

2001 Annual Report

MBC
MIDDLEFIELD BANC CORP.



An Introduction

It takes foresight, planning and commitment when laying the groundwork to establish, then achieve, long-term goals. Our founding partners had this vision.

Over one hundred years have passed since our inception, and the experience gained over that time is secondary to the relationships we've built.

We expect that they would be proud of our achievements, and that is the principal going forward.



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*Someone's
sitting in the
shade today
because someone
planted a tree a
long time ago.*

Warren Buffet

To Our Shareholders and Friends:

It is, indeed, an honor to be able to write to you from the perspective of one hundred years of service to our communities. From the modest beginnings in September 1901, your bank has grown to be an organization of which we can all be very proud. We celebrated that service and anniversary throughout 2001, concluding with a community-wide celebration on September 15th. You will find some remembrances of that event and of our history included herein.

Even though it was a year of celebration, 2001 was also a year of great challenges, both inside and outside of the banking industry. The events of September 11th will, of course, shape our history and perspectives for many years to come. However, the year also saw the Federal Reserve cut interest rates a record setting eleven times. The Prime Rate on December 31st was one half of what it was on January 1st! Although these actions were designed to aid the economy of the nation, they did, in fact, work to greatly compress our net interest margin and, therefore, constrict our earnings.

We believe, however, that we were prepared for the challenges offered during the year. We are pleased to report that our company did achieve a record level of earnings during the year just concluded. Furthermore, our levels of assets, loans and deposits were at an all-time high.

Net income for the year was \$2,270,607, which represents a modest increase from 2000. Our corresponding returns on average assets and average equity were 1.22% and 11.89%, respectively. Although these return ratios were down slightly from 2000, they do reflect strength in comparison to our peers and in our high level of capital.

During 2001, growth was also achieved from a perspective of service to our customers. In August, we introduced our internet banking site. At www.middlefieldbank.com you may have full transactional access to your accounts, as well as the capability to pay your bills, all from the comfort of your home or office. During the same month, we were pleased to work with Hiram College as we installed an ATM at the Kennedy Center on campus. September witnessed the grand opening of our Chardon office at 348 Center Street. This banking office, our fifth, surpassed its first year growth goals within the first four months of operation. We concluded the year by purchasing land in the Village of Orwell in Ashtabula County. Our regulatory applications have been filed and we would anticipate opening during the first quarter of 2003.

Our total assets grew in excess of twelve percent during 2001. Our year-end totals of \$197,857,964, were fueled by growth on both sides of the balance sheet. Loans increased 13%, while deposits grew nearly 14%. Total stockholders' equity finished the year at \$19,786,807. This high level of capital is reflective of the strength of our company.

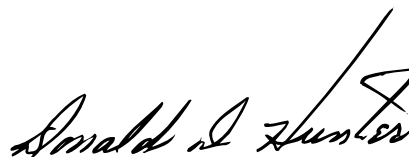
We are pleased to have provided our shareholders with a dividend level that increased nearly 30% during the year. The support and loyalty of our shareholders is greatly appreciated.

As we enter our second century of service, we are ever mindful of our heritage. We recognize that our course is closely linked with those people that we call friends and neighbors. Our passion remains strong in desiring to offer only the best in community banking services. We thank you for your support.

Sincerely,



Thomas G. Caldwell
President and Chief Executive Officer



Donald D. Hunter
Chairman, Board of Directors



Thomas G. Caldwell



All things arise



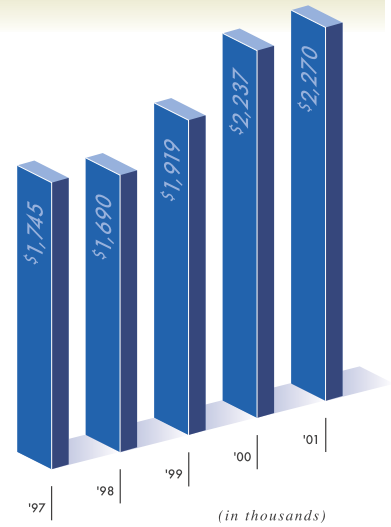
from simple beginnings...

Middlefield Banc Corp.
*Consolidated Audited
 Financial Statements*

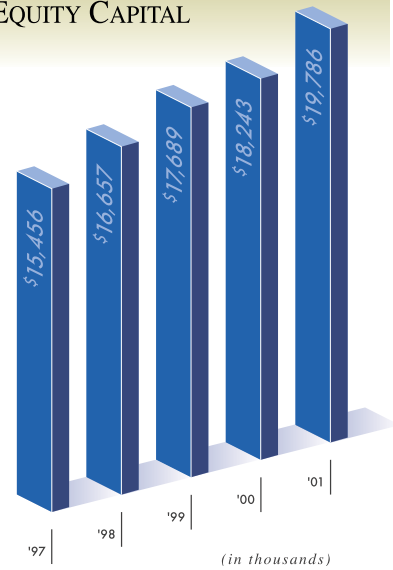
December 31, 2001

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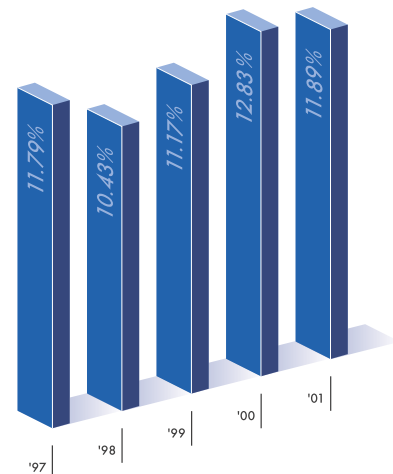
NET INCOME



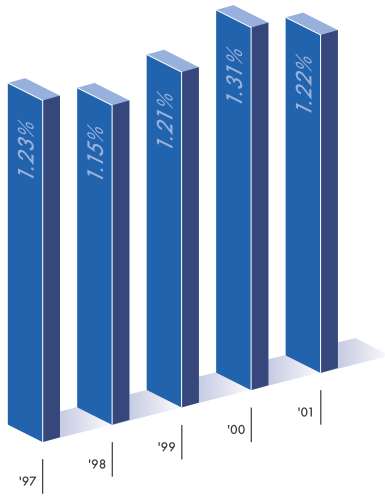
EQUITY CAPITAL



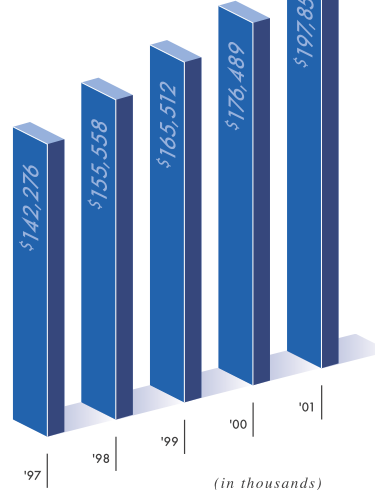
RETURN ON AVERAGE EQUITY



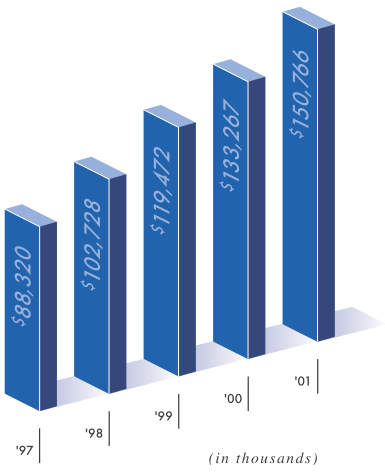
RETURN ON AVERAGE ASSETS



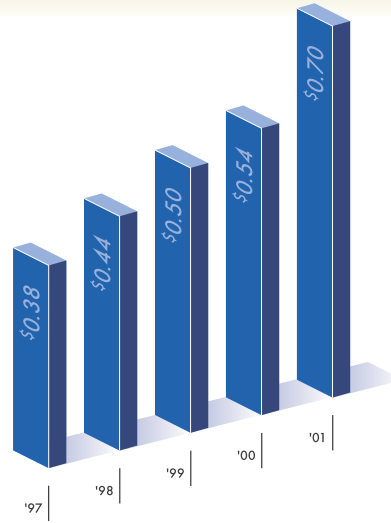
TOTAL ASSETS



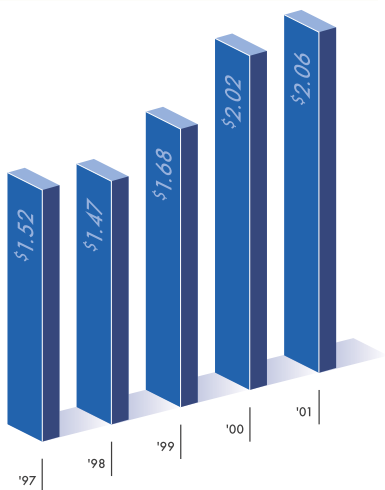
NET LOANS OUTSTANDING



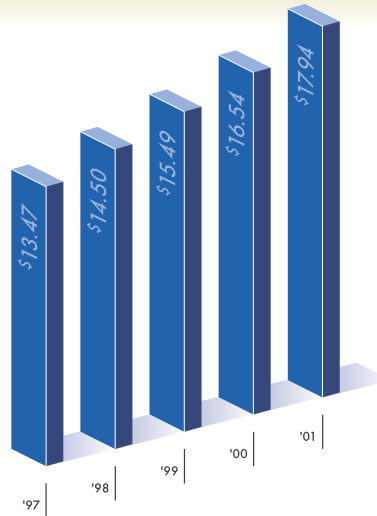
DIVIDENDS PER SHARE



EARNINGS PER SHARE



BOOK VALUE PER SHARE



CONSOLIDATED BALANCE SHEET

	December 31,	
	2001	2000
ASSETS		
Cash and due from banks	\$ 3,443,435	\$ 3,574,875
Federal funds sold	2,450,000	1,265,000
Cash and cash equivalents	<u>5,893,435</u>	<u>4,839,875</u>
Interest-bearing deposits in other institutions	1,240,207	984,441
Investment securities available for sale	21,179,786	11,868,337
Investment securities held to maturity (estimated market value of \$10,471,978 and \$17,942,255)	10,229,068	17,942,310
Loans	152,828,355	135,304,215
Less allowance for loan losses	2,062,252	2,037,322
Net loans	<u>150,766,103</u>	<u>133,266,893</u>
Premises and equipment	6,244,797	5,432,472
Accrued interest and other assets	<u>2,304,568</u>	<u>2,154,485</u>
TOTAL ASSETS	<u>\$ 197,857,964</u>	<u>\$ 176,488,813</u>
LIABILITIES		
Deposits:		
Noninterest-bearing demand	\$ 24,952,407	\$ 23,155,904
Interest-bearing demand	6,523,152	6,116,094
Money market	7,940,807	9,127,760
Savings	41,518,906	32,260,775
Time	86,447,456	76,505,513
Total deposits	<u>167,382,728</u>	<u>147,166,046</u>
Short-term borrowings	660,678	543,222
Other borrowings	9,301,334	9,861,596
Accrued interest and other liabilities	726,417	674,587
TOTAL LIABILITIES	<u>178,071,157</u>	<u>158,245,451</u>
STOCKHOLDERS' EQUITY		
Common stock, no par value; 5,000,000 shares authorized, 1,148,676 shares issued	6,287,011	6,287,011
Retained earnings	14,842,519	13,343,980
Accumulated other comprehensive income	133,717	88,811
Treasury stock, at cost (45,722 shares)	(1,476,440)	(1,476,440)
TOTAL STOCKHOLDERS' EQUITY	<u>19,786,807</u>	<u>18,243,362</u>
TOTAL LIABILITIES AND STOCKHOLDERS' EQUITY	<u>\$ 197,857,964</u>	<u>\$ 176,488,813</u>

See accompanying notes to consolidated financial statements.



CONSOLIDATED STATEMENT OF INCOME

	Year Ended December 31,		
	2001	2000	1999
INTEREST INCOME			
Interest and fees on loans	\$ 11,807,799	\$ 10,853,292	\$ 9,408,603
Interest-bearing deposits in other institutions	61,718	97,037	81,211
Federal funds sold	138,415	99,320	90,676
Investment securities:			
Taxable	1,235,922	1,195,504	1,281,341
Tax-exempt	462,715	525,017	586,788
Total interest income	<u>13,706,569</u>	<u>12,770,170</u>	<u>11,448,619</u>
INTEREST EXPENSE			
Deposits	6,198,365	5,311,657	4,539,351
Short-term borrowings	15,411	64,031	8,425
Other borrowings	534,146	534,196	500,500
Total interest expense	<u>6,747,922</u>	<u>5,909,884</u>	<u>5,048,276</u>
NET INTEREST INCOME	6,958,647	6,860,286	6,400,343
Provision for loan losses	<u>170,000</u>	<u>275,000</u>	<u>296,000</u>
NET INTEREST INCOME AFTER PROVISION FOR LOAN LOSSES	<u>6,788,647</u>	<u>6,585,286</u>	<u>6,104,343</u>
NONINTEREST INCOME			
Service charges on deposit accounts	930,431	823,888	667,220
Investment securities gains (losses)	97,807	-	(606)
Other income	165,955	158,775	137,744
Total noninterest income	<u>1,194,193</u>	<u>982,663</u>	<u>804,358</u>
NONINTEREST EXPENSE			
Salaries and employee benefits	2,316,342	2,240,522	2,258,779
Occupancy expense	291,706	320,539	334,199
Equipment expense	292,168	283,174	235,703
Data processing costs	361,839	315,011	292,059
Professional fees	247,222	212,298	152,346
Ohio state franchise tax	225,081	208,457	222,240
Other expense	1,007,016	828,616	759,048
Total noninterest expense	<u>4,741,374</u>	<u>4,408,617</u>	<u>4,254,374</u>
Income before income taxes	3,241,466	3,159,332	2,654,327
Income taxes	<u>970,859</u>	<u>922,661</u>	<u>735,318</u>
NET INCOME	<u>\$ 2,270,607</u>	<u>\$ 2,236,671</u>	<u>\$ 1,919,009</u>
EARNINGS PER SHARE			
Basic	\$ 2.06	\$ 2.02	\$ 1.68
Diluted	2.06	2.02	1.68

See accompanying notes to consolidated financial statements.

