Knue, Branch Manager

Patrick J. Lyons, Branch Manager

John L. Welter, IV, Branch Manager

Julie B. Carpenter, Loan Officer

Human Resources

Jackie L. Henson, Vice-President

Patricia L. Levine, Vice-President

Janice L. Smitherman, Assistant Vice-President - Employee Benefits

Business Development

Dennis J. Burke, Vice-President

Robert M. Tucei, Senior Vice-President and Chief Credit Officer

Credit Administration

J. Patrick Wild, Vice-President

Donna F. Bessetti, Vice-President

Jesse J. Miguez, Assistant Vice-President

Ronnie F. Harrison, Assistant Vice-President

Kathleen M. Worrell, Insurance Officer

Thomas J. Sliman, Senior Vice-President and Chief Information Officer

Technology and Facilities

Sandra L. York, Vice-President - Information Systems
George S. Trantum, Vice-President - Technical Support
James M. Gruich, Assistant Vice-President - Technology Security
Gloria A. Cothorn, Assistant Vice-President - Electronic Banking
Ronald L. Baldwin, Systems Support Technician Officer
Frederick J. Breal, Property Officer
Cheryl A. Dewey, Data Processing Officer
Thomas A. Esposito, Jr., Business Solutions Officer
John M. Zorich, Internet Banking Technology Officer

Lauri A. Wood, Senior Vice President and Chief Financial Officer

Financial

Connie F. Lepoma, Assistant Vice-President
Cassandra F. Reid, Assistant Cashier

Investments

Peggy M. Byrd, Vice-President
Janet H. Wood, Assistant Vice-President

M. O. Lawrence, III, Senior Vice-President and Senior Trust Officer

Asset Management & Trust Services

Ann F. Guice, Vice-President
Louise C. Wilson, Trust Officer
Thomas H. Wicks, Trust Officer
Daniel A. Bass, Trust Officer
C. J. Dunaway, Trust Officer

Jeannette E. Romero, Senior Vice President and Retail Banking Officer

Account Services

Kathy S. Comstock, Savings Officer
Toni A. Ganucheau, Assistant Cashier

ATM/Bankcard

Cheryl A. Dubaz, Assistant Vice-President - ATM
Charlotte R. Balius, Bankcard Officer

Operations

Susan B. Page, Assistant Vice-President - Operations
Ardell M. Roberts, Assistant Cashier
Hugh J. Kavanagh, Assistant Cashier
Diana W. Williams - Branch Manager
Laura E. Elliott, Assistant Branch Manager

Security

Robin Vignes, Vice-President
Minh-Tuyet Nguyen, Security Officer
Margaret H. Chandler, Assistant Security Officer

Audit, Compliance and Loan Review

Gregory M. Batia, Vice-President and Auditor
Evelyn R. Herrington, Vice-President - Compliance
Robert E. Smith, Jr., Vice-President - Loan Review
F. Kay Rice, Loan Review Officer
Rebecca A. Williams, Assistant Auditor
Darnell Y. Schreck, Assistant Cashier - Compliance

Branch Locations

The Peoples Bank, Biloxi, Mississippi

Biloxi Branches

Main Office, 152 Lameuse Street, Biloxi, Mississippi 39530,
(228) 435-5511
Cedar Lake Office, 11355 Cedar Lake Road, Biloxi, Mississippi 39532
(228) 435-8688
West Biloxi Office, 2430 Pass Road, Biloxi, Mississippi 39531,
(228) 435-8203

Gulfport Branches

Downtown Gulfport Office, 1105 30th Avenue, Gulfport,
Mississippi 39501, (228) 897-8715
Handsboro Office, 0412 E. Pass Road, Gulfport, Mississippi 39507,
(228) 897-8717
Orange Grove Office, 12020 Highway 49 North, Gulfport,
Mississippi 39503, (228) 897-8718

Other Branches

Bay St. Louis Office, 408 Highway 90 East, Bay St. Louis,
Mississippi 39520, (228) 897-8710
Diamondhead Office, 4408 West Aloha Drive, Diamondhead,
Mississippi 39525, (228) 897-8714
D'Iberville-St. Martin Office, 10491 Lemoyne Boulevard,
D'Iberville, Mississippi 39532, (228) 435-8202
Gautier Office, 2601 Highway 90, Gautier, Mississippi 39553,
(228) 497-1766
Long Beach Office, 298 Jeff Davis Avenue, Long Beach,
Mississippi 39560 (228) 897-8712
Ocean Springs Office, 2015 Bienville Boulevard, Ocean Springs,
Mississippi 39564, (228) 435-8204
Pass Christian Office, 125 Henderson Avenue, Pass Christian,
Mississippi 39571, (228) 897-8719
Saucier Office, 17689 Second Street, Saucier, Mississippi 39574,
(228) 897-8716
Wiggins Office, 1312 S. Magnolia Drive, Wiggins, Mississippi 39577
(228) 897-8722

PEOPLES FINANCIAL CORPORATION AND SUBSIDIARIES

Corporate Office

Mailing Address

P. O. Box 529
Biloxi, MS 39533-0529
(228) 435-8205

Physical Address

152 Lameuse Street
Biloxi, MS 39530

Website

www.thepeoples.com

Corporate Stock

The common stock of Peoples Financial Corporation is traded on the NASDAQ Small Cap Market under the symbol: PFBX. The current market makers are:

Johnston Lemon & Company
Morgan Keegan & Company, Inc.
Sterne, Agee & Leach, Inc.

Shareholder Information

For complete information concerning the common stock of Peoples Financial Corporation, including dividend reinvestment, or general information about the Company, direct inquiries to transfer agent/investor relations:

Asset Management & Trust Services Department
The Peoples Bank, Biloxi, Mississippi
Attention: M. O. Lawrence, III, Senior Vice-President
P. O. Box 1416, Biloxi, Mississippi 39533-1416
(228) 435-8208,
e-mail: investorrelations@thepeoples.com

Independent Auditors

Piltz, Williams, LaRosa & Company, Biloxi, Mississippi

S.E.C. Form 10-K Requests

A copy of the Annual Report on Form 10-K, as filed with the Securities and Exchange Commission, may be obtained without charge by directing a written request to:

Lauri A. Wood, Chief Financial Officer and Controller
Peoples Financial Corporation
P. O. Drawer 529, Biloxi, Mississippi 39533-0529
(228) 435-8412, e-mail: lwood@thepeoples.com

BOARD OF DIRECTORS



PEOPLES FINANCIAL CORPORATION THE PEOPLES BANK, BILOXI, MISSISSIPPI

BACK ROW FROM LEFT: Jeffrey H. O'Keefe, *President, Bradford-O'Keefe Funeral Homes, Inc.*; Tyrone J. Gollott, *Vice-Chairman of The Peoples Bank; Secretary-Treasurer, Gollott & Sons Transfer & Storage, Inc.*; Lyle M. Page*, *Partner, Page, Mannino, Peresich & McDermott.*

FRONT ROW FROM LEFT: Rex E. Kelly*, *Director of Corporate Communications, Mississippi Power Company*; Drew Allen*, *President, Allen Beverages, Inc.*; Chevis C. Swetman*, *Chairman of the Board*; Dan Magruder*, *Vice-Chairman of Peoples Financial Corporation*; President, *Rex Distributing Co., Inc.*; Liz Corso Joachim, *President, Frank P. Corso, Inc.*

*Member of both boards.

PEOPLES FINANCIAL CORPORATION AND SUBSIDIARIES

The following presents Management's discussion and analysis of the consolidated financial condition and results of operations of Peoples Financial Corporation and Subsidiaries (the Company) for the years ended December 31, 2003, 2002 and 2001. These comments highlight the significant events for these years and should be considered in combination with the Consolidated Financial Statements and Notes to Consolidated Financial Statements included in this annual report.

FORWARD-LOOKING INFORMATION

Congress passed the Private Securities Litigation Act of 1995 in an effort to encourage corporations to provide information about a company's anticipated future financial performance. This act provides a safe harbor for such disclosure which protects the companies from unwarranted litigation if actual results are different from management expectations. This report contains forward-looking statements and reflects industry conditions, company performance and financial results. These forward-looking statements are subject to a number of factors and uncertainties which could cause the Company's actual results and experience to differ from the anticipated results and expectations expressed in such forward-looking statements.

CRITICAL ACCOUNTING POLICIES

Certain critical accounting policies affect the more significant estimates and assumptions used in the preparation of the consolidated financial statements. The Company's single most critical accounting policy relates to its allowance for loan losses, which reflects the estimated losses resulting from the inability of its borrowers to make loan payments. If there was a deterioration of any of the factors considered by Management in evaluating the allowance for loan losses, as discussed in Note A, the estimates of loss would be updated, and additional provisions for loan losses may be required.

OVERVIEW

Net income was \$5,018,000 for the year ended December 31, 2003, as compared with \$3,191,000 for the year ended December 31, 2002.

Net interest income improved from \$17,808,000 for 2002 to \$19,227,000 for 2003 as the Company continues its interest rate management policies begun in 2002. These policies particularly include the aggressive pricing of loans and the favorable repricing of deposits, specifically large and brokered certificates of deposit. Also, the provision for loan losses was \$2,428,000 for 2002, as compared with a provision of \$447,000 for 2003, as the Company had previously identified and provided for potential significant loan losses in the prior year.

FINANCIAL CONDITION

Available for Sale Securities

Available for sale securities increased \$56,002,000 at December 31, 2003 as compared with December 31, 2002 primarily as a result of the management of the bank subsidiary's liquidity position and its interest margin. The Company reinvested funds from maturities in held to maturity securities in available for sale securities.

Gross unrealized gains were \$2,113,000, \$3,032,000 and \$2,787,000 and gross unrealized losses were \$1,094,000, \$12,000 and \$84,000 for available for sale securities at December 31, 2003, 2002 and 2001, respectively. Gains of \$57,000, \$210,000 and \$243,000 were realized on the liquidation or sale of available for sale securities in 2003, 2002 and 2001, respectively.

Held to Maturity Securities

Held to maturity securities decreased \$13,235,000 at December 31, 2003, compared with December 31, 2002. The decrease in these securities is directly attributable to the management by the Company of its liquidity position, as discussed above. Funds available from the maturity of these securities were generally invested in available for sale securities.

Gross unrealized gains were \$176,000, \$438,000 and \$725,000, at December 31, 2003, 2002 and 2001, respectively, while gross unrealized losses were \$2,000 and \$18,000, at December 31, 2003 and 2001, respectively. There were no significant realized gains or losses from calls of these investments for the years ended December 31, 2003, 2002 and 2001.

Federal Home Loan Bank Stock

The Company acquired common stock issued by the Federal Home Loan Bank as a prerequisite for participating in their loan programs.

Loans

The Company's loan portfolio decreased \$14,373,000 at December 31, 2003, as compared with December 31, 2002. This decrease was a result of decreased loan demand in the Company's trade area caused by the softening of the local economy. Another contributing factor was the refinancing of loans in our trade area's highly competitive interest rate environment. During the fourth quarter of 2003, the loan portfolio increased as the local economy became stabilized. The Company anticipates that this positive loan growth will continue in 2004. Funds that are available to fund loan demand in the future are presently invested primarily in available for sale securities. Fluctuations in the various categories of loans are illustrated in Note C.

Other Real Estate

The Other Real Estate (ORE) portfolio increased \$188,000 at December 31, 2003 as compared with December 31, 2002 due to the foreclosure of several large parcels of real estate. The Company is actively marketing these properties and anticipates a significant reduction in ORE for 2004. Gains (losses) realized on sales of ORE were \$248,170, (\$43,666) and \$118,716 for the years ended December 31, 2003, 2002 and 2001, respectively.

Other Assets

Other assets increased \$1,031,000 at December 31, 2003, as compared with December 31, 2002, due to deferred taxes on unrealized losses on available for sale securities.

Deposits

Total deposits decreased \$15,617,000 at December 31, 2003, as compared with December 31, 2002. Significant increases or decreases in total deposits and/or significant fluctuations among the different types of deposits are anticipated by Management as customers in the casino industry and county and municipal areas reallocate their resources periodically. The Company has managed its funds including planning the timing of investment maturities and the classification of investments and using other funding sources and their maturity so as to achieve appropriate liquidity. Specifically, the Company obtained \$30,000,000 in brokered deposits during 2000, the last of which matured in 2003. The Company does not currently plan to obtain further brokered deposits.

Federal Funds Purchased and Securities Sold Under Agreements to Repurchase

Federal funds purchased and securities sold under agreements to repurchase increased \$27,794,000 at December 31, 2003, as compared with December 31, 2002. This fluctuation is directly related to customers' periodic reallocation of their funds in a non-deposit product and the management of the Company's liquidity position.

Borrowings from Federal Home Loan Bank

The Company acquires funds from the Federal Home Loan Bank in the management of the liquidity position. As discussed in Note E, the Company acquired \$10,000,000 in advances which matures on January 9, 2004.

Other Liabilities

Other liabilities increased \$814,000 at December 31, 2003, as compared with December 31, 2002, as a result of an increase in liabilities related to deferred compensation benefits for a retired officer and current officers and directors of the bank subsidiary.

Shareholders' Equity

During 2003, 2002 and 2001, there were significant events that impacted the components of shareholders' equity. These events are detailed in Note H to the Consolidated Financial Statements included in this report.

Strength, security and stability have been the hallmark of the Company since its founding in 1985 and of its bank subsidiary since its founding in 1896. A strong capital foundation is fundamental to the continuing prosperity of the Company and the security of its customers and shareholders. There are numerous indicators of capital adequacy including primary capital ratios and capital formation rates. The Five-Year Comparative Summary of Selected Financial Information presents these ratios for those periods. This summary is included in the annual report to shareholders. The Company's total risk-based capital ratio at December 31, 2003, 2002 and 2001 was 24.81%, 24.16% and 21.90% as compared with the required standard of 8.00%. The Five-Year Comparative Summary of Selected Financial Information presents these figures.

Bank regulations limit the amount of dividends that may be paid by the bank subsidiary without prior approval of the Commissioner of Banking and Consumer Finance of the State of Mississippi. At December 31, 2003, approximately \$7,142,000 of undistributed earnings of the bank subsidiary included in consolidated surplus and retained earnings was available for future distribution to the Company as dividends, subject to approval by the Board of Directors. The Company cannot predict what dividends, if any, will be paid in the future, however the Board of Directors has established a goal of achieving a 35% dividend payout ratio.

RESULTS OF OPERATIONS

Net Interest Income

Net interest income, the amount by which interest income on loans, investments and other interest earning assets exceeds interest expense on deposits and other borrowed funds, is the single largest component of the Company's income. Management's objective is to provide the largest possible amount of income while balancing interest rate, credit, liquidity and capital risk.

Total interest income decreased \$2,359,000 for the year ended December 31, 2003, as compared with the year ended December 31, 2002, and had decreased \$9,861,000 for the year ended December 31, 2002, as compared with the year ended December 31, 2001. The Company experienced a decline in interest income, particularly from loans, as a result of the decrease in the volume of loans and the decrease in interest rates earned on loans.

Total interest expense decreased \$3,777,000 for the year ended December 31, 2003, as compared with the year ended December 31, 2002, and had decreased \$8,738,000 for the year ended December 31, 2002, as compared with the year ended December 31, 2001. As previously discussed, the Company used brokered time deposits and borrowings from the Federal Home Loan Bank to address its liquidity position. The cost of these funding sources was higher than other more traditional deposit funds, and has had a slightly negative impact on the Company's net margin. As these funds have been repriced more favorably, the Company has realized a positive improvement in its interest margin.

Provision for Loan Losses

The Company continuously monitors its relationships with its loan customers, especially those in concentrated industries such as seafood, gaming and hotel/motel, and their direct and indirect impact on its operations. A thorough analysis of current economic conditions and the quality of the loan portfolio is conducted on a quarterly basis using the latest available information. These analyses are utilized in the computation of the adequacy of the allowance for loan losses. A provision is charged to income on a periodic basis to absorb potential losses based on these analyses. Further information related to the computation of the provision is presented in Note A.

During 2001 and 2002, the Company identified negative events with respect to an overall softening of the economy and negative events with respect to specific credits which required a large increase to the Company's provision for loan losses during those years. The Company believes that this action provided sufficient funds to absorb significant potential losses. Provisions for loan losses amounted to \$2,428,000 and \$2,503,000 for the years ended December 31, 2002 and 2001, respectively. A provision for loan

losses of \$447,000 was charged to expense for the year ended December 31, 2003. Management continues to closely evaluate the entire loan portfolio, in accordance with its policies and procedures and will provide for any future potential losses as deemed necessary. As a part of this evaluation, the Company also closely monitors any improvements to specific credits previously identified in prior years as having a potential loss. Any such improvements and their potential impact on the provision for loan losses are considered on a periodic basis. Although some uncertainty exists, the Company is monitoring positive events with respect to specific credits that may be resolved during 2004.

Other Income

Other income decreased \$408,000 for the year ended December 31, 2003, as compared with the year ended December 31, 2002, primarily as a result of the income realized in 2002 from proceeds from whole life insurance owned by the bank subsidiary.

RELATED PARTIES

The Company extends loans to certain officers and directors and their personal business interests, at terms and rates comparable to other loans of similar credit risks. Further disclosure of these transactions are presented in Note C. The Company has not currently engaged, nor does it have any plans to engage, in any other transactions with any related persons or entities.

LIQUIDITY

Liquidity represents the Company's ability to adequately provide funds to satisfy demands from depositors, borrowers and other commitments by either converting assets to cash or accessing new or existing sources of funds. Management monitors these funds requirements in such a manner as to satisfy these demands and provide the maximum earnings on its earning assets. Note J discloses information relating to financial instruments with off-balance-sheet risk, including letters of credit and outstanding unused loan commitments. The Company closely monitors the potential effects of funding these commitments on its liquidity position.

Deposits, payment of principal and interest on loans, proceeds from maturities of investment securities, earnings on investment securities, and purchases of federal funds and securities sold under agreements to repurchase are the principal sources of funds for the Company. During 2000, the Company began using other, non-traditional sources of funds, including borrowings from the Federal Home Loan Bank. The Company generally anticipates relying on traditional sources of funds, especially deposits and purchases of federal funds, for its liquidity needs in 2004.

THE SARBANES - OXLEY ACT OF 2002

The Sarbanes - Oxley Act of 2002 (the "Act") was signed into law on July 30, 2002. The Act requires the implementation of provisions designed to enhance public company governance, responsibility and disclosure. The issues addressed by the Act include the composition and responsibilities of a public company's board of directors and its committees, especially the Audit and Nominating Committees, the certification of financial statements by the chief executive officer and chief financial officer, timely reporting of trading by insiders and independence of external auditors. The Company has implemented all effective provisions of the Act and is closely monitoring those provisions which have not yet become effective. The Company will take the necessary actions to ensure compliance with the Act, as well as the listing requirements of NASDAQ, on which the Company is registered.

NEW ACCOUNTING PRONOUNCEMENTS

The Financial Accounting Standards Board (FASB) has issued several statements during the current year. Statement 148, "Accounting for Stock-Based Compensation - Transition and Disclosure", Statement 149, "Amendment of Statement 133 on Derivative Instruments and Hedging Activities" and Statement 150, "Accounting for Certain Financial Instruments with Characteristics of Both Liabilities and Equity" are effective for the current year. The Company evaluated the implementation of adopting these new pronouncements and determined that their adoption did not have a material effect on its financial statements.

OFF-BALANCE SHEET ARRANGEMENTS

The Company is a party to off-balance-sheet arrangements in the normal course of business to meet the financing needs of its customers. These arrangements include unused commitments to extend credit, which amounted to \$95,165,000 at December 31, 2003, and irrevocable letters of credit, which amounted to \$3,388,997 at December 31, 2003. The Company uses the same credit policies in making commitments and conditional obligations as it does for on-balance-sheet arrangements. Since some of the commitments and irrevocable letters of credit may expire without being drawn upon, the total amounts do not necessarily represent future cash requirements. As discussed previously, the Company carefully monitors its liquidity needs and considers the cash requirements, especially for loan commitments, in making decisions on investments and obtaining funds from its other sources. Further information relating to off-balance sheet instruments can be found in Note J.

QUANTITATIVE AND QUALITATIVE DISCLOSURE ABOUT MARKET RISK

Market risk is the risk of loss arising from adverse changes in market prices and rates. Interest rate risk is the most significant market risk affecting the Company. Other types of market risk, such as foreign currency exchange rate risk and commodity price risk, do not arise in the normal course of the Company's business activities. Also, the Company does not currently, and has no plans to, engage in trading activities or use derivative or off-balance sheet instruments to manage interest rate risk.