CONSOLIDATED STATEMENT OF CHANGES IN STOCKHOLDERS' EQUITY

	Common Stock Shares	Amount	Retained Earnings	Accumulated Other Comprehensive Income (Loss)	Treasury Stock	Total Stockholders' Equity	Comprehensive Income
Balance, December 31, 1998	1,148,67	\$ 6,287,011	\$ 10,355,898	\$ 13,888	\$ -	\$16,656,797	
Net income			1,919,009			1,919,009	\$1,919,009
Other comprehensive income:							
Unrealized loss on available for sale securities net of tax benefit of \$53,843				(104,519)		(104,519)	(104,519)
Comprehensive income						(572,343)	\$1,814,490
Cash dividends (\$.50 per share)			(572,343)			(572,343)	
Purchase of treasury stock					(306,175)	(306,175)	
Sale of treasury stock					96,286	96,286	
Balance, December 31, 1999	1,148,676	6,287,011	11,702,564	(90,631)	(209,889)	17,689,055	
Net income			2,236,671			2,236,671	\$2,236,671
Other comprehensive income:							
Unrealized gain on available for sale securities net of taxes of \$92,440				179,442		179,442	179,442
Comprehensive income						(595,255)	\$2,416,113
Cash dividends (\$.54 per share)			(595,255)			(595,255)	
Purchase of treasury stock					(1,311,050)	(1,311,050)	
Sale of treasury stock					44,499	44,499	
Balance, December 31, 2000	1,148,676	6,287,011	13,343,980	88,811	(1,476,440)	18,243,362	
Net income			2,270,607			2,270,607	\$2,270,607
Other comprehensive income:							
Unrealized gain on available for sale securities net of taxes of \$23,133				44,906		44,906	44,906
Comprehensive income						(772,068)	\$ 2,315,513
Cash dividends (\$.70 per share)			(772,068)			(772,068)	
Balance, December 31, 2001	1,148,676	\$ 6,287,011	\$ 14,842,519	\$ 133,717	\$(1,476,440)	\$19,786,807	
				2001	2000	1999	
Components of comprehensive income (loss):							
Change in net unrealized gain (loss) on investments available for sale				\$ 109,459	\$ 179,442	\$ (104,919)	
Realized (gains) losses included in net income, net of (taxes) benefit of \$(33,254), \$0, and \$206				(64,553)	-	400	
Total				\$ 44,906	\$ 179,442	\$ (104,519)	

See accompanying notes to consolidated financial statements



CONSOLIDATED STATEMENT OF CASH FLOWS

	Year Ended December 31,		
	2001	2000	1999
OPERATING ACTIVITIES			
Net income	\$ 2,270,607	\$ 2,236,671	\$ 1,919,009
Adjustments to reconcile net income to net cash provided by operating activities:			
Provision for loan losses	170,000	275,000	296,000
Depreciation and amortization	300,531	352,613	287,641
Amortization of premium and discount on investment securities		69,237	75,563 93,664
Amortization of net deferred loan costs (fees)	(31,666)	35,489	(112,126)
Investment securities (gains) losses	(97,807)	-	606
Deferred income taxes	54,403	(87,521)	(58,739)
Decrease (increase) in accrued interest receivable	140,147	(59,663)	85,288
Increase in accrued interest payable	38,927	84,301	18,700
Other, net	(211,763)	39,943	(19,926)
Net cash provided by operating activities	2,702,616	2,952,396	2,510,117
INVESTING ACTIVITIES			
Decrease (increase) in interest-bearing deposits in other institutions, net	(255,766)	2,361,081	(1,107,918)
Investment securities available for sale:			
Proceeds from repayments and maturities	5,144,986	766,880	4,931,129
Purchases	(16,392,621)	(2,561,359)	(9,842,151)
Proceeds from sales	2,092,980	-	149,885
Investment securities held to maturity:			
Proceeds from repayments and maturities	7,853,057	3,997,990	8,280,098
Purchases	(200,000)	-	-
Proceeds from sales	-	-	1,054,648
Increase in loans, net	(17,637,544)	(14,105,641)	(16,927,161)
Purchase of regulatory stock	(143,100)	(136,100)	(128,800)
Purchase of premises and equipment	(1,112,856)	(150,361)	(520,313)
Net cash used for investing activities	(20,650,864)	(9,827,510)	(14,110,583)
FINANCING ACTIVITIES			
Net increase in deposits	20,216,682	12,071,587	6,266,570
Increase (decrease) in short-term borrowings, net	117,456	(1,964,448)	2,507,670
Proceeds from other borrowings	-	2,000,000	1,000,000
Repayment of other borrowings	(560,262)	(1,740,900)	(973,706)
Purchase of treasury stock	-	(1,311,050)	(306,175)
Sale of treasury stock	-	44,499	96,286
Cash dividends	(772,068)	(595,255)	(572,343)
Net cash provided by financing activities	19,001,808	8,504,433	8,018,302
Increase (decrease) in cash and cash equivalents	1,053,560	1,629,319	(3,582,164)
CASH AND CASH EQUIVALENTS			
AT BEGINNING OF YEAR	4,839,875	3,210,556	6,792,720
CASH AND CASH EQUIVALENTS			
AT END OF YEAR	\$ 5,893,435	\$ 4,839,875	\$ 3,210,556
SUPPLEMENTAL INFORMATION			
Cash paid during the year for:			
Interest on deposits and borrowings	\$ 6,708,995	\$ 5,825,583	\$ 5,029,576
Income taxes	980,000	1,097,000	735,756

See accompanying notes to consolidated financial statements.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

A summary of the significant accounting and reporting policies applied in the presentation of the accompanying financial statements follows:

Nature of Operations and Basis of Presentation

Middlefield Banc Corp. (the "Company") is an Ohio corporation organized to become the holding company of The Middlefield Banking Company (the "Bank"). The Bank is a state-chartered bank located in Ohio. The Company and its subsidiary derive substantially all of their income from banking and bank-related services which include interest earnings on residential real estate, commercial mortgage, commercial, and consumer financings as well as interest earnings on investment securities and deposit services to its customers through five locations. The Company is supervised by the Board of Governors of the Federal Reserve System, while the Bank is subject to regulation and supervision by the Federal Deposit Insurance Corporation and the Ohio Division of Financial Institutions.

The consolidated financial statements of the Company include its wholly-owned subsidiary, the Bank. Significant intercompany items have been eliminated in preparing the consolidated financial statements.

The financial statements have been prepared in conformity with accounting principles generally accepted in the United States of America. In preparing the financial statements, management is required to make estimates and assumptions that affect the reported amounts of assets and liabilities as of the balance sheet date and revenues and expenses for the period. Actual results could differ significantly from those estimates.

Investment Securities

Investment securities are classified at the time of purchase, based on management's intention and ability, as securities held to maturity or securities available for sale. Debt securities acquired with the intent and ability to hold to maturity are stated at cost adjusted for amortization of premium and accretion of discount which are computed using a level yield method and recognized as adjustments of interest income. Certain other debt securities have been classified as available for sale to serve principally as a source of liquidity. Unrealized holding gains and losses for available for sale securities are reported as a separate component of stockholders' equity, net of tax, until realized. Realized security gains and losses are computed using the specific identification method. Interest and dividends on investment securities are recognized as income when earned.

Common stock of the Federal Home Loan Bank ("FHLB") represents ownership in an institution that is wholly-owned by other financial institutions. This equity security is accounted for at cost and classified with other assets.

Loans

Loans are reported at their principal amount net of the allowance for loan losses. Interest income is recognized as income when earned on the accrual method. The accrual of interest is discontinued on a loan when management believes, after considering economic and business conditions, the borrower's financial condition is such that collection of interest is doubtful. Interest received on nonaccrual loans is recorded as income against principal according to management's judgment as to the collectibility of such principal.

Loan origination fees and certain direct loan origination costs are being deferred and the net amount amortized as an adjustment of the related loan's yield. Management is amortizing these amounts over the contractual life of the related loans.

Allowance for Loan Losses

The allowance for loan losses represents the amount which management estimates is adequate to provide for probable loan losses inherent in its loan portfolio. The allowance method is used in providing for loan losses. Accordingly, all loan losses are charged to the allowance, and all recoveries are credited to it. The allowance for loan losses is established through a provision for loan losses which is charged to operations. The provision is based on management's periodic evaluation of the adequacy of the allowance for loan losses which encompasses the overall risk characteristics of the various portfolio segments, past experience with losses, the impact of economic conditions on borrowers, and other relevant factors. The estimates used in determining the adequacy of the allowance for loan losses, including the amounts and timing of future cash flows expected on impaired loans, are particularly susceptible to significant change in the near term.

A loan is considered impaired when it is probable the borrower will not repay the loan according to the original contractual terms of the loan agreement. Management has determined that first mortgage loans on one-to-four family properties and all consumer loans represent large groups of smaller-balance homogeneous loans that are to be collectively evaluated. Loans that experience insignificant payment delays, which are defined as 90 days or less, generally are not classified as impaired. A loan is not impaired during a period of delay in payment if the Company expects to collect all amounts due including interest accrued at the contractual interest rate for the period of delay. All loans identified as impaired are evaluated independently by management. The Company estimates credit losses on impaired loans based on the present value of expected cash flows or the fair value of the underlying collateral if the loan repayment is expected to come from the sale or operation of such collateral. Impaired loans, or portions thereof, are charged off when it is determined a realized loss has occurred. Until such time, an allowance for loan losses is maintained for estimated losses. Cash receipts on impaired loans are applied first to accrued interest receivable unless otherwise required by the loan terms, except when an impaired loan is also a nonaccrual loan in which case the portion of the payment related to interest is recognized as income.

Premises and Equipment

Premises and equipment are stated at cost net of accumulated depreciation. Depreciation is computed on the straight-line method over the estimated useful lives of the assets. Expenditures for maintenance and repairs are charged against income as incurred. Costs of major additions and improvements are capitalized.

Income Taxes

The Company and the Bank file a consolidated federal income tax return. Deferred tax assets and liabilities are reflected at currently enacted income

Earnings Per Share

The Company provides dual presentation of basic and diluted earnings per share. Basic earnings per share is calculated utilizing net income as reported in the numerator and average shares outstanding in the denominator. The computation of diluted earnings per share differs in that the dilutive effects of any stock options, warrants, and convertible securities are adjusted in the denominator.

Stock Options

The Company maintains a stock option plan for key officers, employees, and non-employee directors. When the exercise price of the Company's stock options is greater than or equal to the market price of the underlying stock on the date of the grant, no compensation expense is recognized in the Company's financial statements. Pro forma net income and earnings per share are presented to reflect the impact of the stock option plan assuming compensation expense had been recognized based on the fair value of the stock options granted under the plan.

Stockholders' Equity

On August 14, 2000, the Board of Directors approved a two-for-one stock split. Average shares outstanding and all per share amounts included in the consolidated financial statements are based on the increased number of shares giving retroactive effect to the stock split.

Cash Flow Information

The Company has defined cash and cash equivalents as those amounts included in the consolidated balance sheet captions Cash and due from banks and Federal funds sold.

Recent Accounting Pronouncements

In July 2001, the Financial Accounting Standards Board (FASB) issued Statement of Financial Accounting Standards (FAS) No. 141, *Business Combinations*, effective for all business combinations initiated after June 30, 2001, as well as all business combinations accounted for by the purchase method that are completed after June 30, 2001. The new statement requires that the purchase method of accounting be used for all business combinations and prohibits the use of the pooling-of-interests method. The adoption of Statement No. 141 is not expected to have a material effect on the Company's financial position or results of operations.

In July 2001, the FASB issued Statement of Financial Accounting Standards No. 142, *Goodwill and Other Intangible Assets*, effective for fiscal years beginning after December 15, 2001. The statement changes the accounting for goodwill from an amortization method to an impairment-only approach. Thus, amortization of goodwill, including goodwill recorded in past business combinations, will cease upon adoption of this statement. However, the new statement did not amend FAS 72, *Accounting for Certain Acquisitions of Banking or Thrift Institutions*, which requires recognition and amortization of unidentified intangible assets relating to the acquisition of financial institutions or branches thereof. The FASB has decided to undertake a limited scope project to reconsider the provisions of FAS 72 in 2002. Therefore, the adoption of Statement No. 142 is not expected to have a material effect on the Company's financial position or results of operations.

In August 2001, the FASB issued FAS No. 143, *Accounting for Asset Retirement Obligations*, which requires that the fair value of a liability be recognized when incurred for the retirement of a long-lived asset and the value of the asset be increased by that amount. The statement also requires that the liability be maintained at its present value in subsequent periods and outlines certain disclosures for such obligations. The adoption of this statement, which is effective January 1, 2003, is not expected to have a material effect on the Company's financial statements.

In October 2001, the FASB issued FAS No. 144, *Accounting for the Impairment or Disposal of Long-Lived Assets*. FAS 144 supercedes FAS 121 and applies to all long-lived assets (including discontinued operations) and consequently amends APB Opinion No. 30, *Reporting Results of Operations – Reporting the Effects of Disposal of a Segment of a Business*. FAS 144 requires that long-lived assets that are to be disposed of by sale be measured at the lower of book value or fair value less costs to sell. FAS 144 is effective for financial statements issued for fiscal years beginning after December 15, 2001 and, generally, its provisions are to be applied prospectively. The adoption of this statement is not expected to have a material effect on the Company's financial statements.

Reclassification of Comparative Amounts

Certain items previously reported have been reclassified to conform with the current year's format. Such reclassifications did not affect net income or stockholders'



2. EARNINGS PER SHARE

There are no convertible securities which would affect the numerator in calculating basic and diluted earnings per share; therefore, net income as presented on the Consolidated Statement of Income will be used as the numerator. The following table sets forth the composition of the weighted-average common shares (denominator) used in the basic and diluted earnings per share computation.

	2001	2000	1999
Weighted-average common shares outstanding	1,148,676	1,148,676	1,148,676
Average treasury stock shares	(45,722)	(42,704)	(3,426)
Weighted-average common shares and common stock equivalents used to calculate basic earnings per share	1,102,954	1,105,972	1,145,250
Additional common stock equivalents (stock options) used to calculate diluted earnings per share	1,146	-	-
Weighted-average common shares and common stock equivalents used to calculate diluted earnings per share	1,104,100	1,105,972	1,145,250

Options to purchase 9,500 shares of common stock at prices from \$31.00 to \$31.75 per share were outstanding during 2001 but were not included in the computation of diluted EPS because to do so would have been anti-dilutive.