The Company has risk management policies in place to monitor and limit exposure to market risk. The Asset/Liability Committee (ALCO), whose members include the chief executive officer and senior and middle management from the financial, lending, investing, and deposit areas, is responsible for the day-to-day operating guidelines, approval of strategies affecting net interest income and coordination of activities within policy limits established by the Board of Directors based on the Company's tolerance for risk. Specifically, the key objectives of the Company's asset/liability management program are to manage the exposure of planned net interest margins to unexpected changes due to interest rate fluctuations. These efforts will also affect loan pricing policies, deposit interest rate policies, asset mix and volume guidelines and liquidity. The ALCO committee reports to the Board of Directors on a quarterly basis. During 2004, the ALCO committee will enhance its risk management analysis through the implementation of software to assist in balance sheet management, interest rate risk analysis and portfolio modeling.

The Company has implemented a conservative approach to its asset/liability management. The net interest margin is managed on a daily basis largely as a result of the management of the liquidity needs of the bank subsidiary. The Company generally follows a policy of investing in short term U. S. Agency securities with maturities of two years or less. Due to the low interest rate environment, the duration of investments has been extended to seven years or less with call provisions. The loan portfolio consists of a 40% - 60% blend of fixed and floating rate loans. It is the general loan policy to offer loans with maturities of five years or less; however the market is now dictating floating rate terms to be extended to fifteen years. On the liability side, more than 66% of the deposits are demand and savings transaction accounts. Additionally, more than 75% of the certificates of deposit mature within eighteen months. Since the Company's deposits are generally not rate-sensitive, they are considered to be core deposits. The short term nature of the financial assets and liabilities allows the Company to meet the dual requirements of liquidity and interest rate risk management.

The interest rate sensitivity tables below provide additional information about the Company's financial instruments that are sensitive to changes in interest rates. The negative gap in 2004 is mitigated by the nature of the Company's deposits, whose characteristics have been previously described. The tabular disclosure reflects contractual interest rate repricing dates and

contractual maturity dates. Loan maturities have been adjusted for reserve for loan losses. There have been no adjustments for such factors as prepayment risk, early calls of investments, the effect of the maturity of balloon notes or the early withdrawal of deposits. The Company does not believe that the aforementioned factors have a significant impact on expected maturity.

Interest rate sensitivity at December 31, 2003 was as follows (in thousands):

	2004	2005	2006	2007	2008	Beyond	Total	12/31/03 Fair Value
Loans, net	\$ 195,878	\$ 27,523	\$ 6,233	\$ 10,399	\$ 33,757	\$ 17,734	\$ 291,524	\$ 294,685
Average rate	5.58%	7.60%	7.51%	6.22%	5.92%	6.05%	5.82%	
Securities	31,568	14,560	9,320	31,852	50,176	76,337	213,813	213,987
Average rate	3.45	5.11	3.34	3.55	3.63	4.31	3.87	
Total Financial Assets	227,446	42,083	15,553	42,251	83,933	94,071	505,337	508,672
Average rate	5.75	7.12	5.86	4.52	4.83	4.74	5.31	
Deposits	273,265	15,088	4,387	2,035	1,356	2	296,133	297,008
Average rate	1.38	3.69	3.11	3.39	3.39	3.67	1.96	
Long-term funds	10,273	184	236	168	160	6,159	17,180	18,076
Average rate	1.30	4.91	4.91	4.91	4.91	6.26	4.96	
Total Financial Liabilities	283,538	15,272	4,623	2,203	1,516	6,161	313,313	315,084
Average rate	1.37	3.71	3.24	3.55	3.59	6.26	2.34	

Interest rate sensitivity at December 31, 2002 was as follows (in thousands):

	2003	2004	2005	2006	2007	Beyond	Total	12/31/02 Fair Value
Loans, net	\$ 235,880	\$ 21,654	\$ 28,094	\$ 7,485	\$ 7,965	\$ 4,521	\$ 305,599	\$ 307,501
Average rate	5.98%	8.05%	7.91%	8.04%	6.56%	6.66%	6.47%	
Securities	54,478	35,122	7,799	20,605	25,939	27,056	170,999	171,437
Average rate	4.22	3.48	4.31	4.00	4.13	4.65	3.93	
Total Financial Assets	290,358	56,776	35,893	28,090	33,904	31,577	476,598	478,938
Average rate	5.73	6.17	7.44	5.70	4.93	5.04	5.59	
Deposits	290,104	9,199	10,536	1,579	1,053	4	312,475	314,495
Average rate	2.59	3.43	4.12	4.02	4.02	3.89	3.47	
Long-term funds	153	382	193	105	97	5,717	6,647	7,398
Average rate	5.29	5.32	5.25	5.25	5.25	6.37	6.24	
Total Financial Liabilities	290,257	9,581	10,729	1,684	1,150	5,721	319,122	321,893
Average rate	2.59	3.51	4.14	4.09	4.12	6.37	3.53	

PEOPLES FINANCIAL CORPORATION AND SUBSIDIARIES

DECEMBER 31,	2003	2002	2001
Assets			
Cash and due from banks	\$ 33,861,029	\$ 39,654,247	\$ 32,034,976
Available for sale securities	207,486,172	151,483,997	142,902,274
Held to maturity securities, fair value of \$4,527,000-2003; \$18,026,000-2002; \$38,986,000-2001	4,352,854	17,587,690	38,278,962
Federal Home Loan Bank Stock, at cost	1,974,200	1,927,000	1,870,500
Loans	297,922,945	312,296,263	347,168,766
Less: Allowance for loan losses	6,398,694	6,696,911	5,658,210
Loans, net	291,524,251	305,599,352	341,510,556
Bank premises and equipment, net	17,952,504	17,059,400	18,117,908
Other real estate	1,383,451	1,195,720	1,799,527
Accrued interest receivable	3,096,002	2,858,190	3,728,850
Other assets	13,804,039	12,773,580	6,768,669
Total assets	\$ 575,434,502	\$ 550,139,176	\$ 587,012,222
Liabilities & Shareholders' Equity			
Liabilities:			
Deposits:			
Demand, non-interest bearing	\$ 76,423,904	\$ 75,698,316	\$ 76,215,302
Savings and demand, interest bearing	173,913,054	164,954,932	145,248,560
Time, \$100,000 or more	58,182,870	74,064,356	105,446,070
Other time deposits	64,036,836	73,456,208	85,632,730
Total deposits	372,556,664	388,173,812	412,542,662
Federal funds purchased and securities sold under agreements to repurchase	95,039,261	67,245,703	82,488,859
Borrowings from Federal Home Loan Bank	17,069,848	6,313,077	5,548,988
Notes payable	110,235	334,371	336,251
Other liabilities	7,154,545	6,340,607	6,026,436
Total liabilities	491,930,553	468,407,570	506,943,196
Shareholders' Equity:			
Common Stock, \$1 par value, 15,000,000 shares authorized, 5,557,379, 5,583,472, and 5,620,239 shares issued and outstanding at December 31, 2003, 2002 and 2001, respectively	5,557,379	5,583,472	5,620,239
Surplus	65,780,254	65,780,254	65,780,254
Undivided profits	11,574,074	8,510,341	7,052,559
Unearned compensation	(94,899)	(143,043)	(174,043)
Accumulated other comprehensive income, net of tax	687,141	2,000,582	1,790,017
Total shareholders' equity	83,503,949	81,731,606	80,069,026
Total liabilities and shareholders' equity	\$ 575,434,502	\$ 550,139,176	\$ 587,012,222

See Notes to Consolidated Financial Statements.

CONSOLIDATED STATEMENTS OF INCOME

PEOPLES FINANCIAL CORPORATION AND SUBSIDIARIES

YEARS ENDED DECEMBER 31,	2003	2002	2001
Interest income:			
Interest and fees on loans	\$ 17,181,975	\$ 20,061,342	\$ 28,174,153
Interest and dividends on securities:			
U. S. Treasury	1,320,545	1,397,148	2,064,729
U. S. Government agencies and corporations	5,882,469	5,161,358	5,881,969
States and political subdivisions	368,934	350,498	514,351
Other investments	249,185	257,339	445,784
Interest on federal funds sold	62,109	196,207	203,566
Total interest income	25,065,217	27,423,892	37,284,552
Interest expense:			
Deposits	4,383,806	8,052,732	15,696,840
Long-term borrowings	456,694	382,912	437,144
Federal funds purchased and securities sold under agreements to repurchase	998,139	1,179,993	2,219,601
Total interest expense	5,838,639	9,615,637	18,353,585
Net interest income	19,226,578	17,808,255	18,930,967
Provision for allowance for losses on loans	447,000	2,428,000	2,503,000
Net interest income after provision for allowance for losses on loans	18,779,578	15,380,255	16,427,967
Other operating income:			
Trust department income and fees	1,458,037	1,419,463	1,418,847
Service charges on deposit accounts	6,709,852	6,822,638	6,388,406
Gain on liquidation, sale and calls of securities	57,356	209,659	243,126
Other income	1,512,169	1,920,452	1,205,750
Total other operating income	9,737,414	10,372,212	9,256,129
Other operating expense:			
Salaries and employee benefits	10,989,269	10,923,858	11,447,070
Net occupancy	1,466,797	1,506,113	1,178,261
Equipment rentals, depreciation and maintenance	2,760,125	2,802,343	2,776,745
Other expense	6,247,956	6,641,849	5,795,068
Total other operating expense	21,464,147	21,874,163	21,197,144
Income before income taxes and extraordinary gain	7,052,845	3,878,304	4,486,952
Income taxes	2,035,000	687,582	1,082,000
Income before extraordinary gain	5,017,845	3,190,722	3,404,952
Extraordinary gain, net of income tax			594,000
Net income	\$ 5,017,845	\$ 3,190,722	\$ 3,998,952
Basic and diluted earnings per share	\$.90	\$.57	\$.71
Basic and diluted earnings per share before extraordinary gain	\$.90	\$.57	\$.60

CONSOLIDATED STATEMENTS OF SHAREHOLDERS' EQUITY

PEOPLES FINANCIAL CORPORATION AND SUBSIDIARIES

	Number of Common Shares		Common Stock		Surplus
Balance, January 1, 2001	5,795,207	\$	5,795,207	\$	65,780,254
Comprehensive Income:					
Net income					
Net unrealized gain on available for sale securities, net of tax					
Reclassification adjustment for available for sale securities called or sold in current year, net of tax					
Total comprehensive income					
Purchase of common shares by ESOP					
Allocation of ESOP shares					
Cash dividends (\$.12 per share)					
Dividend declared (\$.12 per share)					
Issuance of stock for stock incentive plan	6,886		6,886		
Effect of stock retirement on accrued dividends					
Retirement of stock	(181,854)		(181,854)		
Balance, December 31, 2001	5,620,239		5,620,239		65,780,254
Comprehensive Income:					
Net income					
Net unrealized gain on available for sale securities, net of tax					
Reclassification adjustment for available for sale securities called or sold in current year, net of tax					
Total comprehensive income					
Allocation of ESOP shares					
Cash dividends (\$.12 per share)					
Dividend declared (\$.12 per share)					
Issuance of stock for stock incentive plan	7,142		7,142		
Retirement of stock	(43,909)		(43,909)		
Balance, December 31, 2002	5,583,472		5,583,472		65,780,254
Comprehensive Income:					
Net income					
Net unrealized loss on available for sale securities, net of tax					
Reclassification adjustment for available for sale securities called or sold in current year, net of tax					
Total comprehensive income					
Allocation of ESOP shares					
Cash dividends (\$.14 per share)					
Dividend declared (\$.15 per share)					
Retirement of stock	(26,093)		(26,093)		
Balance, December 31, 2003	5,557,379	\$	5,557,379	\$	65,780,254

See Notes to Consolidated Financial Statements.

Undivided Profits	Unearned Compensation	Accumulated Other Comprehensive Income	Comprehensive Income	Total
\$ 7,093,830	\$ (535,840)	\$ 583,406	\$	\$ 78,716,857
3,998,952			\$ 3,998,952	3,998,952
		1,359,541	1,359,541	1,359,541
		(152,930)	(152,930)	(152,930)
			<u>\$ 5,205,563</u>	
	(80,043)			(80,043)
	441,840			441,840
(675,388)				(675,388)
(674,428)				(674,428)
93,097				99,983
15,545				15,545
(2,799,049)				(2,980,903)
7,052,559	(174,043)	1,790,017		80,069,026
3,190,722			\$ 3,190,722	3,190,722
		471,295	471,295	471,295
		(260,730)	(260,730)	(260,730)
			<u>\$ 3,401,287</u>	
	31,000			31,000
(672,080)				(672,080)
(670,017)				(670,017)
92,846				99,988
(483,689)				(527,598)
8,510,341	(143,043)	2,000,582		81,731,606
5,017,845			\$ 5,017,845	5,017,845
		(1,195,267)	(1,195,267)	(1,195,267)
		(118,174)	(118,174)	(118,174)
			<u>\$ 3,704,404</u>	
	48,144			48,144
(778,570)				(778,570)
(833,607)				(833,607)
(341,935)				(368,028)
\$ 11,574,074	\$ (94,899)	\$ 687,141	\$	\$ 83,503,949

PEOPLES FINANCIAL CORPORATION AND SUBSIDIARIES

YEARS ENDED DECEMBER 31,	2003	2002	2001
Cash flows from operating activities:			
Net income	\$ 5,017,845	\$ 3,190,722	\$ 3,998,952
Adjustments to reconcile net income to net cash provided by operating activities:			
(Gain) loss on sales of other real estate	(248,170)	43,666	(118,716)
Gain on sales, calls and liquidation of securities	(57,356)	(209,659)	(243,126)
Gain on sale of bank premises	(130,503)	(182,861)	
Stock incentive plan		99,988	99,983
Depreciation	1,676,000	1,842,000	1,864,827
Provision for allowance for loan losses	447,000	2,428,000	2,503,000
Provision for losses on other real estate	210,358	533,848	409,264
Changes in assets and liabilities:			
Accrued interest receivable	(237,812)	870,660	768,863
Other assets	(323,618)	448,969	140,233
Other liabilities	304,832	40,412	(638,777)
Net cash provided by operating activities	6,658,576	9,105,745	8,784,503
Cash flows from investing activities:			
Proceeds from maturities, sales and calls of available for sale securities	130,443,200	145,297,421	46,359,462
Investment in available for sale securities	(188,388,210)	(153,352,620)	(139,028,899)
Proceeds from maturities and calls of held to maturity securities	13,234,836	20,745,000	143,715,000
Investment in held to maturity securities		(53,728)	(83,942,007)
Investment in Federal Home Loan Bank stock	(47,200)	(56,500)	(223,200)
Proceeds from sales of other real estate	827,665	1,010,723	1,044,119
Loans, net decrease	12,650,517	32,498,774	27,242,762
Proceeds from sale of bank premises	445,068	355,620	
Acquisition of premises and equipment	(2,883,669)	(956,251)	(1,649,463)
Other assets	325,425	(6,282,010)	521,482
Net cash provided by (used in) investing activities	(33,392,368)	39,206,429	(5,960,744)
Cash flows from financing activities:			
Demand and savings deposits, net increase	9,683,710	19,189,386	15,851,110
Time deposits made, net decrease	(25,300,858)	(43,558,236)	(17,032,525)
Notes payable		72,799	
Principal payments on notes	(175,992)	(43,679)	(14,273)
Cash dividends	(1,448,587)	(1,346,508)	(1,297,316)
Retirement of common stock	(368,028)	(527,598)	(2,980,903)
Borrowings from Federal Home Loan Bank	10,756,771	764,089	
Repayments to Federal Home Loan Bank			(17,610,519)
Federal funds purchased and securities sold under agreements to repurchase, net increase (decrease)	27,793,558	(15,243,156)	17,149,775
Net cash provided by (used in) financing activities	20,940,574	(40,692,903)	(5,934,651)
Net increase (decrease) in cash and cash equivalents	(5,793,218)	7,619,271	(3,110,892)
Cash and cash equivalents, beginning of year	39,654,247	32,034,976	35,145,868
Cash and cash equivalents, end of year	\$ 33,861,029	\$ 39,654,247	\$ 32,034,976

See Notes to Consolidated Financial Statements.

PEOPLES FINANCIAL CORPORATION AND SUBSIDIARIES

NOTE A - BUSINESS AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES:

Business of The Company

Peoples Financial Corporation is a one-bank holding company headquartered in Biloxi, Mississippi. Its two operating subsidiaries are The Peoples Bank, Biloxi, Mississippi, and PFC Service Corp. Its principal subsidiary is The Peoples Bank, Biloxi, Mississippi, which provides a full range of banking, financial and trust services to individuals and small and commercial businesses operating in Harrison, Hancock, Stone and Jackson counties.

Principles of Consolidation

The consolidated financial statements include the accounts of Peoples Financial Corporation and its wholly-owned subsidiaries, The Peoples Bank, Biloxi, Mississippi, and PFC Service Corp. All significant intercompany transactions and balances have been eliminated in consolidation.

Basis of Accounting

Peoples Financial Corporation and Subsidiaries recognize assets and liabilities, and income and expense, on the accrual basis of accounting. The preparation of financial statements in conformity with generally accepted accounting principles requires Management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from these estimates.

Cash and Due from Banks

The Company is required to maintain average reserve balances in its vault or on deposit with the Federal Reserve Bank. The average amount of these reserve requirements was approximately \$10,220,000, \$9,013,000 and \$8,420,000 for the years ending December 31, 2003, 2002 and 2001, respectively.

The Company's bank subsidiary maintained account balances in excess of amounts insured by the Federal Deposit Insurance Corporation. At December 31, 2003, the bank subsidiary had excess deposits of \$8,001,000. These amounts were uninsured and uncollateralized.

Securities

The classification of securities is determined by Management at the time of purchase. Securities are classified as held to maturity when the Company has the positive intent and ability to hold the security until maturity. Securities held to maturity are stated at amortized cost.

Securities not classified as held to maturity are classified as available for sale and are stated at fair value. Unrealized gains and losses, net of tax, on these securities are recorded in shareholders' equity as accumulated other comprehensive income.

The amortized cost of available for sale securities and held to maturity securities is adjusted for amortization of premiums and accretion of discounts to maturity, determined using the interest method. Such amortization and accretion is included in interest income on securities. The specific identification method is used to determine realized gains and losses on sales of securities, which are reported as gain on sale and calls of securities in other operating income.

Loans

The loan portfolio consists of commercial and industrial and real estate loans within the Company's trade area in South Mississippi. The loan policy establishes guidelines relating to pricing, repayment terms, collateral standards including loan to value (LTV) limits, appraisal and environmental standards, lending authority, lending limits and documentation requirements.

Loans are stated at the amount of unpaid principal, reduced by unearned income and the allowance for loan losses. Interest on loans is recognized over the terms of each loan based on the unpaid principal balance.

Loan origination fees are recognized as income when received. Revenue from these fees is not material to the financial statements.

The Company places loans on a nonaccrual status when, in the opinion of Management, they possess sufficient uncertainty as to timely collection of interest or principal so as to preclude the

recognition in reported earnings of some or all of the contractual interest. Accrued interest on loans classified as nonaccrual is reversed at the time the loans are placed on nonaccrual. Interest received on nonaccrual loans is applied against principal. Loans are restored to accrual status when the obligation is brought current or has performed in accordance with the contractual terms for a reasonable period of time and the ultimate collectibility of the total contractual principal and interest is no longer in doubt. Loans classified as nonaccrual are generally identified as impaired loans. The policy for recognizing income on impaired loans is consistent with the nonaccrual policy.

Allowance for Loan Losses

The allowance for loan losses is established through provisions for loan losses charged against earnings. Loans deemed to be uncollectible are charged against the allowance for loan losses, and subsequent recoveries, if any, are credited to the allowance.

The allowance for loan losses is based on Management's evaluation of the loan portfolio under current economic conditions and is an amount that Management believes will be adequate to absorb probable losses on loans existing at the reporting date. The evaluation includes Management's assessment of several factors: review and evaluations of specific loans, changes in the nature and volume of the loan portfolio, current and anticipated economic conditions and the related impact on specific borrowers and industry groups, a study of loss experience, a review of classified, nonperforming and delinquent loans, the estimated value of any underlying collateral, an estimate of the possibility of loss based on the risk characteristics of the portfolio, adverse situations that may affect the borrower's ability to repay and the results of regulatory examinations. This evaluation is inherently subjective as it requires material estimates that may be susceptible to significant change.