3. INVESTMENT SECURITIES AVAILABLE FOR SALE

The amortized cost and estimated market values of securities available for sale are as follows:

Estimated Market Value	2001		
	Gross Amortized Cost	Gross Unrealized Gains	Unrealized Losses
U.S. Government agency securities	\$ 2,152,877	\$ 60,470	\$ -
Obligations of states and political subdivisions:			
Taxable	1,411,166	16,700	(2,957)
Tax-exempt			5,822,240
1,424,909			
107,864 (15,099)	5,915,005		550,472
25,809 - 576,281			
(59,593) 11,050,244			
Total	\$ 20,977,184	\$ 280,251	\$ (77,649)

3. INVESTMENT SECURITIES AVAILABLE FOR SALE (continued)

Estimated Market Value	2000			
		Gross Amortized Cost	Gross Unrealized Gains	Unrealized Losses
U.S. Government agency securities	\$ 3,990,419	\$ 70,843	\$ (1,419)	\$ 4,059,843
Obligations of states and political subdivisions:				
Taxable	1,458,400	11,744	(2,645)	
1,467,499			Tax-exempt	3,685,472
42,258 (16,746)	3,710,984	Corporate securities	701,306	3,400
(2,800) 701,906	Mortgage-backed securities	1,898,177	29,928	-
1,928,105				
Total	\$ 11,733,774	\$ 158,173	\$ (23,610)	
\$ 11,868,337				

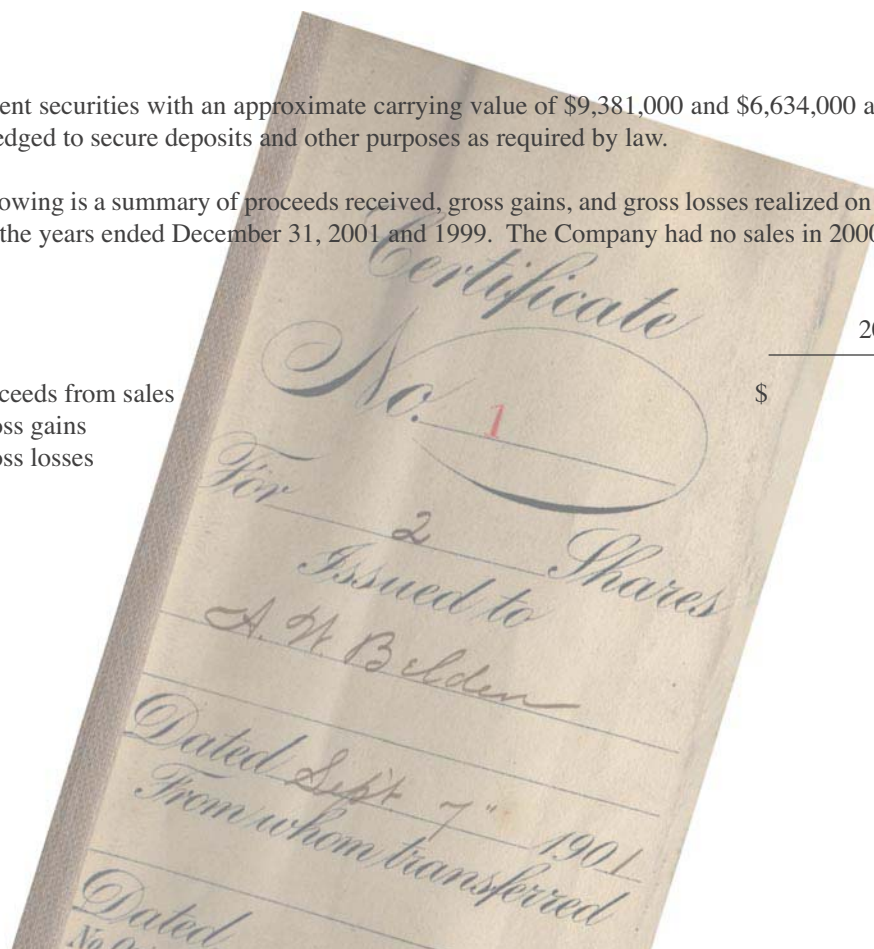
The amortized cost and estimated market value of debt securities at December 31, 2001, by contractual maturity, are shown below. Expected maturities will differ from contractual maturities because borrowers may have the right to call or prepay obligations with or without call or prepayment penalties.

	Amortized Cost	Estimated Market Value
Due in one year or less	\$ 3,002,083	\$ 3,016,125
Due after one year through five years	5,601,912	5,754,035
Due after five years through ten years	1,460,622	1,503,912
Due after ten years	10,912,567	10,905,714
Total	\$ 20,977,184	\$ 21,179,786

Investment securities with an approximate carrying value of \$9,381,000 and \$6,634,000 at December 31, 2001 and 2000, respectively, were pledged to secure deposits and other purposes as required by law.

The following is a summary of proceeds received, gross gains, and gross losses realized on the sale of investment securities available for sale for the years ended December 31, 2001 and 1999. The Company had no sales in 2000.

	2001	1999
Proceeds from sales	\$ 2,092,980	\$ 149,885
Gross gains	97,807	-
Gross losses	-	116



4. INVESTMENT SECURITIES HELD TO MATURITY

The amortized cost and estimated market values of investment securities held to maturity are as follows:

	2001			
	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Estimated Market Value
Obligations of states and political subdivisions:				
Taxable	\$ 2,255,342	\$ 57,931	\$ -	\$ 2,313,273
Tax-exempt	5,561,426	120,456	-	5,681,882
Corporate securities	2,213,060	59,896	-	2,272,956
Mortgage-backed securities	199,240	4,627	-	203,867
Total	\$ 10,229,068	\$ 242,910	\$ -	\$ 10,471,978

	2000			
	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Estimated Market Value
U.S. Government agency securities	\$ 1,899,752	\$ -	\$ (8,565)	\$ 1,891,187
Obligations of states and political subdivisions:				
Taxable	3,723,251	18,354	(19,685)	3,721,920
Tax-exempt	7,480,801	26,182	(7,420)	7,499,563
Corporate securities	4,525,466	7,829	(18,683)	4,514,612
Mortgage-backed securities	313,040	1,933	-	314,973
Total	\$ 17,942,310	\$ 54,298	\$ (54,353)	\$ 17,942,255

The amortized cost and estimated market value of debt securities at December 31, 2001, 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 Market Value
Due in one year or less	\$ 3,759,548	\$ 3,808,002
Due after one year through five years	6,119,000	6,296,593
Due after five years through ten years	51,278	53,548
Due after ten years	299,242	313,835
Total	\$ 10,229,068	\$ 10,471,978

Investment securities held to maturity with carrying values of approximately \$3,205,000 and \$7,742,000 and estimated market values of approximately \$3,424,000 and \$7,743,000 at December 31, 2001 and 2000, respectively, were pledged to secure public deposits and other purposes required by law.

The following is a summary of proceeds received, gross gains, and gross losses realized on the sale of investment securities held to maturity for the year ended December 31, 1999. These sales occurred within 90 days of maturity of the security. The Company had no sales in 2001 or 2000.

	1999
Proceeds from sales	\$ 1,054,648
Gross gains	-
Gross losses	490

5. LOANS

Major classifications of loans are summarized as follows:

	2001	2000
Commercial and industrial	\$ 28,313,488	\$ 21,508,391
Real estate - construction	3,199,738	2,568,095
Real estate - mortgage:		
Residential	113,048,775	101,403,937
Commercial	3,387,969	4,809,088
Consumer installment	4,878,385	5,014,704
	<u>152,828,355</u>	<u>135,304,215</u>
Less allowance for loan losses	2,062,252	2,037,322
Net loans	<u>\$ 150,766,103</u>	<u>\$ 133,266,893</u>

The Company's primary business activity is with customers located within its local trade area, eastern Geauga County, and contiguous counties to the north, east, and south. Commercial, residential, consumer, and agricultural loans are granted. Although the Company has a diversified loan portfolio at December 31, 2001 and 2000, loans outstanding to individuals and businesses are dependent upon the local economic conditions in its immediate trade area.

6. ALLOWANCE FOR LOAN LOSSES

Changes in the allowance for loan losses for the years ended December 31, are as follows:

	2001	2000	1999
Balance, January 1	\$ 2,037,322	\$ 1,756,137	\$ 1,538,726
Add:			
Provisions charged to operations	170,000	275,000	296,000
Recoveries	120,814	61,002	39,822
Less loans charged off	265,884	54,817	118,411
Balance, December 31	<u>\$ 2,062,252</u>	<u>\$ 2,037,322</u>	<u>\$ 1,756,137</u>

7. PREMISES AND EQUIPMENT

Major classifications of premises and equipment are summarized as follows:

	2001	2000
Land and land improvements	\$ 1,104,646	\$ 1,094,685
Building and leasehold improvements	6,018,245	5,203,258
Furniture, fixtures, and equipment	2,349,709	1,977,013
Construction in-progress	-	84,788
	<u>9,472,600</u>	<u>8,359,744</u>
Less accumulated depreciation	3,227,803	2,927,272
Total	<u>\$ 6,244,797</u>	<u>\$ 5,432,472</u>

Construction in-progress at December 31, 2000 represents the costs incurred to date for a new branch office of the Bank that was completed in 2001. Depreciation charged to operations was \$300,531 in 2001, \$337,158 in 2000, and \$287,641 in 1999.

8. OTHER ASSETS

The components of other assets are as follows:

	2001	2000
FHLB stock	\$ 1,056,000	\$ 912,900
Accrued interest on investment securities	329,312	397,582
Accrued interest on loans	423,752	495,629
Deferred tax asset, net	190,848	268,385
Other	304,656	79,989
Total	<u>\$ 2,304,568</u>	<u>\$ 2,154,485</u>

9. DEPOSITS

Time deposits include certificates of deposit in denominations of \$100,000 or more. Such deposits aggregated \$15,866,131 and \$11,529,786 at December 31, 2001 and 2000, respectively.

Maturities on time deposits of \$100,000 or more at December 31, 2001, are as follows:

Within three months	\$ 3,336,786
Beyond three but within six months	1,828,665
Beyond six but within twelve months	2,803,985
Beyond one year	7,896,695
Total	<u>\$ 15,866,131</u>

10. SHORT-TERM BORROWINGS

The outstanding balances and related information of short-term borrowings which includes securities sold under agreements to repurchase and federal funds purchased are summarized as follows:

	2001	2000
Balance at year-end	\$ 660,678	\$ 543,222
Average balance outstanding	637,106	1,059,042
Maximum month-end balance	833,008	3,581,491
Weighted-average rate at year-end	0.79%	5.43%
Weighted-average rate during the year	2.42%	6.05%

Average balances outstanding during the year represent daily average balances, and average interest rates represent interest expense divided by the related average balance.

The Company maintains a \$4,000,000 line of credit at an adjustable rate, currently 4.25 percent, from The State Bank and Trust Company. At December 31, 2001 and 2000, there were no outstanding balances on this line.

11. OTHER BORROWINGS

Other borrowings consist of fixed rate advances from the FHLB as follows:

<i>Maturity</i>	<i>Interest Rate</i>	2001	2000
July 1, 2007	6.40%	\$ 1,301,334	\$ 1,861,596
September 4, 2008	5.36%	4,000,000	4,000,000
October 2, 2008	4.53%	2,000,000	2,000,000
July 28, 2010	6.45%	2,000,000	2,000,000
Total		<u>\$ 9,301,334</u>	<u>\$ 9,861,596</u>

Advances from FHLB maturing July 1, 2007 require monthly principal and interest payments and a 20 percent payoff of outstanding principal every July 1. Monthly principal and interest payments are adjusted after each 20 percent payoff. Under terms of a blanket agreement, collateral for the FHLB borrowings are secured by certain qualifying assets of the Bank which consist principally of first mortgage loans.

12. OTHER LIABILITIES

The components of other liabilities are as follows:

	2001	2000
Accrued interest on deposits	\$ 607,204	\$ 568,277
Other	119,213	106,310
Total	<u>\$ 726,417</u>	<u>\$ 674,587</u>

13. INCOME TAXES

The provision for federal income taxes consists of:

	2001	2000	1999
Current payable	\$ 916,456	\$ 1,010,182	\$ 794,057
Deferred	54,403	(87,521)	(58,739)
Total provision	<u>\$ 970,859</u>	<u>\$ 922,661</u>	<u>\$ 735,318</u>

The tax effects of deductible and taxable temporary differences that give rise to significant portions of the deferred tax assets and deferred tax liabilities are as follows:

	2001	2000
Deferred tax assets:		
Allowance for loan losses	\$ 632,233	\$ 621,654
Gross deferred tax assets	<u>632,233</u>	<u>621,654</u>

Deferred tax liabilities:

Deferred origination fees, net	164,450	141,232
Premises and equipment	119,082	96,982
Net unrealized gain on securities	68,885	3 45,751
Other	88,968	69,304
Gross deferred tax liabilities	<u>441,385</u>	<u>353,269</u>
Net deferred tax assets	<u>\$ 190,848</u>	<u>\$ 268,385</u>

No valuation allowance was established at December 31, 2001 and 2000 in view of the Company's ability to carryback to taxes paid in previous years and certain tax strategies, coupled with the anticipated future taxable income as evidenced by the Company's earnings potential.

The reconciliation between the federal statutory rate and the Company's effective consolidated income tax rate is as follows:

	2001		2000		1999	
	Amount	% of Pre-tax Income	Amount	% of Pre-tax Income	Amount	% of Pre-tax Income
Provision at statutory rate	\$ 1,102,098	34.0%	\$ 1,074,173	34.0%	\$ 902,471	34.0%
Tax-free income	(157,362)	(4.9)	(178,520)	(5.7)	(200,165)	(7.5)
Nondeductible interest expense	26,068	0.8	19,966	0.6	24,813	0.9
Other	55	0.1	7,042	0.3	8,199	0.3
Actual tax expense and effective rate	<u>\$ 970,859</u>	<u>30.0%</u>	<u>\$ 922,661</u>	<u>29.2%</u>	<u>\$ 735,318</u>	<u>27.7%</u>

14. EMPLOYEE BENEFITS

Retirement Plan

The Bank maintains a section 401(k) employee savings and investment plan for all full-time employees and officers of the Bank with more than one year of service. The Bank's contribution to the plan is based on 50 percent matching of voluntary contributions up to 6 percent of compensation. An eligible employee can contribute up to 15 percent of salary. Employee contributions are vested at all times, and the Bank contributions are fully vested after 6 years beginning at the second year in 20 percent increments. Contributions for 2001, 2000, and 1999 to this plan amounted to \$49,130, \$44,411, and \$42,149, respectively.