Bank Premises and Equipment

Bank premises and equipment are stated at cost, less accumulated depreciation. Depreciation is computed primarily by the straight-line method based on the estimated useful lives of the related assets.

Other Real Estate

Other real estate acquired through foreclosure is carried at the lower of cost (primarily outstanding loan balance) or estimated market value, less estimated costs to sell. If, at foreclosure, the carrying value of the loan is greater than the estimated market value of the property acquired, the excess is charged against the allowance for loan losses and any subsequent adjustments are charged to expense. Costs of operating and maintaining the properties, net of related income and gains (losses) on their disposition, are charged to expense as incurred.

Trust Department Income and Fees

Corporate trust fees are accounted for on an accrual basis and personal trust fees are recorded when received for 2003. All trust fees were recorded for 2002 and 2001 when received.

Income Taxes

The Company files a consolidated tax return with its wholly-owned subsidiaries. The tax liability of each entity is allocated based on the entity's contribution to consolidated taxable income. The provision for applicable income taxes is based upon reported income and expenses as adjusted for differences between reported income and taxable income. The primary differences are exempt income on state, county and municipal securities; differences in provisions for losses on loans as compared to the amount allowable for income tax purposes; directors' and officers' insurance; depreciation for income tax purposes over (under) that reported for financial statements; gains reported under the installment sales method for tax purposes and gains on the sale of bank premises which were structured under the provisions of Section 1031 of the Internal Revenue Code.

Advertising

Advertising costs are expensed as incurred.

Leases

All leases are accounted for as operating leases in accordance with the terms of the leases.

Earnings Per Share

Basic and diluted earnings per share are computed on the basis of the weighted average number of common shares outstanding, 5,563,015, 5,603,834 and 5,629,872 in 2003, 2002 and 2001, respectively.

Statements of Cash Flows

The Company has defined cash and cash equivalents to include cash and due from banks. The Company paid \$5,937,967, \$9,929,357 and \$18,768,387 in 2003, 2002 and 2001, respectively, for interest on deposits and borrowings. Income tax payments totaled \$2,537,223, \$1,639,612 and \$1,847,250 in 2003, 2002 and 2001, respectively. Loans transferred to other real estate amounted to \$977,584, \$984,430 and \$2,073,113 in 2003, 2002 and 2001, respectively. The income tax effect on the accumulated other comprehensive income was (\$676,621), \$108,473 and \$621,587, at December 31, 2003, 2002 and 2001, respectively.

Reclassifications

Certain reclassifications have been made to the prior year statements to conform to current year presentation. The reclassifications had no effect on prior year net income.

NOTE B - SECURITIES:

The amortized cost and estimated fair value of securities at December 31, 2003, 2002, and 2001, respectively, are as follows (in thousands):

December 31, 2003	Amortized cost	Gross unrealized gains	Gross unrealized losses	Estimated fair value
Available for sale securities:				
Debt securities:				
U. S. Treasury	\$ 49,977	\$ 465	\$ (38)	\$ 50,404
U. S. Government agencies and corp.	145,507	778	(801)	145,484
States and political subdivisions	7,154	161	(48)	7,267
Total debt securities	202,638	1,404	(887)	203,155
Equity securities	3,829	709	(207)	4,331
Total available for sale securities	\$ 206,467	\$ 2,113	\$ (1,094)	\$ 207,486
Held to maturity securities:				
U. S. Treasury	\$ 1,000	\$ 17	\$	\$ 1,017
States and political subdivisions	3,353	159	(2)	3,510
Total held to maturity securities	\$ 4,353	\$ 176	\$ (2)	\$ 4,527

December 31, 2002	Amortized cost	Gross unrealized gains	Gross unrealized losses	Estimated fair value
Available for sale securities:				
Debt securities:				
U. S. Treasury	\$ 46,948	\$ 709	\$ (1)	\$ 47,656
U. S. Government agencies and corp.	93,627	1,468		95,095
States and political subdivisions	4,061	89	(11)	4,139
Total debt securities	144,636	2,266	(12)	146,890
Equity securities	3,828	766		4,594
Total available for sale securities	\$ 148,464	\$ 3,032	\$ (12)	\$ 151,484
Held to maturity securities:				
U. S. Treasury	\$ 5,998	\$ 120	\$	\$ 6,118
U. S. Government agencies and corp.	7,000	143		7,143
States and political subdivisions	4,590	175		4,765
Total held to maturity securities	\$ 17,588	\$ 438	\$	\$ 18,026

December 31, 2001	Amortized cost	Gross unrealized gains	Gross unrealized losses	Estimated fair value
Available for sale securities:				
Debt securities:				
U. S. Treasury	\$ 20,975	\$ 207	\$ (10)	\$ 21,172
U. S. Government agencies and corp.	113,494	1,557	(74)	114,977
States and political subdivisions	1,759	4		1,763
Total debt securities	136,228	1,768	(84)	137,912
Equity securities	3,971	1,019		4,990
Total available for sale securities	\$ 140,199	\$ 2,787	\$ (84)	\$ 142,902
Held to maturity securities:				
U. S. Treasury	\$ 18,948	\$ 283	\$	\$ 19,231
U. S. Government agencies and corp.	13,687	306		13,993
States and political subdivisions	5,644	136	(18)	5,762
Total held to maturity securities	\$ 38,279	\$ 725	\$ (18)	\$ 38,986

The amortized cost and estimated fair value of debt securities at December 31, 2003, (in thousands) by contractual maturity, are shown below. Expected maturities will differ from contractual

maturities because borrowers may have the right to call or prepay obligations with or without call or prepayment penalties.

	Amortized cost	Estimated fair value
Available for sale securities:		
Due in one year or less	\$ 30,168	\$ 30,438
Due after one year through five years	104,057	104,696
Due after five years through ten years	63,596	63,256
Due after ten years	4,817	4,765
Totals	\$ 202,638	\$ 203,155
Held to maturity securities:		
Due in one year or less	\$ 1,130	\$ 1,149
Due after one year through five years	1,213	1,241
Due after five years through ten years	283	299
Due after ten years	1,727	1,838
Totals	\$ 4,353	\$ 4,527

Proceeds from maturities and calls of held to maturity debt securities during 2003, 2002 and 2001 were \$13,234,836, \$20,745,000 and \$143,715,000, respectively. There were no sales of held to maturity debt securities during 2003, 2002 and 2001. Proceeds from maturities and calls of available for sale debt securities were \$130,443,200, \$145,297,421 and \$46,359,462 during 2003, 2002 and 2001, respectively. Available for sale debt securities were sold in 2001 for a gain of \$243,126. There were no sales of available for sale debt securities during 2003 and 2002. The Company realized gains of \$57,356 and \$209,659 from the liquidation of equity securities in 2003 and 2002, respectively.

Securities with an amortized cost of approximately \$154,105,000, \$139,625,000 and \$149,013,000 at December 31, 2003, 2002 and 2001, respectively, were pledged to secure public deposits, federal funds purchased and other balances required by law.

Federal Home Loan Bank (FHLB) common stock was purchased during 1999 in order for the Company to participate in certain FHLB programs. The amount to be invested in FHLB stock was calculated according to FHLB guidelines as a percentage of certain mortgage loans. The investment is carried at cost. Dividends received are reinvested in FHLB stock.

NOTE C - LOANS:

The composition of the loan portfolio was as follows (in thousands):

December 31,	2003	2002	2001
Real estate, construction	\$ 14,896	\$ 21,534	\$ 25,636
Real estate, mortgage	223,246	197,478	224,524
Loans to finance agricultural production and other loans to farmers	3,980	7,375	7,241
Commercial and industrial loans	41,832	65,946	71,271
Loans to individuals for household, family and other consumer expenditures	11,020	15,990	15,068
Obligations of states and political subdivisions (primarily industrial revenue bonds and local government tax anticipation notes)	2,560	3,637	3,233
All other loans	389	336	196
Totals	\$ 297,923	\$ 312,296	\$ 347,169

Transactions in the allowance for loan losses are as follows (in thousands):

	2003	2002	2001
Balance, January 1	\$ 6,697	\$ 5,658	\$ 4,568
Recoveries	600	676	561
Loans charged off	(1,345)	(2,065)	(1,974)
Provision for allowance for loan losses	447	2,428	2,503
Balance, December 31	\$ 6,399	\$ 6,697	\$ 5,658

In the ordinary course of business, the Company extends loans to certain officers and directors and their personal business interests at, in the opinion of Management, terms and rates comparable to

other loans of similar credit risks. These loans do not involve more than normal risk of collectability and do not include other unfavorable features.

An analysis of the activity with respect to such loans to related parties is as follows (in thousands):

	2003	2002	2001
Balance, January 1	\$ 10,080	\$ 12,340	\$ 14,118
New loans and advances	14,453	19,529	20,511
Repayments	(15,587)	(21,789)	(22,289)
Balance, December 31	\$ 8,946	\$ 10,080	\$ 12,340

Industrial revenue bonds with a carrying value of \$502,187, \$700,356 and \$898,687 at December 31, 2003, 2002 and 2001, respectively, were pledged to secure public deposits.

Nonaccrual loans amounted to \$7,415,073, \$6,550,169 and \$650,215 at December 31, 2003, 2002 and 2001, respectively.

The total recorded investment in impaired loans amounted to \$7,415,073, \$6,550,169 and \$650,215 at December 31, 2003, 2002 and 2001, respectively. The amount of that recorded investment in

impaired loans for which there is a related allowance for loan losses was \$7,415,073, \$6,550,169 and \$650,215 at December 31, 2003, 2002 and 2001, respectively. At December 31, 2003, 2002 and 2001, the average recorded investment in impaired loans was \$7,400,000, \$6,602,000 and \$661,000, respectively. The amount of interest not accrued on these loans was approximately \$261,000 and \$212,000 in 2003 and 2002, respectively. The amount of interest not accrued on these loans did not have a significant effect on earnings in 2001.