Supplemental Retirement Plan

Effective December 1, 2001, the Directors Retirement Plan was adopted to provide post-retirement payments over a ten-year period to members of the Board of Directors who have completed five or more years of service. The Plan requires payment of 25 percent of the final average annual board fees paid to a director in the three years preceding the director's retirement. The expense of the plan for the year ended December 31, 2001 amounted to \$4,107.

Stock Option Plan

At the annual meeting in May 1999, the Board of Directors approved and stockholders ratified the formation of the 1999 Stock Option Plan (the "Plan"). The Plan provides for granting incentive stock options and non-qualified stock options for key officers and employees and non-employee directors of the Company. A total of 114,866 shares of authorized and unissued or issued common stock are reserved for issuance under the Plan, which expires ten years from the date of stockholder ratification. The per share exercise price of an option granted will not be less than the fair value of a share of common stock on the date the option is granted. No option shall become exercisable earlier than one year from the date the Plan was approved by the stockholders.

The following table presents share data related to the outstanding options:

	2001	Weighted- average Exercise Price	2000	Weighted- average Exercise Price
Outstanding, January 1	20,980	\$ 27.42	9,900	\$ 31.53
Granted	-	-	11,480	24.00
Exercised	-	-	-	-
Forfeited	-	-	(400)	31.00
Outstanding, December 31	20,980	\$ 27.42	20,980	\$ 27.42
Exercisable at year-end	20,980	27.42	9,500	31.55

The following table summarizes the characteristics of stock options at December 31, 2001:

Grant Date	Exercise Price	Outstanding Contractual Shares	Average Life	Exercisable		
				Exercise Price	Average Shares	Exercise Price
June 14, 1999	\$ 31.75	7,000	7.45	\$ 31.75	7,000	\$ 31.75
November 23, 1999	31.00	2,500	7.89	31.00	2,500	31.00
December 11, 2000	24.00	11,480	8.95	24.00	11,480	24.00
		20,980		27.42	20,980	27.42

The Company accounts for the Plan under provisions of APB Opinion No. 25, "Accounting for Stock Issued to Employees," and related interpretations. Under this Opinion, no compensation expense has been recognized with respect to the Plan because the exercise price of the Company's employee stock options equals the market price of the underlying stock on the grant date.

For purposes of computing pro forma results, the Company estimated the fair values of stock options using the Black-Scholes option pricing model. The model requires the use of subjective assumptions which can materially affect fair value estimates. Therefore, the pro forma results are estimates of results of operations as if compensation expense had been recognized for the stock option plans.

14. EMPLOYEE BENEFITS (continued)

Stock Option Plan (Continued)

The fair value of each stock option granted was estimated using the following weighted-average assumptions for grants in 2000 and 1999: (1) expected dividend yield was 2.50 percent and 2.00 percent, respectively; (2) risk-free interest rate of 5.29 percent and 5.34 percent, respectively; (3) expected volatility of 5.00 percent; and (4) expected lives of options of ten years.

	2001	2000
Net income applicable to common stock:		
As reported	\$ 2,270,607	\$ 2,236,671
Pro forma	2,232,963	2,195,370
Basic net income per common share:		
As reported	\$ 2.06	\$ 2.02
Pro forma	2.02	1.97
Diluted net income per common share:		
As reported	\$ 2.06	\$ 2.02
Pro forma	2.02	1.97

15. COMMITMENTS

In the normal course of business, there are various outstanding commitments and certain contingent liabilities which are not reflected in the accompanying consolidated financial statements. These commitments and contingent liabilities represent financial instruments with off-balance sheet risk. The contract or notional amounts of those instruments reflect the extent of involvement in particular types of financial instruments which were comprised of the following:

	2001	2000
Commitments to extend credit	\$ 17,265,756	\$ 10,103,358
Standby letters of credit	72,692	100,692
Total	<u>\$ 17,338,448</u>	<u>\$ 10,204,050</u>

The instruments involve, to varying degrees, elements of credit and interest rate risk in excess of the amount recognized in the balance sheet. The same credit policies are used in making commitments and conditional obligations as for on-balance sheet instruments. Generally, collateral is not required to support financial instruments with credit risk. The terms are typically for a one-year period with an annual renewal option subject to prior approval by management.

Commitments to extend credit are agreements to lend to a customer as long as there is no violation of any condition established in the loan agreement. These commitments are comprised primarily of available commercial and personal lines of credit. Standby letters of credit are conditional commitments issued to guarantee the performance of a customer to a third party.

The exposure to loss under these commitments is limited by subjecting them to credit approval and monitoring procedures. Substantially all commitments to extend credit are contingent upon customers maintaining specific credit standards at the time of the loan funding. Management assesses the credit risk associated with certain commitments to extend credit in determining the level of the allowance for loan losses. Since many of the commitments are expected to expire without being drawn upon, the contractual amounts do not necessarily represent future funding requirements.



16. REGULATORY RESTRICTIONS

Loans

Federal law prevents the Company from borrowing from the Bank unless the loans are secured by specific obligations. Further, such secured loans are limited in amount of ten percent of the Bank's common stock and capital surplus.

Dividends

The Bank is subject to a dividend restriction which generally limits the amount of dividends that can be paid by an Ohio state-chartered bank. Under the Ohio Banking Code, cash dividends may not exceed net profits as defined for that year combined with retained net profits for the two preceding years less any required transfers to surplus. Under this formula, the amount available for payment of dividends in 2002 is \$2,477,000 plus 2002 profits retained up to the date of the dividend declaration.

17. REGULATORY CAPITAL

Federal regulations require the Company and the Bank to maintain minimum amounts of capital. Specifically, each is required to maintain certain minimum dollar amounts and ratios of Total and Tier I capital to risk-weighted assets and of Tier I capital to average total assets.

In addition to the capital requirements, the Federal Deposit Insurance Corporation Improvement Act ("FDICIA") established five capital categories ranging from "well capitalized" to "critically undercapitalized." Should any institution fail to meet the requirements to be considered "adequately capitalized," it would become subject to a series of increasingly restrictive regulatory actions.

As of December 31, 2001 and 2000, the FDIC categorized the Bank as well capitalized under the regulatory framework for prompt corrective action. To be classified as a well capitalized financial institution, Total risk-based, Tier 1 risk-based, and Tier 1 Leverage capital ratios must be at least ten percent, six percent, and five percent, respectively.

The Company's actual capital ratios are presented in the following table which shows the Company met all regulatory capital requirements. The capital position of the Bank does not differ significantly from the Company's.

	2001		2000	
	Amount	Ratio	Amount	Ratio
<u>Total Capital</u>				
<u>(to Risk-weighted Assets)</u>				
Actual	\$ 21,147,628	17.82%	\$ 19,534,601	17.75%
For Capital Adequacy Purposes	9,493,703	8.00	8,802,236	8.00
To Be Well Capitalized	11,867,129	10.00	11,002,795	10.00
<u>Tier I Capital</u>				
<u>(to Risk-weighted Assets)</u>				
Actual	\$ 19,657,090	16.56 %	\$ 18,154,551	
16.50% For Capital Adequacy Purposes	4,746,851	4.00	4,401,118	4.00
To Be Well Capitalized	7,120,277	6.00	6,601,677	6.00
<u>Tier I Capital</u>				
<u>(to Average Assets)</u>				

18. FAIR VALUE DISCLOSURE OF FINANCIAL INSTRUMENTS

The estimated fair value of the Company's financial instruments at December 31, are as follows:

	2001		2000	
	Carrying Value	Fair Value	Carrying Value	Fair Value
Financial assets:				
Cash and due from banks	\$3,443,435	\$3,443,435	\$3,574,875	\$3,574,875
Federal funds sold	2,450,000	2,450,000	1,265,000	1,265,000
Interest-bearing deposits in other institutions	1,240,207	1,240,207	984,441	984,441
Investment securities:				
Available for sale	21,179,786	21,179,786	11,868,337	11,868,337
Held to maturity	10,229,068	10,471,978	17,942,310	17,942,255
Net loans	150,766,103	157,569,103	133,266,893	135,415,893
Regulatory stock	1,056,000	1,056,000	912,900	912,900
Accrued interest receivable	753,064	753,064	893,211	893,211
Total	\$191,117,663	\$198,163,573	\$170,707,967	\$172,856,912
Financial liabilities:				
Deposits	\$167,382,728	\$170,258,728	\$ 147,166,046	\$147,424,151
Short-term borrowings	660,678	660,678	543,222	543,222
Other borrowings	9,301,334	9,679,000	9,861,596	9,907,000
Accrued interest payable	607,204	607,204	568,277	568,277
Total	\$177,951,944	\$181,205,610	\$158,139,141	\$158,442,650

Financial instruments are defined as cash, evidence of ownership interest in an entity, or a contract which creates an obligation or right to receive or deliver cash or another financial instrument from/to a second entity on potentially favorable or unfavorable terms.

Fair value is defined as the amount at which a financial instrument could be exchanged in a current transaction between willing parties other than in a forced liquidation sale. If a quoted market price is available for a financial instrument, the estimated fair value would be calculated based upon the market price per trading unit of the instrument.

If no readily available market exists, the fair value estimates for financial instruments should be based upon management's judgment regarding current economic conditions, interest rate risk, expected cash flows, future estimated losses, and other factors as determined through various option pricing formulas or simulation modeling. As many of these assumptions result from judgments made by management based upon estimates which are inherently uncertain, the resulting estimated fair values may not be indicative of the amount realizable in the sale of a particular financial instrument. In addition, changes in assumptions on which the estimated fair values are based may have a significant impact on the resulting estimated fair values.

As certain assets such as deferred tax assets and premises and equipment are not considered financial instruments, the estimated fair value of financial instruments would not represent the full value of the Company.

The Company employed simulation modeling in determining the estimated fair value of financial instruments for which quoted market prices were not available based upon the following assumptions:

Cash and Due from Banks, Interest-bearing Deposits in Other Institutions, Federal Funds Sold, Regulatory Stock, Accrued Interest Receivable, Accrued Interest Payable, and Short-term Borrowings

The fair value is equal to the current carrying value.

Investment Securities

The fair value of investment securities available for sale and held to maturity is equal to the available quoted market price. If no quoted market price is available, fair value is estimated using the quoted market price for similar securities.

Loans, Deposits, and Other Borrowings

The fair value of loans, certificates of deposit, and other borrowings is estimated by discounting the future cash flows using a simulation model which estimates future cash flows and constructs discount rates that consider reinvestment opportunities, operating expenses, noninterest income, credit quality, and prepayment risk. Demand, savings, and money market deposit accounts are valued at the amount payable on demand as of year-end.

Commitments to Extend Credit

These financial instruments are generally not subject to sale, and estimated fair values are not readily available. The carrying value, represented by the net deferred fee arising from the unrecognized commitment or letter of credit, and the fair value, determined by discounting the remaining contractual fee over the term of the commitment using fees currently charged to enter into similar agreements with similar credit risk, are not considered material for disclosure. The contractual amounts of unfunded commitments and letters of credit are presented in Note 15.

19. PARENT COMPANY

Following are condensed financial statements for the Company.

CONDENSED BALANCE SHEET

	December 31,	
	2001	2000
ASSETS		
Cash and due from banks	\$ 167,074	\$ 502,849
Interest-bearing deposits in other institutions	377,207	26,441
Investment in subsidiary bank	19,242,526	17,681,862
Other assets	-	32,210
TOTAL ASSETS	<u>\$ 19,786,807</u>	<u>\$ 18,243,362</u>
STOCKHOLDERS' EQUITY	<u>\$ 19,786,807</u>	<u>\$ 18,243,362</u>

CONDENSED STATEMENT OF INCOME

	Year Ended December 31,		
	2001	2000	1999
INCOME			
Dividends from subsidiary bank	\$ 854,703	\$ 1,335,994	\$ 765,617
Interest income	4,709	25,600	49,823
Total income	859,412	1,361,594	815,440
EXPENSES	<u>152,626</u>	<u>120,243</u>	<u>55,704</u>
Income before income tax benefit	706,786	1,241,351	759,736
Income tax benefit	(48,063)	(34,178)	-
Income before equity in undistributed net income of subsidiary	754,849	1,275,529	759,736
Equity in undistributed net income of subsidiary	<u>1,515,758</u>	<u>961,142</u>	<u>1,159,273</u>

19. PARENT COMPANY (Continued)

CONDENSED STATEMENT OF CASH FLOWS

	Year Ended December 31,		
	2001	2000	1999
OPERATING ACTIVITIES			
Net income	\$ 2,270,607	\$ 2,236,671	\$ 1,919,009
Adjustments to reconcile net income to net cash provided by operating activities:			
Equity in undistributed net income of subsidiary	(1,515,758)	(961,142)	(1,159,273)
Other	32,210	(32,176)	(898)
Net cash provided by operating activities	787,059	1,243,353	758,838
INVESTING ACTIVITIES			
Decrease (increase) in interest-bearing deposits in other institutions	(350,766)	1,002,177	(389,814)
Investment securities available for sale:			
Proceeds from repayments and maturities	-	-	1,500,000
Purchases	-	-	(1,500,000)
Investment securities held to maturity:			
Proceeds from repayments and maturities	-	-	500,000
Net cash provided by (used for) investing activities	(350,766)	1,002,177	110,186
FINANCING ACTIVITIES			
Purchase of treasury stock	-	(1,311,050)	(306,175)
Sale of treasury stock	-	44,499	96,286
Cash dividends	(772,068)	(595,255)	(572,343)
Net cash used for financing activities	(772,068)	(1,861,806)	(782,232)
Increase (decrease) in cash	(335,775)	383,724	86,792
CASH AT BEGINNING OF YEAR	502,849	119,125	32,333
CASH AT END OF YEAR	\$ 167,074	\$502,849	\$ 119,125



20. SELECTED QUARTERLY FINANCIAL DATA (unaudited)

	Three Months Ended			
	March 31, 2001	June 30, 2001	September 30, 2001	December 31, 2001
Total interest income	\$ 3,299,426	\$ 3,462,634	\$ 3,508,111	\$ 3,534,205
Total interest expense	<u>1,655,626</u>	<u>1,725,151</u>	<u>1,730,710</u>	<u>1,636,435</u>
Net interest income	1,643,800	1,737,483	1,777,401	1,897,770
Provision for loan losses	39,000	41,000	45,000	45,000
Net interest income after provision for loan losses	<u>1,604,800</u>	<u>1,696,483</u>	<u>1,732,401</u>	<u>1,852,770</u>
Total noninterest income	258,665	267,775	365,793	204,153
Total noninterest expense	<u>1,090,308</u>	<u>1,237,226</u>	<u>1,149,978</u>	<u>1,263,862</u>
Income before income taxes	773,157	727,032	948,216	793,061
Income taxes	235,900	235,600	288,326	211,033
Net income	<u>\$ 537,257</u>	<u>\$ 491,432</u>	<u>\$ 659,890</u>	<u>\$ 582,028</u>
Per share data:				
Net income				
Basic	\$ 0.49	\$ 0.45	\$ 0.60	\$ 0.53
Diluted	0.49	0.44	0.60	0.53
Average shares outstanding				
Basic	1,102,954	1,102,954	1,102,954	1,102,954
Diluted	1,104,304	1,104,694	1,103,475	1,103,395