NOTE D - BANK PREMISES AND EQUIPMENT:

Bank premises and equipment are shown as follows (in thousands):

December 31,	Estimated useful lives	2003	2002	2001
Land		\$ 4,522	\$ 4,839	\$ 4,988
Buildings	5-40 years	17,533	15,584	15,315
Furniture, fixtures and equipment	3-10 years	12,173	11,596	11,107
Totals, at cost		34,228	32,019	31,410
Less: Accumulated depreciation		16,275	14,960	13,292
Totals		\$ 17,953	\$ 17,059	\$ 18,118

NOTE E - BORROWINGS FROM FEDERAL HOME LOAN BANK:

At December 31, 2003, the Company had \$5,000,000 outstanding in advances under a \$76,000,000 line of credit with the Federal Home Loan Bank of Dallas ("FHLB"). This advance bore interest at 6.50% and matures in 2010. The Company also had \$10,000,000

outstanding under the line which bears interest at 1.06% and matures January 9, 2004. The advances are collateralized by a blanket floating lien on the Company's residential first mortgage loans.

NOTE F - NOTES PAYABLE:

December 31,	2003	2002	2001
Small Business Administration, outstanding mortgage on property acquired. The note bears interest at 5 3/8% & is payable at \$1,952 monthly through January 2004.	\$	\$ 147,029	\$ 162,208
Notes payable on automobiles. The notes are non interest-bearing and payable in monthly installments through January 2005.	15,336	44,299	
RiverHills Bank, \$750,000 line of credit for Peoples Financial Corporation Employee Stock Ownership Plan, secured by the guarantee of the Company; Interest at New York Prime (4.00% at December 31, 2003) due quarterly, principal due at maturity in June 2004.	94,899	143,043	174,043
Totals	\$ 110,235	\$ 334,371	\$ 336,251

The maturities of notes payable are as follows:

2004	\$ 109,769
2005	466
Total	\$ 110,235

NOTE G - INCOME TAXES:

Federal income taxes payable (or refundable) and deferred taxes (or deferred charges) as of December 31, 2003, 2002 and 2001, included in other assets or other liabilities, were as follows (in thousands):

December 31,	2003	2002	2001
Deferred tax assets:			
Allowance for loan losses	\$ 2,114	\$ 2,215	\$ 1,542
Employee benefit plans' liabilities	1,328	1,145	938
Other	836	685	431
Deferred tax assets	<u>(4,278)</u>	<u>(4,045)</u>	<u>(2,911)</u>
Deferred tax liabilities:			
Accumulated depreciation	732	820	947
Deferred gain on sale of bank premises	1,784	1,750	1,687
Installment sales	13	13	13
Unrealized gains on available for sale securities, charged to equity	347	1,026	813
Deferred tax liabilities	<u>2,876</u>	<u>3,609</u>	<u>3,460</u>
Net deferred taxes	(1,402)	(436)	549
Current payable (refundable)	(20)	200	75
Totals	<u>\$ (1,422)</u>	<u>\$ (236)</u>	<u>\$ 624</u>

Income taxes consist of the following components (in thousands):

Years Ended December 31,	2003	2002	2001
Current	\$ 2,322	\$ 1,886	\$ 2,202
Deferred	(287)	(1,198)	(1,120)
Totals	<u>\$ 2,035</u>	<u>\$ 688</u>	<u>\$ 1,082</u>

Deferred income taxes (benefits) resulted from the following (in thousands):

Years Ended December 31,	2003	2002	2001
Depreciation	\$ (88)	\$ (127)	\$ (124)
Provision for loan losses	101	(628)	(580)
Officers' and directors' life insurance	(183)	(281)	(220)
Deferred gain on sale of bank premises	34	63	
Unrealized gain on available for sale securities, charged to equity	(679)	213	620
Other	(151)	(225)	(196)
Totals	<u>\$ (966)</u>	<u>\$ (985)</u>	<u>\$ (500)</u>

Income taxes amounted to less than the amounts computed by applying the U.S. Federal income tax rate of 34.0% for 2003, 2002 and

2001, to earnings before income taxes. The reason for these differences is shown below (in thousands):

Years Ended December 31,	2003 Amount	%	2002 Amount	%	2001 Amount	%
Taxes computed at statutory rate	\$ 2,398	34.0	\$ 1,319	34.0	\$ 1,526	34.0
Increase (decrease) resulting from:						
Tax-exempt interest income	(184)	(2.6)	(187)	(4.8)	(259)	(5.8)
Non-deductible interest	8	0.1	15	0.4	30	0.7
Credit for certified historic structure					(113)	(2.5)
Non-taxable life insurance proceeds			(201)	(5.2)	(62)	(1.4)
Dividend exclusion	(54)	(0.8)	(63)	(1.6)	(96)	(2.1)
Other, net	(133)	(1.8)	(195)	(5.1)	56	1.2
Total income taxes	\$ 2,035	28.9	\$ 688	17.7	\$ 1,082	24.1

NOTE H - SHAREHOLDERS' EQUITY:

Banking regulations limit the amount of dividends that may be paid by the bank subsidiary without prior approval of the Commissioner of Banking and Consumer Finance of the State of Mississippi. At December 31, 2003, approximately \$7,142,000 of undistributed earnings of the bank subsidiary included in consolidated surplus and retained earnings was available for future distribution to the Company as dividends, subject to the approval by Board of Directors.

On May 24, 2000, the Company's Board of Directors approved the repurchase of up to 2.50% of the outstanding shares of the Company's common stock. As of December 31, 2003, the 147,633 shares available under this plan had been repurchased and retired. On December 8, 2000, the Company's Board of Directors approved the repurchase of 146,304 shares of the outstanding common stock from one unrelated shareholder at a purchase price of \$2,432,000. This repurchase was executed on January 2, 2001, and these shares were subsequently retired. On November 26, 2002, the Company's Board of Directors approved the repurchase of up to 2.50% of the outstanding shares of the Company's common stock. As of December 31, 2003, 21,613 shares had been repurchased and retired under the plan approved November 26, 2002.

On May 23, 2001, the Company's Board of Directors approved a stock incentive program for two executive officers. Under this plan, whole shares valued as of the distribution date at \$50,000 were distributed to each of these officers who continue to meet the eligibility requirements on June 15, 2001, and on January 15 of the four succeeding years. On June 15, 2001 and January 15, 2002, a total of 6,886 and 7,142 shares, respectively, of Peoples Financial Corporation common stock was issued. This incentive program was established subsequent to the surrender of collateral assignment

split dollar policies that had been obtained on behalf of these executives. On December 6, 2002, the Company's Board of Directors approved the termination of the stock incentive program, which was replaced by the acquisition of endorsement split dollar policies for the two executive officers.

On November 25, 2003, the Company's Board of Directors approved a semi-annual dividend of \$.15 per share. This dividend has a record date of January 9, 2004 and a distribution date of January 16, 2004.

The bank subsidiary is subject to various regulatory capital requirements administered by the federal banking agencies. Failure to meet minimum capital requirements can initiate certain mandatory, and possibly additional discretionary, actions by the regulators that, if undertaken, could have a direct material effect on the bank subsidiary's financial statements. Under capital adequacy guidelines and the regulatory framework for prompt corrective action, the bank subsidiary must meet specific capital guidelines that involve quantitative measures of the bank subsidiary's assets, liabilities and certain off-balance sheet items as calculated under regulatory accounting practices. The bank subsidiary's capital amounts and classification are also subject to qualitative judgments by the regulators about components, risk weightings and other factors.

Quantitative measures established by regulation to ensure capital adequacy require the bank subsidiary to maintain minimum amounts and ratios of Total and Tier 1 capital to risk-weighted assets, and Tier 1 capital to average assets.

As of December 31, 2003, the most recent notification from the Federal Deposit Insurance Corporation categorized the bank subsidiary as well capitalized under the regulatory framework for prompt corrective action. To be categorized as well capitalized, the bank subsidiary must have a Total risk-based capital ratio of

10.00% or greater, a Tier I risk-based capital ratio of 6.00% or greater and a Leverage capital ratio of 5.00% or greater. There are no conditions or events since that notification that Management believes have changed the bank subsidiary's category.

The bank subsidiary's actual capital amounts and ratios and required minimum capital amounts and ratios for 2003, 2002 and 2001, are as follows (in thousands):

	Actual		For Capital Adequacy Purposes	
	Amount	Ratio	Amount	Ratio
December 31, 2003:				
Total Capital (to Risk Weighted Assets)	\$ 85,583	24.81%	\$ 27,600	8.00%
Tier I Capital (to Risk Weighted Assets)	81,270	23.56%	13,800	4.00%
Tier I Capital (to Average Assets)	81,270	14.44%	22,511	4.00%
December 31, 2002:				
Total Capital (to Risk Weighted Assets)	\$ 83,768	24.16%	\$ 27,720	8.00%
Tier I Capital (to Risk Weighted Assets)	79,437	22.91%	13,860	4.00%
Tier I Capital (to Average Assets)	79,437	13.98%	22,798	4.00%
December 31, 2001:				
Total Capital (to Risk Weighted Assets)	\$ 83,201	21.90%	\$ 30,930	8.00%
Tier I Capital (to Risk Weighted Assets)	78,453	20.65%	15,195	4.00%
Tier I Capital (to Average Assets)	78,453	13.25%	23,677	4.00%

NOTE I - OTHER INCOME AND EXPENSES:

Other income consisted of the following:

Years Ended December 31,	2003	2002	2001
Other service charges, commissions and fees	\$ 226,946	\$ 189,835	\$ 208,332
Gain on sale of bank premises	130,503	182,861	
Rentals	473,292	494,055	511,751
Income from proceeds of insurance policies		592,436	
Other income	681,428	461,265	485,667
Totals	\$ 1,512,169	\$ 1,920,452	\$ 1,205,750

Other expenses consisted of the following:

Years Ended December 31,	2003	2002	2001
Advertising	\$ 515,538	\$ 433,037	\$ 463,103
Data processing	282,420	268,044	233,390
FDIC and state banking assessments	117,271	127,234	132,629
Legal and accounting	382,161	395,016	272,337
Postage and freight	167,517	227,871	211,792
Stationery, printing and supplies	250,976	169,583	191,803
Other real estate	59,887	636,789	328,133
ATM expense	2,223,479	2,477,104	2,282,118
Federal Reserve service charges	154,701	153,783	152,815
Conferences and classes	120,293	99,325	112,469
Taxes and licenses	267,319	276,910	252,491
Consulting fees	363,282	45,880	11,250
Trust expense	381,233	373,483	350,525
Other	961,879	957,790	800,213
Totals	\$ 6,247,956	\$ 6,641,849	\$ 5,795,068

NOTE J - FINANCIAL INSTRUMENTS WITH OFF-BALANCE-SHEET RISK:

The Company is a party to financial instruments with off-balance-sheet risk in the normal course of business to meet the financing needs of its customers. These financial instruments include commitments to extend credit and irrevocable letters of credit. These instruments involve, to varying degrees, elements of credit and interest rate risk in excess of the amount recognized in the balance sheet. The contract amounts of those instruments reflect the extent of involvement the bank subsidiary has in particular classes of financial instruments. The Company's exposure to credit loss in the event of nonperformance by the other party to the financial instrument for commitments to extend credit and irrevocable letters of credit is represented by the contractual amount of those instruments. The Company uses the same credit policies in making commitments and conditional obligations as it does for on-balance-sheet instruments.

Commitments to extend credit are agreements to lend to a customer as long as there is no violation of any conditions established in the agreement. Irrevocable letters of credit written are conditional commitments issued by the Company to guarantee the performance of a customer to a third party. Commitments and irrevocable letters of credit generally have fixed expiration dates or other termination clauses and may require payment of a fee. Since

some of the commitments and irrevocable letters of credit may expire without being drawn upon, the total amounts do not necessarily represent future cash requirements. The Company evaluated each customer's creditworthiness on a case-by-case basis. The amount of collateral obtained upon extension of credit is based on Management's credit evaluation of the customer. Collateral obtained varies but may include equipment, real property and inventory.

The Company generally grants loans to customers in its primary trade area of Harrison, Hancock, Jackson and Stone counties.

At December 31, 2003, 2002 and 2001, the Company had outstanding irrevocable letters of credit aggregating \$3,388,997, \$2,849,400 and \$3,344,016, respectively. At December 31, 2003, 2002 and 2001, the Company had outstanding unused loan commitments aggregating \$95,165,000, \$87,382,000 and \$74,254,000, respectively. Approximately \$46,688,000, \$43,543,000 and \$27,810,000 of outstanding commitments were at fixed rates and the remainder were at variable rates at December 31, 2003, 2002 and 2001, respectively.

NOTE K - CONTINGENCIES:

During 2003, a lawsuit was filed against the Company's bank subsidiary. This litigation, which specifies damages of \$1,500,000 and punitive damages of \$12,500,000, has been filed by an insurance company trying to reverse a settlement it voluntarily agreed to in 2000. The bank subsidiary intends to vigorously contest the allegations of the complaint. The bank is involved in

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

NOTE L - CONDENSED PARENT COMPANY ONLY FINANCIAL INFORMATION:

Peoples Financial Corporation began its operations September 30, 1985, when it acquired all the outstanding stock of The Peoples

Bank, Biloxi, Mississippi. A condensed summary of its financial information is shown below.

CONDENSED BALANCE SHEETS (IN THOUSANDS)

December 31,	2003	2002	2001
Assets			
Investments in subsidiaries, at underlying equity:			
Bank subsidiary	\$ 82,957	\$ 81,558	\$ 79,483
Nonbank subsidiary	1	1	1
Cash in bank subsidiary	546	84	263
Other assets	1,462	1,462	1,821
Total assets	\$ 84,966	\$ 83,105	\$ 81,568
Liabilities and Shareholders' Equity			
Notes payable	\$ 95	\$ 143	\$ 174
Other liabilities	1,367	1,230	1,325
Total liabilities	1,462	1,373	1,499
Shareholders' equity	83,504	81,732	80,069
Total liabilities and shareholders' equity	\$ 84,966	\$ 83,105	\$ 81,568

CONDENSED STATEMENTS OF INCOME (IN THOUSANDS)

Years Ended December 31,	2003	2002	2001
Income			
Earnings of unconsolidated bank subsidiary:			
Distributed earnings	\$ 2,280	\$ 1,400	\$ 700
Undistributed earnings	2,739	1,752	3,375
Interest income	5	7	14
Other income	79	230	41
Total income	5,103	3,389	4,130
Expenses			
Other expense	86	185	183
Total expenses	86	185	183
Income before income taxes	5,017	3,204	3,947
Income tax (benefit)	(1)	13	(52)
Net income	\$ 5,018	\$ 3,191	\$ 3,999

CONDENSED STATEMENTS OF CASH FLOWS (IN THOUSANDS)

Years Ended December 31,	2003	2002	2001
Cash flows from operating activities:			
Net income	\$ 5,018	\$ 3,191	\$ 3,999
Adjustments to reconcile net income to net cash provided by operating activities:			
Gain on liquidation of investment	(57)	(210)	
Net income of unconsolidated subsidiaries	(5,019)	(3,152)	(4,075)
Stock incentive plan		100	100
Changes in assets and liabilities:			
Other assets		15	71
Net cash provided by (used in) operating activities	(58)	(56)	95
Cash flows from investing activities:			
Proceeds from liquidation of investment	57	352	
Dividends from unconsolidated subsidiary	2,280	1,400	700
Net cash provided by investing activities	2,337	1,752	700
Cash flows from financing activities:			
Retirement of stock	(368)	(528)	(2,981)
Dividends paid	(1,449)	(1,347)	(1,297)
Net cash used in financing activities	(1,817)	(1,875)	(4,278)
Net increase (decrease) in cash	462	(179)	(3,483)
Cash, beginning of year	84	263	3,746
Cash, end of year	\$ 546	\$ 84	\$ 263

Peoples Financial Corporation paid income taxes of \$2,537,223, \$1,639,612 and \$1,847,250 in 2003, 2002 and 2001, respectively. No

interest was paid during the three years ended December 31, 2003.

NOTE M - EMPLOYEE BENEFIT PLAN:

The Company sponsors the Peoples Financial Corporation Employee Stock Ownership Plan (ESOP). Employees who work more than 1,000 hours are eligible to participate in the ESOP. The Plan included 401(k) provisions and the former Gulf National Bank Profit Sharing Plan. Effective January 1, 2001, the ESOP was amended to separate the 401(k) funds into the Peoples Financial Corporation 401(k) Plan. The separation had no impact on the eligibility or benefits provided to participants of either plan. The 401(k) provides for a matching contribution of 75% of the amounts contributed by the employee (up to 6% of compensation). Contributions are determined by the Board of Directors and may be paid either in cash or Peoples Financial Corporation capital stock. Total contributions to the plan charged to operating expense were \$360,000, \$360,000 and \$734,000 in 2003, 2002 and 2001, respectively.

ESOP debt for acquisition of Company shares has been guaranteed by the Company and is reported as a debt of the Company. Shares pledged as collateral are reported as unearned compensation in equity. ESOP debt for acquisition from The Peoples Bank, Biloxi, Mississippi, is eliminated in consolidation. As shares are committed to be released, the Company reports compensation expense equal to the current market price of the shares, and the shares become outstanding for net income per share computations. Dividends on allocated ESOP shares are recorded as a reduction of retained earnings; dividends on unallocated ESOP shares are recorded as a reduction of debt and accrued interest.

Compensation expense of \$7,021,816, \$7,167,143 and \$7,681,720 relating to the ESOP was recorded during 2003, 2002 and 2001, respectively. The ESOP held 467,499, 533,733 and 560,010 allocated shares at December 31, 2003, 2002, and 2001 respectively.

The Company established an Executive Supplemental Income Plan and a Directors' Deferred Income Plan, which provide for pre-retirement and post-retirement benefits to certain key executives and directors. The Company has acquired insurance policies, with the bank subsidiary as owner and beneficiary, that it may use as a source to pay potential benefits to the plan participants. These contracts are carried at their cash surrender value, which amounted to \$10,588,084, \$10,276,887 and \$4,558,220 at December 31, 2003, 2002 and 2001, respectively. The present value of accumulated benefits under these plans, using an interest rate of 7.50% and 8.00% and the interest ramp-up method for 2003 and 2002 and using an interest rate of 7.5% and the projected unit cost method for 2001, has been accrued. The accrual amounted to \$3,375,938, \$2,882,009 and \$2,418,114 at December 31, 2003, 2002 and 2001, respectively.

The Company also has additional plans for non-vested post-retirement benefits for certain key executives and directors. The Company has acquired insurance policies, with the bank subsidiary as owner and beneficiary, that it may use as a source to pay potential benefits to the plan participants. Additionally, there are two endorsement split dollar policies, with the bank subsidiary as owner and beneficiary, which provide a guaranteed death benefit

to the participants' beneficiaries. These contracts are carried at their cash surrender value, which amounted to \$989,004, \$686,381 and \$420,221 at December 31, 2003, 2002 and 2001, respectively. The present value of accumulated benefits under these plans using an interest rate of 7.50% in 2003, 2002 and 2001 and the projected unit cost method has been accrued. The accrual amounted to \$530,372, \$485,534 and \$341,819 at December 31, 2003, 2002 and 2001, respectively.

The Company provides post-retirement health insurance to certain of its retired employees. Employees are eligible to participate in the retiree health plan if they retire from active service no earlier than their Social Security normal retirement age, which varies from 65 to 67 based on the year of birth. In addition, the employee must have at least 25 continuous years of service with the Company immediately preceding retirement. However, any active employee who was at least age 65 as of January 1, 1995, does not have to meet the 25 years of service requirement. The accumulated post-retirement benefit obligation at January 1, 1995, was \$517,599, which the Company elected to amortize over 20 years. The Company reserves the right to modify, reduce or eliminate these health benefits.

The following is a summary of the components of the net periodic post-retirement benefit cost:

Years Ended December 31,	2003	2002	2001
Service cost	\$ 157,515	\$ 107,533	\$ 67,981
Interest cost	104,409	94,603	70,461
Amortization of net transition obligation	20,600	20,600	20,600
Net periodic post-retirement benefit cost	\$ 282,524	\$ 222,736	\$ 159,042

The discount rate used in determining the accumulated post-retirement benefit obligation was 6.25% in 2003, 6.50% in 2002, and 7.25% in 2001. The assumed health care cost trend rate used in measuring the accumulated post-retirement benefit obligation was 10.00% in 2003. The rate was assumed to decrease gradually to 5.00% for 2013 and remain at that level thereafter. If the health care cost trend rate assumptions were increased 1.00%, the accumulated post-retirement benefit obligation as of December 31, 2003, would be increased by 24.39%, and the aggregate of the

service and interest cost components of the net periodic post-retirement benefit cost for the year then ended would have increased by 28.72%. If the health care cost trend rate assumptions were decreased 1.00%, the accumulated post-retirement benefit obligation as of December 31, 2003, would be decreased by 18.64%, and the aggregate of the service and interest cost components of the net periodic post-retirement benefit cost for the year then ended would have decreased by 21.37%.