	Three Months Ended				2000
	March 31, 2000	June 30, 2000	September 30, 2000	December 31, 2000	
Total interest income	\$ 3,050,487	\$ 3,141,341	\$ 3,268,702	\$ 3,309,640	
Total interest expense	<u>1,357,310</u>	<u>1,409,416</u>	<u>1,542,773</u>	<u>1,600,385</u>	
Net interest income	1,693,177	1,731,925	1,725,929	1,709,255	
Provision for loan losses	<u>75,000</u>	<u>75,000</u>	<u>75,000</u>	<u>50,000</u>	
Net interest income after provision for loan losses	<u>1,618,177</u>	<u>1,656,925</u>	<u>1,650,929</u>	<u>1,659,255</u>	
Total noninterest income	219,897	224,333	247,238	291,195	
Total noninterest expense	<u>1,045,414</u>	<u>1,097,167</u>	<u>1,072,384</u>	<u>1,193,652</u>	
Income before income taxes	792,660	784,091	825,783	756,798	
Income taxes	<u>235,370</u>	<u>232,000</u>	<u>254,000</u>	<u>201,291</u>	
Net income	<u>\$ 557,290</u>	<u>\$ 552,091</u>	<u>\$ 571,783</u>	<u>\$ 555,507</u>	
Per share data:					
Net income					
Basic	\$ 0.50	\$ 0.50	\$ 0.52	\$ 0.50	
Diluted	0.50	0.50	0.52	0.50	
Average shares outstanding					
Basic	1,117,069	1,101,675	1,101,554	1,101,663	
Diluted	1,117,069	1,101,675	1,101,554	1,101,663	

SNODGRASS

Certified Public Accountants and Consultants



REPORT OF INDEPENDENT AUDITORS

Board of Directors and Stockholders
Middlefield Banc Corp.

We have audited the accompanying consolidated balance sheet of Middlefield Banc Corp. and subsidiary as of December 31, 2001 and 2000, and the related consolidated statements of income, changes in stockholders' equity, and cash flows for each of the three years in the period ended December 31, 2001. 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 Middlefield Banc Corp. and subsidiary as of December 31, 2001 and 2000, and the results of their operations and their cash flows for each of the three years in the period ending December 31, 2001, in conformity with accounting principles generally accepted in the United States of America.

S. R. Snodgrass, A.C.

February 22, 2002

S.R. Snodgrass, A.C.
1000 Stonewood Drive, Suite 200 Wexford, PA 15090-8399 Phone: 724-934-0344 Facsimile: 724-934-0345

Selected Financial Data

The summary financial information to follow is not a substitute for Middlefield's historical financial information and other detailed financial information we provide elsewhere in this document. You should read the summary financial information together with the historical financial information and other detailed financial information we provide elsewhere in this document. We derived the financial data from Middlefield's audited financial statements for the fiscal years ended December 31, 1997 through 2001.

	As of or For the Years Ended December 31,				
	2001	2000	1999	1998	1997
(In thousands, except share and per share amounts and ratios)					
Income Statement Data:					
Interest income	\$ 13,707	\$ 12,770	\$ 11,449	\$ 10,901	\$ 10,600
Interest expense	6,748	5,910	5,048	5,085	5,084
Net interest income	6,959	6,860	6,401	5,816	5,516
Provision for loan losses	170	275	296	270	200
Net interest income after provision for loan losses	6,789	6,585	6,105	5,546	5,316
Noninterest income, including securities gains (losses)	1,194	983	804	599	546
Noninterest expense	4,741	4,409	4,254	3,825	3,493
Income before income taxes	3,242	3,159	2,655	2,320	2,369
Income taxes	971	922	735	630	624
Net income	\$ 2,271	\$ 2,237	\$ 1,920	\$ 1,690	\$ 1,745
Balance Sheet Data:					
Investment securities	\$ 31,409	\$ 29,811	\$ 31,818	\$ 36,656	\$ 38,460
Loans, net	\$ 150,766	\$ 133,267	\$ 119,472	\$ 102,728	\$ 88,320
Total deposits	\$ 167,383	\$ 147,166	\$ 135,094	\$ 128,828	\$ 121,482
FHLB Cincinnati advances	\$ 9,301	\$ 9,862	\$ 9,602	\$ 9,576	\$ 4,849
Total stockholders' equity	\$ 19,791	\$ 18,243	\$ 17,689	\$ 16,657	\$ 15,465
Total assets	\$ 197,862	\$ 176,489	\$ 165,512	\$ 155,558	\$ 142,276
Per Common Share Data: ⁽¹⁾					
Basic net income	\$ 2.06	\$ 2.02	\$ 1.68	\$ 1.47	\$ 1.52
Diluted net income	\$ 2.06	\$ 2.02	\$ 1.68	N/A	N/A
Book value	\$ 17.94	\$ 16.54	\$ 15.49	\$ 14.50	\$ 13.46
Weighted Average Number of Shares:					
Basic	1,102,954	1,105,972	1,145,250	1,148,676	1,148,676
Diluted	1,104,100	1,105,972	1,145,250	N/A	N/A
Selected Ratios:					
Return on average total stockholders' equity	11.89 %	12.83 %	11.17 %	10.43 %	11.79 %
Return on average total assets	1.22 %	1.31 %	1.21 %	1.15 %	1.26 %
Dividend payout ratio	33.94 %	26.61 %	29.82 %	29.53 %	24.98 %
Efficiency ratio ⁽²⁾	58.16 %	56.21 %	59.05 %	59.62 %	57.62 %
Asset Quality Ratios:					
Reserve for loan losses to ending total loans	1.35 %	1.51 %	1.45 %	1.48 %	1.49 %
Net loan charge-offs to average loans	0.10 %	— %	0.07 %	0.07 %	— %
Capital Ratios:					
Average stockholders' equity to average assets	10.24 %	10.20 %	10.83 %	11.04 %	10.72 %
Leverage ratio ⁽³⁾	9.94 %	10.32 %	10.93 %	11.35 %	10.80 %
Total risk-based capital ratio ⁽³⁾	17.82 %	17.75 %	18.39 %	18.37 %	18.54 %

(1) Per share amounts are adjusted for a 10% stock dividend paid in 1998 and 1997 and a 2-for-1 stock split in 2000.

(2) Efficiency ratio is noninterest expense divided by the sum of net interest income plus noninterest income minus nonrecurring items.

(3) Computed in accordance with Federal Reserve Board and FDIC guidelines.

Overview

The consolidated review and an analysis of Middlefield Banc Corp. ("Middlefield") is intended to assist the reader in evaluating the performance of Middlefield for the years ended December 31, 2001 and 2000. This information should be read in conjunction with the consolidated financial statements and accompanying notes to the financial statements.

Middlefield is an Ohio corporation organized to become the holding company of The Middlefield Banking Company ("Bank"). The Bank is a state-chartered bank located in Middlefield, Ohio. Middlefield and its subsidiary bank derive substantially all of their income from banking and bank-related services, including interest earnings on residential real estate, commercial mortgage, commercial, and consumer financings as well as interest earnings on investment securities and deposit services to its customers through five locations.

Forward Looking Statement

The Private Securities Litigation Reform Act of 1995 contains safe harbor provisions regarding forward-looking statements. Forward-looking statements can be identified by terminology such as "believes," "expects," "anticipates," "estimates," "intends," "should," "will," "plans," "potential" and similar words. Forward-looking statements are also statements that are not statements of historical fact. Forward-looking statements necessarily involve risks and uncertainties. They are merely predictive or statements of probabilities, involving known and unknown risks, uncertainties and other factors. If one or more of these risks of uncertainties occurs or if the underlying assumptions prove incorrect, actual results in 2002 and beyond could differ materially from those expressed in or implied by the forward-looking statements.

Forward-looking statements are based upon a variety of estimates and assumptions. The estimates and assumptions involve judgments about a number of things, including future economic, competitive, and financial market conditions and future business decisions. These matters are inherently subject to significant business, economic, and competitive uncertainties, all of which are difficult to predict and many of which are beyond Middlefield's control. Although Middlefield believes its estimates and assumptions are reasonable, actual results could vary materially from those shown. Inclusion of forward-looking information does not constitute a representation by Middlefield or any other person that the indicated results will be achieved. Investors are cautioned not to place undue reliance on forward-looking information.

Results of Operations

Middlefield recorded net income of \$2.3 million in 2001, which represents an increase of \$34,000, or 1.5%, over 2000. Net income for 2000 of \$2.2 million represented an increase of \$318,000, or 16.6%, over 1999. Basic and diluted earnings per share have increased each of the past three years to \$2.06 per share for 2001, \$2.02 per share for 2000, and \$1.68 per share for 1999.

Net Interest Income — 2001 Compared to 2000. Net interest income for 2001 increased slightly to \$7.0 million, compared to \$6.9 million for 2000. Interest income of \$13.7 million in 2001 represents an increase of \$0.9 million, or 7.3%, over 2000, and 2001 was influenced primarily by an increase in interest earned on loans receivable of \$1.0 million. Correspondingly, interest expense of \$6.7 million in 2001 increased by \$0.8 million, or 14.2%, and resulted almost entirely from an increase in interest expense on deposits. The average balance of interest-earning assets increased \$16.4 million for 2001 and was comprised of increases in loans receivable, specifically real estate mortgages, of \$14.9 million, or 11.6%, to \$143.6 million, and interest-bearing deposits with other banks of \$1.8 million, or 47.3%, to \$5.6 million. Due to the declining rate environment in 2001, the tax-equivalent yield on interest-earning assets declined to 7.79% from 8.02% for 2000. While the yield on loans receivable and interest-bearing deposits with other banks was reduced by 21 and 190 basis points, respectively, the investment securities yield remained unchanged as management engaged in restructuring the investment securities portfolio to include higher yielding mortgage-backed securities with longer maturity periods. Partially offsetting increases in interest income in 2001 was an increase in the average balances of time deposits of \$13.3 million, or 19.1%, to \$83.2 million and savings deposits of \$3.4 million, or 10.6%, to \$35.4 million. The average cost of funds on interest-bearing liabilities increased to 4.71% in 2001 from 4.58% in 2000, primarily resulting from an increase of 14 basis points for the more competitively priced certificates of deposit products.

2000 Compared to 1999. Net interest income for 2000 was \$6.9 million, a 7.2% increase over 1999. Interest income of \$12.8 million in 2000 represented an increase of \$1.3 million, or 11.5%, over 1999. Interest expense of \$5.9 million in 2000 increased by \$0.9 million, or 17.1%, over 1999. Although there was an increase in general interest rate levels during these periods, interest income and expense were both primarily driven by increases in the average balances of related interest-earning assets and interest-bearing liabilities. The average balances of loans receivable, specifically real estate mortgages, increased \$16.9 million, or 15.1%, to \$128.7 million as of December 31, 2000. The tax-equivalent yield on interest earning assets increased to 8.02% for the year ended 2000 from 7.84% for the year ended 1999 and was mainly driven by a 16 basis-point increase in investment securities. Partially offsetting increases to net interest income was an increase in the average balance of certificates of deposit of \$9.5 million, coupled with a 36 basis-point increase in the cost of such funds. This increase to interest expense is attributable to marketing efforts and higher-yielding promotional products, resulting in an overall increase in the cost of funds from 4.26% to 4.58% from 1999 to 2000.

Average Balances, Interest Rates and Yields. The following table sets forth certain information relating to our average balance sheet, and it reflects the average yield on assets and average cost of liabilities for the periods indicated and the average yields earned and rates paid. Such yields are derived by dividing income or expense by the average balance of assets or liabilities, respectively, for the periods presented. Average balances are derived from daily average balances.

(Dollars in thousands)	Year ended December 31,								
	2001			2000			1999		
	Average balance	Interest ⁽¹⁾	Average yield/cost ⁽⁴⁾	Average balance	Interest ⁽¹⁾	Average yield/cost ⁽⁴⁾	Average balance	Interest	Average yield/cost ⁽⁴⁾
Interest-earning assets:									
Loans receivable	\$ 143,560	\$ 11,808	8.23%	\$ 128,661	\$ 10,852	8.43%	\$ 111,745	\$ 9,409	8.42%
Investment securities	29,887	1,625	6.24%	30,162	1,658	6.39%	33,983	1,819	6.24%
Interest-earning deposits with other banks	5,647	274	4.85%	3,833	259	6.76%	4,254	220	
5.17%									
Total interest-earning assets	179,094	13,707	7.79%	162,656	12,769	8.02%	149,982	11,448	
7.83%									
Non-interest-earning assets	7,455			8,231			8,674		
Total assets	186,549			\$ 170,887			\$ 158,656		
Interest-bearing liabilities:									
Interest-bearing demand deposits	\$ 6,296	153	2.43%	\$ 6,268	174	2.78%	\$ 5,473	139	2.54%
Money market deposits	8,123	244	3.00%	10,310	308	2.99%	15,249	454	2.98%
Savings deposits	35,432	954	2.69%	32,036	855	2.67%	28,183	726	2.58%
Certificates of deposit	83,177	4,847	5.83%	69,866	3,975	5.69%	60,390	3,220	5.33%
Borrowings	10,211	550	5.39%	10,641	598	5.62%	9,224	509	5.52%
Total interest-bearing liabilities	143,239	6,748	4.71%	129,121	5,910	4.58%	118,519	5,048	4.26%
Non interest-bearing liabilities:									
Other liabilities	24,216			24,336			22,950		
Stockholders' equity	19,094			17,430			17,187		
Total liabilities and stockholders' equity	\$ 186,549			\$ 170,887			\$ 158,656		
Net interest income		\$ 6,959			\$ 6,859			\$ 6,400	
Interest rate spread ⁽²⁾			3.08 %			3.44 %			3.58 %
Net yield on interest-earning assets ⁽³⁾			3.89 %			4.22 %			4.27 %
Ratio of average interest-earning assets to average interest-bearing liabilities			125.03 %			125.97 %			126.55 %

⁽¹⁾ Interest income and expense are for the period that banking operations were in effect.