The following is a reconciliation of the accumulated post-retirement benefit obligation:

Accumulated post-retirement benefit obligation as of December 31, 2002	\$1,693,122
Service cost	135,006
Interest cost	104,409
Actuarial loss	294,994
Benefits paid	(74,549)
Accumulated post-retirement benefit obligation as of December 31, 2003	<u>\$2,152,982</u>

December 31,	2003	2002	2001
Accumulated post-retirement benefit obligation:			
Retirees	\$ 659,859	\$ 422,403	\$ 395,895
Eligible to retire	1,493,123	50,218	44,172
Not eligible to retire		1,220,501	881,657
Total	<u>2,152,982</u>	<u>1,693,122</u>	<u>1,321,724</u>
Plan assets at fair value	<u>-0-</u>	<u>-0-</u>	<u>-0-</u>
Accumulated post-retirement benefit obligation in excess of plan assets	2,152,982	1,693,122	1,321,724
Unrecognized transition obligation	(226,597)	(247,197)	(267,797)
Unrecognized cumulative net gain from past experience different from that assumed and from changes in assumptions	(887,947)	(615,462)	(394,611)
Accrued post-retirement benefit cost	<u>\$ 1,038,438</u>	<u>\$ 830,463</u>	<u>\$ 659,316</u>

NOTE N - FAIR VALUE OF FINANCIAL INSTRUMENTS:

SFAS 107, "Disclosures About Fair Value of Financial Instruments," requires all entities to disclose the fair value of financial instruments, both assets and liabilities recognized and not recognized in the statement of condition, for which it is practical to estimate its fair value. SFAS 107 excluded certain financial instruments and all nonfinancial instruments from its disclosure requirements. Accordingly, the aggregate fair value amounts presented do not represent the underlying value of the Company. In preparing these disclosures, Management made highly sensitive estimates and assumptions in developing the methodology to be utilized in the computation of fair value. These estimates and assumptions were formulated based on judgments regarding economic conditions and risk characteristics of the financial instruments that were present at the time the computations were made. Events may occur that alter these conditions and thus perhaps change the assumptions as well. A change in the assumptions might affect the fair value of the financial instruments disclosed in this footnote. In addition, the tax consequences related to the realization of the unrealized gains and losses have not been computed or disclosed herein. These fair value estimates, methods and assumptions are set forth below.

Cash and Due from Banks

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

Available for Sale Securities

The fair value of available for sale securities is based on quoted market prices.

Held to Maturity Securities

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

Loans

The fair value of loans is estimated by discounting the future cash flows using the current rates at which similar loans would be made to borrowers with similar credit ratings for the remaining maturities. The cash flows considered in computing the fair value of such loans are segmented into categories relating to the nature of the contract and collateral based on contractual principal maturities. Appropriate adjustments are made to reflect probable credit losses. Cash flows have not been adjusted for such factors as prepayment risk or the effect of the maturity of balloon notes.

Deposits

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

Federal Funds Purchased and Securities Sold under Agreements to Repurchase

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

Long Term Funds

The fair value of long term funds is computed by discounting the cash flows using current borrowing rates.

The following table presents carrying amounts and estimated fair values for financial assets and financial liabilities at

December 31, 2003, 2002 and 2001 (in thousands):

	2003		2002		2001	
	Carrying Amount	Fair Value	Carrying Amount	Fair Value	Carrying Amount	Fair Value
Financial Assets:						
Cash and due from banks	\$ 33,861	\$ 33,861	\$ 39,654	\$ 39,654	\$ 32,035	\$ 32,035
Available for sale securities	206,467	207,486	151,484	151,484	142,902	142,902
Held to maturity securities	4,353	4,527	17,588	18,026	38,279	38,986
Loans, net	291,524	294,685	305,599	307,501	341,511	345,155
Financial Liabilities:						
Deposits:						
Non-interest bearing	76,424	76,424	75,698	75,698	76,215	76,215
Interest bearing	296,133	297,008	312,476	314,495	336,328	339,640
Total deposits	372,557	373,432	388,174	390,193	412,543	415,855
Federal funds purchased and securities sold under agreements to repurchase	95,039	95,039	67,246	67,246	82,489	82,489
Long term funds	17,180	18,076	6,647	7,398	5,885	6,356

NOTE O - EXTRAORDINARY GAIN:

In 2001, the Company agreed to an out of court settlement of an insurance claim. An extraordinary gain of \$594,000, net of taxes,

was realized in the prior year as a result of this settlement.

PEOPLES FINANCIAL CORPORATION AND SUBSIDIARIES

Board of Directors
Peoples Financial Corporation and Subsidiaries
Biloxi, Mississippi

We have audited the accompanying consolidated statements of condition of Peoples Financial Corporation and Subsidiaries as of December 31, 2003, 2002 and 2001, and the related consolidated statements of income, shareholders' equity and cash flows for the years then ended. These financial statements are the responsibility of the Company's Management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by Management, as well as evaluating the overall financial statement

presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of Peoples Financial Corporation and Subsidiaries at December 31, 2003, 2002 and 2001, and the results of its operations and its cash flows for the years then ended, in conformity with accounting principles generally accepted in the United States of America.

Certified Public Accountants

Piltz, Williams, Larosa & Co.

PILTZ, WILLIAMS, LAROSA & CO.

Biloxi, Mississippi
January 21, 2004

FIVE-YEAR COMPARATIVE SUMMARY OF SELECTED FINANCIAL INFORMATION (IN THOUSANDS EXCEPT PER SHARE DATA)

PEOPLES FINANCIAL CORPORATION AND SUBSIDIARIES

	2003	2002	2001	2000	1999
Balance Sheet Summary					
Total assets	\$ 575,435	\$ 550,139	\$ 587,012	\$ 587,244	\$ 537,972
Available for sale securities	207,486	151,484	142,902	48,168	33,076
Held to maturity securities	4,353	17,588	38,279	98,052	115,273
Loans, net of unearned discount	297,923	312,296	347,169	377,476	332,510
Deposits	372,557	388,174	412,543	413,724	394,681
Borrowings from FHLB	17,070	6,313	5,549	23,160	
Long term notes payable	110	334	336	291	274
Shareholders' equity	83,504	81,732	80,069	78,717	77,767
Summary of Operations					
Interest income	\$ 25,065	\$ 27,424	\$ 37,285	\$ 42,250	\$ 35,440
Interest expense	5,838	9,616	18,354	19,401	14,441
Net interest income	19,227	17,808	18,931	22,849	20,999
Provision for loan losses	447	2,428	2,503	4,192	120
Net interest income after provision for loan losses	18,780	15,380	16,428	18,657	20,879
Non-interest income	9,737	10,372	9,256	7,678	6,767
Non-interest expense	(21,464)	(21,874)	(21,197)	(19,632)	(18,438)
Income before taxes and extraordinary gain	7,053	3,878	4,487	6,703	9,208
Applicable income taxes	2,035	687	1,082	2,065	2,958
Extraordinary gain			594		
Net income	\$ 5,018	\$ 3,191	\$ 3,999	\$ 4,638	\$ 6,250
Per Share Data					
Basic and diluted earnings per share	\$.90	\$.57	\$.71	\$.79	\$ 1.06
Basic and diluted earnings per share before extraordinary gain	.90	.57	.60	.79	1.06
Dividends per share	.29	.24	.24	.21	.20
Book value	15.03	14.64	14.25	13.58	13.17
Weighted average number of shares	5,563,015	5,603,834	5,629,872	5,857,232	5,905,344
Selected Ratios					
Return on average assets	.88%	.56%	.68%	.82%	1.21%
Return on average equity	6.07%	3.94%	5.04%	5.93%	8.26%
Capital formation rate	2.17%	2.08%	1.72%	1.22%	5.74%
Primary capital to average assets	15.79%	15.39%	14.47%	14.68%	15.86%
Risk-based capital ratios:					
Tier I	23.56%	22.91%	20.65%	19.97%	22.45%
Total	24.81%	24.16%	21.90%	21.13%	23.69%

Note: All share and per share data have been given retroactive effect for the two for one stock split effective April 17, 2000.

Summary of Quarterly Results of Operations (in thousands except per share data)

PEOPLES FINANCIAL CORPORATION AND SUBSIDIARIES

Quarter Ended, 2003	March 31	June 30	September 30	December 31
Interest income	\$ 6,410	\$ 6,332	\$ 6,174	\$ 6,149
Net interest income	4,725	4,708	4,883	4,911
Provision for loan losses	179	139	65	64
Income before income taxes	1,384	1,599	2,116	1,954
Net income	1,037	1,088	1,511	1,382
Basic and diluted earnings per share	.19	.19	.27	.25

Quarter Ended, 2002	March 31	June 30	September 30	December 31
Interest income	\$ 7,118	\$ 6,993	\$ 6,787	\$ 6,526
Net interest income	4,282	4,396	4,507	4,623
Provision for loan losses	445	168	136	1,679
Income before income taxes and extraordinary items	894	787	1,551	646
Net income	667	658	1,145	721
Basic and diluted earnings per share	.12	.12	.20	.13

Market Information

The Company's stock is traded under the symbol PFBX and is quoted in publications under "PplFnMS". The following table sets

forth the high and low sale prices of the Company's common stock as reported on the NASDAQ Stock Market.

Year	Quarter	High	Low	Dividend per share
2003	1st	\$ 15	\$ 13	\$.12
	2nd	16	13	
	3rd	17	14	.14
	4th	18	15	
2002	1st	\$ 15	\$ 12	\$.12
	2nd	15	13	
	3rd	15	12	.12
	4th	15	12	

There were 661 holders of record of common stock of the Company at January 30, 2004, and 5,557,379 shares issued and outstanding. The principal source of funds to the Company for payment of dividends is the earnings of the bank subsidiary. The Commissioner of Banking and Consumer Finance of the State of Mississippi must

approve all dividends paid to the Company by its bank subsidiary. Although Management cannot predict what dividends, if any, will be paid in the future, the Company has paid regular semiannual cash dividends since its founding in 1985.