⁽²⁾ Interest rate spread represents the difference between the average yield on interest-earning assets and the average cost of interest-bearing liabilities.

⁽³⁾ Net yield on interest-earning assets represents net interest income as a percentage of average interest-earning assets.

⁽⁴⁾ Average yields are computed using annualized interest income and expense for the periods.



Rate/Volume Analysis. The following table sets forth certain information regarding the changes in our interest income and interest expense for the periods indicated. For each category of interest-earning assets and interest-bearing liabilities, information is provided on changes attributable to (1) changes in volume (changes in average volume multiplied by prior year rate), and (2) changes in rates (changes in rate multiplied by prior year average volume). Increases and decreases due to both rate and volume have been allocated proportionally to the change due to volume and the change due to rate.

(Dollars in thousands)	Changes in net interest income for the year ended December 31,					
	2001 vs. 2000			2000 vs. 1999		
	Increase (decrease) due to			Increase (decrease) due to		
	Volume	Rate	Total	Volume	Rate	Total
Interest income:						
Loans receivable	\$ 1,217	\$ (262)	\$ 955	\$ 1,427	\$ 17	\$ 1,444
Investment securities	(9)	(24)	(33)	221	(382)	(161)
Other interest-earning assets	37	(22)	15	(19)	57	38
Total interest income	1,245	(308)	937	1,629	(308)	1,321
Interest expense:						
Interest-bearing demand	1	(22)	(21)	21	14	35
Money market	(66)	2	(64)	(148)	2	(146)
Savings 91	8	99	102	27	129	
Certificates of deposit	774	98	872	529	226	755
Other interest-bearing liabilities	(24)	(24)	(48)	79	10	89
Total interest expense	766	63	838	583	279	862
Change in net interest income	\$ 469	\$ (370)	\$ 99	\$ 1,046	\$ (587)	\$ 459

Loan Loss Provision — 2001 Compared to 2000. The provision for loan losses was \$170,000 in 2001 as compared to \$275,000 in 2000. The loan loss provision is based upon management's assessment of a variety of factors, including types and amounts of nonperforming loans, historical loss experience, collectibility of collateral values and guaranties, pending legal action for collection of loans and related guaranties, and current economic conditions. The loan loss provision reflects management's judgment of the current period cost-of-credit risk inherent in the loan portfolio. Although management believes the loan loss provision has been sufficient to maintain an adequate allowance for loan losses, actual loan losses could exceed the amounts that have been charged to operations. The change in the loan loss provision in 2001 was principally a result of a reduction in the amount of classified assets from 2000 to 2001, as well as the mix of such assets.

2000 Compared to 1999. The provision for loan losses was \$275,000 in 2000, compared to \$296,000 in 1999, a 7.1% reduction. The change in the loan loss provision in 2000 was principally a result of a reduction in the amount of new commercial and commercial real estate loans originated during 2000 as compared to 1999. Furthermore, there was an improvement in asset quality reflected by a decrease in nonperforming loans from \$131,000 at the end of 1999 to \$5,000 at the end of 2000.

Noninterest Income — 2001 Compared to 2000. Total noninterest income was \$1.2 million in 2001, an increase of 21.5% over 2000. The increase is accounted for principally by fee income from deposit accounts, which grew commensurate with deposit growth, coupled with the recognition of investment security gains of \$98,000.

2000 Compared to 1999. Total noninterest income was \$983,000 in 2000, an increase of 22.2% over 1999. The increase is also principally fee income from deposit accounts that correspond with the growth in deposit accounts during the period.

Transaction deposit accounts grew at a steady pace in 2001, 2000, and 1999. In general, management prices deposits at rates competitive with rates offered by the other banks in Middlefield's market, which rates tend to be somewhat lower than rates offered by thrift institutions and credit unions. Middlefield generally has not imposed service charges and fees to the same extent as other local institutions. Although a wider range of service charges and fees and higher service charges and fees would yield more income for each dollar of deposits, imposing service charges and fees on a basis equivalent to those imposed by many other area banks might adversely affect deposit growth. To promote deposit growth and provide cross-selling opportunities, Middlefield has not adopted the most aggressive fee structure. Deposit growth is generated by developing strong customer relationships and cross-selling deposit relationships to loan customers. Management intends to continue promoting demand deposit products, particularly noninterest-bearing deposit products, in order to obtain additional interest-free lendable funds.

Noninterest Expense — 2001 Compared to 2000. Noninterest expense increased 7.6% to \$4.7 million for 2001 as compared to \$4.4 million for 2000. Compensation and employee benefits increased \$76,000, or 3.4%, primarily as a result of normal merit raises. Data processing expenses increased \$47,000, or 14.9%, as a result of increased transaction activity with the opening of the Chardon branch. Professional fees increased \$35,000, or 16.5%, and resulted from outside assistance in complying with the increased levels of regulatory compliance of a publicly reported company. Other expenses increased \$178,000 due to the marketing of the 100th anniversary of the Bank, costs incurred with the addition of internet banking, as well as increases in other expenses such as telephones, supplies, *etc.*, that relate to increases in volume that corresponds with the sustained growth of the Bank.

2000 Compared to 1999. Noninterest expense increased 3.6% to \$4.4 million for 2000 as compared to \$4.3 million for 1999. The change in total non-interest expense from 1999 to 2000 is attributable to a 12.1% increase in other expenses, which increased steadily year-to-year primarily as a result of the overall growth of the Bank. Such expenses include additional costs relating to an increase in volume of ATM transactions, and increases in various professional fees and regulatory assessments. There were smaller increases in equipment and data processing expenses as a result of added capital expenditures in prior years from building and furnishing a new branch office in Garrettsville, additional ATMs, and increased transaction activity from operating a larger organization.

Provision for Income Taxes. The provision for income taxes fluctuated in 2001, 2000, and 1999 in direct correlation to the changing level of pre-taxable income during these periods.

Financial Condition

Assets and Liabilities. Middlefield's total assets increased \$21.4 million, or 12.1%, to \$197.9 million at December 31, 2001 from \$176.5 million at December 31, 2000. This increase primarily resulted from a \$17.5 million, or 13.1%, increase in net loans receivable to \$150.8 million at December 31, 2001 that was funded by an \$20.2 million, or 13.7%, net increase in customer deposits. The increase in net loans receivable resulted from the economic health of Middlefield's market area, the Federal Reserve Board's approach to aggressively reducing interest rates, and the strategic, service-oriented marketing approach taken by management to meet the lending needs of the area. The majority of Middlefield's lending activity consists of mortgage loans secured by one-to-four family residential property. Such loans grew \$11.6 million, or 11.5%, to \$113.0 million at December 31, 2001, representing 74.0% of the loan portfolio. Management attributes the increases in residential real estate properties to continued customer referrals and Middlefield's overall relationship with its customers. Also affected by the local economic conditions were commercial and commercial real estate loans, which increased in total by \$5.4 million to \$31.7 million.

Total investment securities increased \$1.6 million to \$31.4 million at December 31, 2001 from \$29.8 million at December 31, 2000. Management's focus on supplementing loan demand primarily by lengthening the maturities of the investment portfolio through a net increase in higher yielding, mortgage-backed securities of \$9.0 million continues, although less aggressively, and reflects the Nation's general economic trends. This has resulted in a shift in the composition of the investment securities portfolio at December 31, 2001, as mortgage-backed securities now comprise 36.0% of the total portfolio as compared to 7.5% at December 31, 2000. Furthermore, available for sale securities now comprise 67.4% of the investment securities portfolio as compared to 41.3% at December 31, 2000.

Total deposits increased \$20.2 million, or 13.7%, to \$167.4 million at December 31, 2001 from \$147.2 million at December 31, 2000. Growth was primarily concentrated in time and savings deposits, which increased \$9.9 and \$9.3 million, respectively, and resulted from continual marketing efforts by management, as well as management's competitive pricing of such products. Time deposits at December 31, 2001 accounted for approximately 51.2% of the total deposit portfolio and remain a dominant resource for funds.

Total stockholders' equity increased \$1.5 million, or 8.5%, to \$19.8 million at December 31, 2001 due to net income of \$2.3 million that was offset somewhat by dividend payments of \$0.8 million. Accumulated other comprehensive income increased as a result of changes in the net unrealized gain on investment securities available for sale due to fluctuations in interest rates. Because of interest rate volatility, accumulated other comprehensive income could materially fluctuate for each interim period and year-end period, depending on economic and interest rate conditions. In addition, future dividend policies will be determined by the board of directors, taking into account Middlefield's earnings and financial condition and applicable governmental regulations and policies.

Allowance for Loan Losses. The allowance for loan losses represents the amount management estimates is adequate to provide for probable losses inherent in the loan portfolio as of the balance sheet date. Accordingly, all loan losses are charged to the allowance, and all recoveries are credited to it. At December 31, 2001, Middlefield's allowance for loan losses increased slightly to \$2.1 million from \$2.0 million at December 31, 2000, and now represents 1.35% of the gross loan portfolio. The allowance for loan losses is established through a provision for loan losses, which is charged to operations. The provision is based on management's periodic evaluation of the adequacy of the allowance for loan losses, taking into account the overall risk characteristics of the various portfolio segments, the bank's loan loss experience, the impact of economic conditions on borrowers, and other relevant factors. The estimates used to determine the adequacy of the allowance for loan losses, including the amounts and timing of future cash flows expected on impaired loans, are particularly susceptible to significant change in the near term. The total allowance for loan losses is a combination of a specific allowance for identified problem loans, a formula allowance, and an unallocated allowance.

The specific allowance incorporates the results of measuring impaired loans as provided in Statement of Financial Accounting Standards ("FAS") No. 114, *Accounting by Creditors for Impairment of a Loan*, and FAS No. 118, *Accounting by Creditors for Impairment of a Loan — Income Recognition and Disclosures*. These accounting standards prescribe the measurement methods, income recognition and disclosures for impaired loans.

The formula allowance is calculated by applying loss factors to outstanding loans by type, excluding loans for which a specific allowance has been determined. Loss factors are based on management's determination of the amounts necessary for concentrations and changes in mix and volume of the loan portfolio, and consideration of historical loss experience.

The unallocated allowance is determined based upon management's evaluation of existing economic and business conditions affecting the key lending areas of the bank and other conditions, such as new loan products, credit quality trends, collateral values, specific industry conditions within portfolio segments that existed as of the balance sheet date, and the impact of those conditions on the collectibility of the loan portfolio. Management reviews these conditions quarterly. The unallocated allowance is subject to a higher degree of uncertainty because it considers risk factors that may not be reflected in the historical loss factors.

Although management believes that it uses the best information available to make such determinations and that the allowance for loan losses was adequate at December 31, 2001, future adjustments could be necessary if circumstances or economic conditions differ substantially from the assumptions used in making the initial determinations. A downturn in the local economy and employment could result in increased levels of nonperforming assets and charge-offs, increased loan loss provisions, and reductions in income. Additionally, as an integral part of the examination process bank regulatory agencies periodically review a bank's loan loss allowance. The banking agencies could require the recognition of additions to the loan loss allowance based on their judgment of information available to them at the time of their examination.

The following table sets forth information concerning the Middlefield's allowance for loan losses at the dates and for the periods presented.

	Loan Loss Experience for the Year Ended December 31,		
	2001	2000	1999
(Dollars in thousands)			
Loan loss allowance, beginning of period	\$ 2,037	\$ 1,756	\$ 1,539
Loans charged off:			
Commercial and industrial	(74)	3	(22)
Real estate construction	<u>0</u>	<u>0</u>	<u>0</u>
Mortgage:			
Residential	<u>(21)</u>	<u>0</u>	<u>(7)</u>
Commercial	(92)	0	0
Consumer installment	(71)	(52)	(89)
Total loans charged off	(258)	(55)	(118)
Recoveries of loans previously charged off:			
Commercial and industrial	4	2	8
Real estate construction	<u>0</u>	<u>0</u>	<u>0</u>
Mortgage:			
Residential	<u>0</u>	<u>0</u>	<u>0</u>
Commercial	87	0	0
Consumer installment	22	59	31
Total recoveries	<u>113</u>	<u>61</u>	<u>39</u>
Net loans recovered (charged off)	<u>(145)</u>	<u>6</u>	<u>(79)</u>
Provision charged to operations	170	275	296
Loan loss allowance, end of period	\$2,062	\$2,037	\$1,756
Loans outstanding:			
Average	\$ 143,560	\$ 128,611	\$ 111,745
End of period, net	\$ 152,828	\$ 135,304	\$ 121,228
Ratio of allowance for loan losses to loans outstanding at end of period	1.35%	1.51%	1.45%
Net recoveries (charge offs) to average loans	(0.10)%	0.00%	(0.07)%

The following table illustrates the allocation of the Middlefield's allowance for probable loan losses for each category of loan for each reported period. The allocation of the allowance to each category is not necessarily indicative of future loss in a particular category and does not restrict our use of the allowance to absorb losses in other loan categories.

loans (Dollars in thousands) category	Allocation of the Allowance for Loan Losses at December 31,					
	2001		2000		1999	
Type of loan:	Amount	Percent of loans in each category to total loans	Amount	Percent of loans in each category to total loans	Amount	Percent of in each to total
Commercial and industrial	\$ 722	18.53%	\$ 723	15.90%	\$ 340	15.33%
Real estate construction	37	2.09%	26	1.90%	23	1.86%

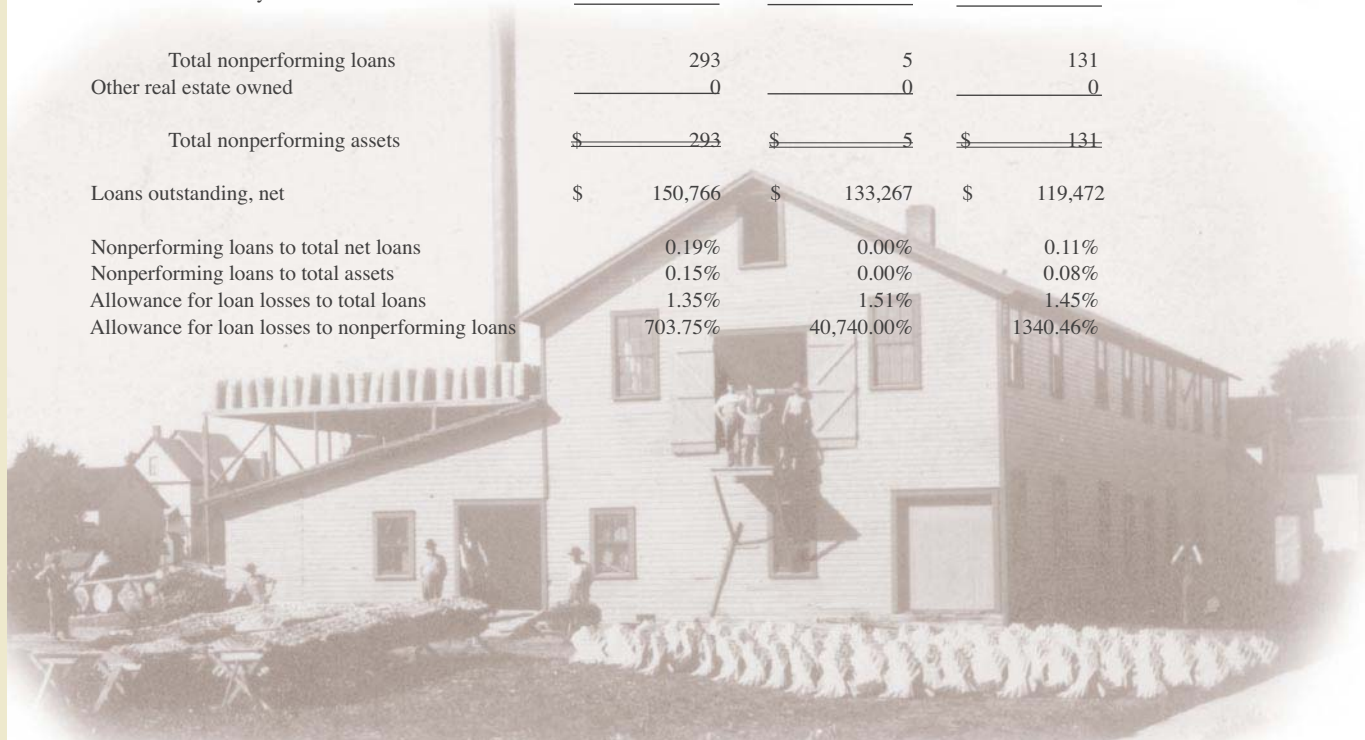
Accrual of interest is discontinued on a loan when management believes, after considering economic and business conditions, the borrower's financial condition is such that collection of interest is doubtful. Interest received on nonaccrual loans is recorded as income against principal according to management's judgment as to the collectibility of principal.

A loan is considered impaired when it is probable the borrower will not repay the loan according to the original contractual terms of the loan agreement. Management has determined that first mortgage loans on one-to-four family properties and all consumer loans represent large groups of smaller-balance homogeneous loans that are to be collectively evaluated. Loans that experience insignificant payment delays, which are defined as 90 days or less, generally are not classified as impaired. A loan is not impaired during a period of delay in payment if the bank expects to collect all amounts due, including interest accrued at the contractual interest rate for the period of delay. All loans identified as impaired are evaluated independently by management. The bank estimates credit losses on impaired loans based on the present value of expected cash flows, or the fair value of the underlying collateral if loan repayment is expected to come from the sale or operation of the collateral. Impaired loans, or portions thereof, are charged off when it is determined a realized loss has occurred. Until that time, an allowance for loan losses is maintained for estimated losses. Unless otherwise required by the loan terms, cash receipts on impaired loans are applied first to accrued interest receivable, except when an impaired loan is also a nonaccrual loan, in which case the portion of the payment related to interest is recognized as income.

Nonperforming loans as a percentage of total loans at December 31, 2001 increased to 0.19% from 2000. The bank had nonaccrual loans of \$48,000 and \$125,000 at December 31, 2001 and 1999, respectively. There were no loans on nonaccrual status at December 31, 2000. Interest income recognized on nonaccrual loans during all of the periods was insignificant. Management does not believe the nonaccrual loans or any amounts classified as nonperforming will have a significant effect on operations or liquidity in 2002. Furthermore, management is not aware of any trends or uncertainties related to any loans classified as doubtful or substandard that might have a material effect on earnings, liquidity, or capital resources. Management is not aware of any information pertaining to material credits that would cause it to doubt the ability of borrowers to comply with repayment terms.

The following table summarizes nonperforming assets by category.

(Dollars in thousands)	Nonperforming Assets at December 31,		
	2001	2000	1999
Commercial and industrial:			
Nonaccrual	\$ 48	\$ 0	\$ 17
Past due 90 days or more	9	0	0
Real estate construction:			
Nonaccrual	0	0	0
Past due 90 days or more	0	0	0
Mortgage — Residential:			
Nonaccrual	0	0	103
Past due 90 days or more	216	0	0
Mortgage — Commercial:			
Nonaccrual	0	0	0
Past due 90 days or more	0	0	0
Consumer installment:			
Nonaccrual	0	0	5
Past due 90 days or more	20	5	6
	<u>293</u>	<u>5</u>	<u>131</u>
Total nonperforming loans	293	5	131
Other real estate owned	<u>0</u>	<u>0</u>	<u>0</u>
Total nonperforming assets	<u>\$ 293</u>	<u>\$ 5</u>	<u>\$ 131</u>
Loans outstanding, net	\$ 150,766	\$ 133,267	\$ 119,472
Nonperforming loans to total net loans	0.19%	0.00%	0.11%
Nonperforming loans to total assets	0.15%	0.00%	0.08%
Allowance for loan losses to total loans	1.35%	1.51%	1.45%
Allowance for loan losses to nonperforming loans	703.75%	40,740.00%	1340.46%



Liquidity. Liquidity management for Middlefield is measured and monitored on both a short- and long-term basis, allowing management to better understand and react to emerging balance sheet trends. After assessing actual and projected cash flow needs, management seeks to obtain funding at the most economical cost to Middlefield. Both short- and long-term liquidity needs are addressed by maturities and sales of investments securities, loan repayments and maturities, and liquidating money market investments such as federal funds sold. The use of these resources, in conjunction with access to credit, provide the core ingredients for satisfying depositor, borrower, and creditor needs.

Middlefield's liquid assets consist of cash and cash equivalents, which include investments in very short-term investments (*i.e.*, federal funds sold), and investment securities classified as available for sale. The level of these assets is dependent on Middlefield's operating, investing, and financing activities during any given period. At December 31, 2001, cash and cash equivalents totaled \$5.9 million or 3.0% of total assets while investment securities classified as available for sale totaled \$21.2 million or 10.7% of total assets. Management believes that the liquidity needs of Middlefield are satisfied by the current balance of cash and cash equivalents, readily available access to traditional funding sources, FHLB advances, and the portion of the investment and loan portfolios that mature within one year. These sources of funds will enable Middlefield to meet cash obligations and off-balance sheet commitments as they come due.

Operating activities provided net cash of \$2.7 million, \$3.0 million, and \$2.5 million for 2001, 2000, and 1999, respectively, generated principally from net income of \$2.3 million, \$2.2 million, and \$1.9 million in each of these respective periods.

Investing activities consist primarily of loan originations and repayments and investment purchases and maturities. These activities used \$20.7 million in funds during 2001, principally for the net origination of loans and the purchase of investment securities of \$17.6 million and \$16.6 million, respectively. Such usage of cash was offset by proceeds from repayments and maturities and sales of investment securities of \$13.0 million and \$2.1 million, respectively. For the same period ended 2000, investing activities used \$9.8 million in funds, principally from the net origination of loans of \$14.1 million and the purchases of investment securities of \$2.6 million. In 2000, these cash usages were offset somewhat by an increase in investment securities repayments and maturities of \$4.8 million coupled with a decline in interest-bearing deposits in other institutions from maturities of certificates of deposits of \$2.4 million. In 1999, investing activities used \$14.1 million from the net origination of loans and the purchase of investment securities of \$16.9 million and \$9.8 million. These were offset somewhat by proceeds from repayments and maturities of \$13.2 million.

Financing activities consist of the solicitation and repayment of customer deposits, borrowings and repayments, treasury stock activity, and the payment of dividends. During 2001, net cash provided by financing activities totaled \$19.0 million, principally derived from an increase in deposit accounts in general, and time deposits specifically. During the same period ended 2000, net cash provided by financing activities was \$8.5 million, and consisted of an increase in deposit accounts of \$12.1 million that was offset by the net acquisition of treasury stock of \$1.3 million and the repayment of other borrowings of \$1.7 million.

Liquidity may be adversely affected by unexpected deposit outflows, excessive interest rates paid by competitors, and similar matters. Management monitors projected liquidity needs and determines the level desirable, based in part on Middlefield's commitment to make loans, as well as management's assessment of Middlefield's ability to generate funds. Middlefield anticipates that it will have sufficient liquidity to satisfy estimated short-term and long-term funding needs.

Capital Resources. Middlefield's primary source of capital has been retained earnings. Historically, Middlefield has generated net retained income to support normal growth and expansion. Management has developed a capital planning policy to not only ensure compliance with regulations, but also to ensure capital adequacy for future expansion.

Middlefield is subject to federal regulations imposing minimum capital requirements. Management monitors both Middlefield's and the Bank's Total risk-based, Tier I risk-based and Tier I leverage capital ratios to assess compliance with regulatory guidelines. At December 31, 2001, both Middlefield and the Bank exceeded the minimum risk-based and leverage capital ratio requirements. Middlefield's Total risk-based, Tier I risk-based and Tier I leverage ratios were 17.82%, 16.56%, and 9.94%, and the Bank's were 17.36%, 16.10%, and 9.76%, respectively, at December 31, 2001.

New Accounting Pronouncements

In July 2001, the Financial Accounting Standards Board (FASB) issued FAS No. 141, Business Combinations, effective for all business combinations initiated after June 30, 2001, as well as all business combinations accounted for by the purchase method that are completed after June 30, 2001. The new statement requires that the purchase method of accounting be used for all business combinations and prohibits the use of the pooling-of-interests method. The adoption of Statement No. 141 is not expected to have a material effect on Middlefield's financial position or results of operations.

In July 2001, the FASB issued Statement of Financial Accounting Standards No. 142, Goodwill and Other Intangible Assets, effective for fiscal years beginning after December 15, 2001. The statement changes the accounting for goodwill from an amortization method to an impairment-only approach. Thus, amortization of goodwill, including goodwill recorded in past business combinations, will cease upon adoption of this statement. However, the new statement did not amend FAS 72, *Accounting for Certain Acquisitions of Banking or Thrift Institutions*, which requires recognition and amortization of unidentified intangible assets relating to the acquisition of financial institutions or branches thereof. The FASB has decided to undertake a limited scope project to reconsider the provisions of FAS 72 in 2002. Therefore, the adoption of Statement No. 142 is not expected to have a material effect on Middlefield's financial position or results of operations.

In August 2001, the FASB issued FAS No. 143, *Accounting for Asset Retirement Obligations*, which requires that the fair value of a liability be recognized when incurred for the retirement of a long-lived asset and the value of the asset be increased by that amount. The statement also requires that the liability be maintained at its present value in subsequent periods and outlines certain disclosures for such obligations. The adoption of this statement, which is effective January 1, 2003, is not expected to have a material effect on Middlefield's financial statements.

In October 2001, the FASB issued FAS No. 144, *Accounting for the Impairment or Disposal of Long-Lived Assets*. FAS 144 supercedes FAS 121 and applies to all long-lived assets (including discontinued operations) and consequently amends APB Opinion No. 30, *Reporting Results of Operations-Reporting the Effects of Disposal of a Segment of a Business*. FAS 144 requires that long-lived assets that are to be disposed of by sale be measured at the lower of book value or fair value less costs to sell. FAS 144 is effective for financial statements issued for fiscal years beginning after December 15, 2001 and, generally, its provisions are to be applied prospectively. The

Impact of Inflation and Changing Prices

Middlefield's consolidated financial statements and related data herein have been prepared in accordance with accounting principles generally accepted in the United States of America, which require measurement of financial condition and results of operations in terms of historical dollars, without considering changes in the relative purchasing power of money over time due to inflation.

Because the primary assets and liabilities of Middlefield and the Bank are monetary in nature, changes in the general level of prices for goods and services have a relatively minor impact on total expenses. Increases in operating expenses such as salaries and maintenance are in part attributable to inflation. However, interest rates have a far more significant effect than inflation on the performance of financial institutions, including the Bank.

Quantitative and Qualitative Disclosures About Market Risk

Like other financial institutions, the Bank is subject to interest rate risk. The Bank's interest-earning assets could mature or reprice more rapidly than or on a different basis from its interest-bearing liabilities (primarily borrowings and deposits with short- and medium-term maturities) in a period of declining interest rates. Although having assets that mature or reprice more frequently on average than liabilities will be beneficial in times of rising interest rates, that asset/liability structure will result in lower net interest income in periods of declining interest rates.

Interest rate sensitivity, or interest rate risk, relates to the effect of changing interest rates on net interest income. Interest-earning assets with interest rates tied to the prime rate for example, or that mature in relatively short periods of time, are considered interest-rate sensitive. Interest-bearing liabilities with interest rates that can be repriced in a discretionary manner, or that mature in relatively short periods of time, are also considered interest-rate sensitive. The differences between interest-sensitive assets and interest-sensitive liabilities over various time horizons are commonly referred to as sensitivity gaps. As interest rates change, a sensitivity gap will have either a favorable effect or an adverse effect on net interest income. A negative gap — with liabilities repricing more rapidly than assets — generally should have a favorable effect when interest rates are falling, and an adverse effect when rates are rising. A positive gap — with assets repricing more rapidly than liabilities — generally should have the opposite effect: an adverse effect when rates are falling and a favorable effect when rates are rising.

Middlefield and the Bank have no financial instruments entered into for trading purposes. Interest rates change daily on federal funds purchased and sold. Federal funds are therefore the most sensitive to the market and have the most stable fair values. Loans and deposits tied to indices such as the prime rate or federal discount rate are also market sensitive, with stable fair values. The least sensitive instruments include long-term, fixed-rate loans and securities and fixed-rate savings deposits, which have the least stable fair value. Management of maturity distributions of assets and liabilities between these extremes is as important as the balances maintained. Management of maturity distributions involves matching interest rate maturities as well as principal maturities, and it influences net interest income significantly. In periods of rapidly changing interest rates, a negative or positive gap can cause major fluctuations in net interest income and earnings. Managing asset and liability sensitivities to enhance growth regardless of changes in market conditions is one of the objectives of the Bank's asset/liability management strategy.

Evaluating the Bank's exposure to changes in interest rates is the responsibility of the Asset/Liability Committee, a committee of Bank directors and officers. The Asset/Liability Committee assesses both the adequacy of the management process used to control interest rate risk and the quantitative level of exposure, ensuring that appropriate policies, procedures, management information systems, and internal controls are in place to maintain interest rate risk at appropriate levels. Evaluating the quantitative level of interest rate risk exposure requires assessment of existing and potential effects of changes in interest rates on the bank's financial condition, including capital adequacy, earnings, liquidity, and asset quality.

The Bank uses a static gap analysis to evaluate the risk associated with changes in interest rates. The table below illustrates the maturities or repricing of the Bank's assets and liabilities at December 31, 2001, based upon the contractual maturity or contractual repricing dates of loans and the contractual maturities of time deposits. Prepayment assumptions have not been applied to fixed-rate mortgage loans. Demand loans, loans having no stated schedule of repayments and no stated maturity, and overdrafts are reported as due in one year or less. Allocation of deposits other than time deposits to the various maturity and repricing periods is based upon management's best estimate, taking into account, among other things, the proposed policy statement issued by federal bank regulators on August 4, 1995.

	Maturing or Repricing Periods				
	—Within 3 Months	4 - 12 Months	1 - 5 Years	Over 5 Years	Total
Interest-earning assets:					
Interest-bearing deposits in other institutions	\$ 2,800	\$ 602	\$ 288	\$ 0	\$ 3,690
Investment securities	2,276	10,591	15,172	2,717	31,206
Commercial and industrial loans ⁽¹⁾	8,650	8,462	7,549	3,652	28,313
Real estate construction loans ⁽¹⁾	484	2,000	180	536	3,200
Real estate mortgage loans ⁽¹⁾	23,818	27,170	56,514	8,935	116,437
Consumer installment loans ⁽¹⁾	803	1,360	2,029	686	4,878
Total interest-earning assets	\$ 39,281	\$ 50,185	\$ 81,732	\$ 16,526	\$ 187,724
Interest-bearing liabilities:					
Interest-bearing demand	\$ 978	\$ 652	\$ 1,305	\$ 3,588	\$ 6,523
Money market	3,189	822	909	3,021	7,941
Savings	6,228	4,152	8,304	22,835	41,519
Time	11,791	30,900	43,756	0	86,447
Short-term borrowings	661	0	0	0	661
Other borrowings	57	2,170	6,904	170	9,301
Total interest-bearing liabilities	\$ 22,904	\$ 38,696	\$ 61,178	\$ 29,614	\$ 152,392
Interest sensitivity gap	\$ 16,377	\$ 11,489	\$ 20,554	\$ (13,088)	\$ 35,332
Cumulative interest sensitivity gap	\$ 16,377	\$ 27,866	\$ 48,420	\$ 35,332	
Cumulative interest sensitivity gap as a percent of total assets	9.28%	15.79%	27.44%	20.02%	

(1) For purposes of the gap analysis, loans are not reduced by the allowance for loan losses and nonperforming loans.

The Bank's policy is that the one-year cumulative interest rate sensitivity gap should generally be within a range of negative 20% to positive 20%. As the table above shows, the one-year gap was within this range as of December 31, 2001, with a positive one-year gap of 15.79%. The cumulative gap at December 31, 2001 is due principally to fixed-rate securities and loans in the "over one year to five years" category to maximize yield on assets.

One way to minimize interest rate risk is to maintain a balanced or matched interest-rate sensitivity position. However, profits are not always maximized by matched funding. To increase net interest income, the Bank selectively mismatches asset and liability repricing to take advantage of short-term interest rate movements. The magnitude of the mismatch depends on a careful assessment of the risks presented by forecasted interest rate movements. The risk inherent in such a mismatch, or gap, is that interest rates might not move as anticipated.

Interest rate risk exposure is reviewed in quarterly meetings of the Asset/Liability Committee. At each meeting, guidelines are established for the following quarter and longer-term exposure. Risk is mitigated by matching maturities or repricing more closely. The Bank does not use derivative financial instruments to manage interest rate risk.

Limitations are inherent in any method of measuring interest rate risk. Actual results can differ significantly from simulated results if, for example, market conditions and management strategies vary from the assumptions used in the analysis. The static "gap" analysis is based on assumptions concerning such matters as when assets and liabilities will reprice in a changing interest rate environment. Because these assumptions are no more than estimates, certain assets and liabilities indicated as maturing or repricing within a stated period might actually mature or reprice at different times and at different volumes from those estimated. The actual prepayments and withdrawals experienced by the Bank after a change in interest rates could deviate significantly from those assumed in calculating the data shown in the table. Adjustable-rate loans, for example, commonly have provisions that limit changes in interest rates each time the interest rate changes and on a cumulative basis over the life of the loan. Also, the renewal or repricing of some assets and liabilities can be discretionary and subject to competitive and other pressures. The ability of many borrowers to service their debt could diminish after an interest rate increase. Therefore, the gap table above does not and cannot necessarily indicate the actual future impact of general interest movements on net interest income.

Middlefield's use of a simulation model to better measure the impact of interest rate changes on net interest income is incorporated into the risk management process to effectively identify, measure, and monitor Middlefield's risk exposure. Interest rate simulations using a variety of assumptions are employed by Middlefield to evaluate its interest rate risk exposure. A shock analysis would result in a variation in net interest income of minus 7.57 percent and a variation of minus 9.95 percent in total equity. It is important to note, however, that this exercise would be of worst-case scenario. It would be more likely to have incremental changes in interest rate, rather than a single significant increase or decrease. When management believes interest rate movements will occur, it can restructure the balance sheet and thereby the ratio of rate sensitive assets to rate sensitive liabilities which in turn will effect the net interest income. As mentioned earlier, in gap analysis, as well as simulation analysis, not all assets and liabilities with similar maturities and repricing opportunities will reprice at the same time or to the same degree and therefore, could affect forecasted results.

Market for Middlefield's Common Equity and Related Stockholder Matters

Middlefield had approximately 577 stockholders of record as of March 1, 2002. There is no established market for Middlefield common stock. The stock is traded very infrequently. Bid prices are quoted from time to time on the National Quotation Bureau's "pink sheets" under the symbol "MBCN." The following table shows the high and low bid prices of and cash dividends paid on Middlefield common stock in 2000 and 2001, adjusted for stock splits and stock dividends. This information does not reflect retail mark-up, mark-down or commissions, and does not necessarily represent actual transactions.

	_____ High bid _____	_____ Low bid _____	Cash dividends per share
2001:			
First Quarter	\$ 28.500	\$ 24.000	\$ 0.140
Second Quarter	\$ 28.500	\$ 27.500	\$ 0.140
Third Quarter	\$ 27.500	\$ 23.250	\$ 0.140
Fourth Quarter	\$ 25.500	\$ 24.000	\$ 0.280
2000:			
First Quarter	\$ 31.000	\$ 30.000	\$ 0.100
Second Quarter	\$ 32.500	\$ 31.000	\$ 0.110
Third Quarter	\$ 31.000	\$ 19.625	\$ 0.115
Fourth Quarter	\$ 25.000	\$ 24.000	\$ 0.215

A Decade of Progress

	1992	1993
Interest Income	\$ 7,346,557	\$ 8,628,915
Interest Expense	4,217,447	4,024,735
Net Interest Income	3,129,110	4,604,180
Provision For Loan Losses	120,000	180,000
Net Interest Income After Provision For Loan Losses	3,009,110	4,424,180
Noninterest Income, Including Security Gains/(Losses)	283,184	351,236
Noninterest Expense	2,267,448	2,803,010
Income Before Income Taxes	1,024,846	1,972,406
Income Taxes	184,000	522,000
Net Income	\$ 840,846	1,450,406
<hr/>		
Total Assets	\$85,988,831	\$125,229,507
Deposits	77,542,872	114,808,975
Equity Capital	8,015,527	10,019,887
Loans Outstanding, Net	44,038,285	62,759,415
Allowance For Loan Losses	510,105	681,118
Net Charge-Offs (Recoveries)	92,427	21,598
Full Time Employees (Average Equivalents)	47	48
Number Of Offices	Three	Three
<hr/>		
Earnings Per Share	\$ 0.92	\$ 1.27
Dividends Per Share	0.21	0.23
Book Value Per Share	7.69	8.73
Dividend Pay-out Ratio	25.41%	18.01%
<hr/>		
Cash Dividends Paid	\$ 213,676	\$ 261,159
Return On Average Assets	1.06%	1.28%
Return On Average Equity	10.62%	14.51%

Notes:

(1) The above per share amounts have been restated to reflect the five for one stock split effected in 1995, the 10% stock dividends paid in 1997 and 1998, and the two for one stock split effected in 2000. (2) Applicable income taxes for 1993 are net of cumulative effect of accounting changes for income taxes of \$37,995.

	1994	1995	1996	1997	1998	1999	2000	2001
\$	9,512,712	\$ 10,336,464	\$ 10,375,117	\$ 10,599,777	\$ 10,901,445	\$ 11,448,619	\$ 12,770,170	\$ 13,706,569
	4,200,784	4,855,690	4,985,064	5,083,713	5,084,615	5,048,276	5,909,884	6,747,922
	5,311,928	5,480,774	5,390,053	5,516,064	5,816,830	6,400,343	6,860,286	6,958,647
	198,000	240,000	351,000	200,000	270,000	296,000	275,000	170,000
	5,113,928	5,240,774	5,039,053	5,316,064	5,546,830	6,104,343	6,585,286	6,788,647
	327,607	355,149	586,328	546,103	598,771	804,358	982,663	1,194,193
	3,076,058	3,221,651	3,245,926	3,493,280	3,824,819	4,254,374	4,408,617	4,741,374
	2,365,477	2,374,272	2,379,455	2,368,887	2,320,782	2,654,327	3,159,332	3,241,466
	651,000	681,660	657,000	624,243	630,337	735,318	992,661	970,859
\$	<u>1,714,477</u>	<u>\$ 1,692,612</u>	<u>\$ 1,722,455</u>	<u>\$ 1,744,644</u>	<u>\$ 1,690,445</u>	<u>\$ 1,919,009</u>	<u>\$ 2,236,671</u>	<u>\$ 2,270,607</u>
\$130,589,544	\$134,570,716	\$133,867,396	\$142,276,167	\$155,557,609	\$165,512,453	\$176,488,813	\$197,857,964	
112,082,402	121,247,047	119,254,240	121,482,038	128,827,889	135,094,459	147,166,046	167,382,728	
11,449,463	12,800,762	14,135,561	15,465,255	16,656,797	17,689,055	18,243,362	19,786,807	
80,431,585	86,250,549	83,946,960	88,320,047	102,728,454	119,471,741	133,266,893	150,766,103	
811,212	1,067,956	1,138,919	1,334,800	1,538,726	1,756,137	2,037,322	2,062,252	
67,906	(16,744)	280,037	4,119	66,074	78,589	(6,185)	145,070	
50	53	53	56	59	61	57	64	
Three	Three	Three	Three	Four	Four	Four	Five	
\$	1.50	\$ 1.48	\$ 1.50	\$ 1.52	\$ 1.47	\$ 1.68	\$ 2.02	\$ 2.06
	0.25	0.29	0.34	0.38	0.44	0.50	0.54	0.70
	9.97	11.15	12.31	13.47	14.50	15.49	16.54	17.94
	16.62%	19.64%	22.61%	24.98%	29.53%	29.82%	26.61%	33.94%
\$	284,901	\$ 332,385	\$ 389,365	\$ 435,747	\$ 499,215	\$ 572,343	\$ 595,255	\$ 772,068
	1.34%	1.30%	1.29%	1.23%	1.15%	1.21%	1.31%	1.22%
	14.99%	14.05%	12.21%	11.67%	10.27%	11.13%	12.44%	11.89%

Reflections from The Chairman

“Time waits for no man.” So it is in life and so it is with the history of our bank.

As Chairman of the Board of Directors of The Middlefield Banking Company, I am proud to say I have been an active part of this institution’s time in history since 1977. I have seen our fine bank grow from a modest level in the earliest days to the over \$200 million in assets today. We have successfully mounted five building projects throughout the years, with each new location offering its share of challenges and opportunity.

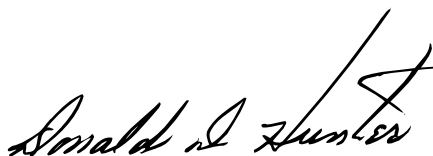
The Middlefield Banking Company moved into the computer age in 1982, installing the first computer system in the basement of the bank. Today we have fully integrated computers, operating at lightening speed, willing and able to accommodate online banking from a customer’s home or office through EasyLink. Computers also allow us to communicate with every branch and every ATM in our network. Who would have thought that possible in the 1940s?

War and hard times have taken their toll on our land of liberty and on our once solid economy. But The Middlefield Banking Company has stood strong. Closing for a “Bank Holiday” by Presidential order in 1933, our predecessors saw the potential doom of The Great Depression. But the bank proved its worth and predicted its future by reopening in short course, testimony to the fine business practices of those who guided its path. Many government bonds were sold by this institution, giving strength to our war efforts abroad. Service men and women of our own local community entrusted The Middlefield Banking Company with their life savings as they went off to war to serve the great country we call home.

How our community has changed over the years, too. Once a thriving, agricultural small town in the rural Western Reserve, merely the last stop of the Interurban Railway, Middlefield is now the center of an industrial revolution within Geauga County. Our area has become home to manufacturing and distribution giants like KraftMaid Cabinetry, Dillen Products, Johnson Rubber, Duramax Marine, and a host of polymer, wood and manufacturing facilities. The Middlefield Banking Company has been instrumental in the furtherance of many of these fine businesses and has contributed to the growth of many more. We have been blessed with many retail, service, food and related businesses moving to our area in support of residents and workers alike.

After the story of The Middlefield Banking Company’s history is recounted, however, the real strength and reason for its success is PEOPLE. This institution would be just that without the thousands of folks who have been dedicated to its future. Customers — from the piggy bank depositor to the largest commercial client — are the fabric that make this bank more than an institution. A knowledgeable caring staff, decisive leadership from qualified administrators, board members with clear direction, and investors with a vision are The Middlefield Banking Company’s success.

I invite you to study our Annual Report that outlines our fiscal success, but more importantly, I invite you to step into the world of The Middlefield Banking Company. Here you will discover the heart of a community bank “serving our customers and our community with honor since 1901.”



Donald D. Hunter
Chairman, Board of Directors



Moments in Time

- 1901:** The Middlefield Banking Company opened its doors on September 16th with authorized working capital of \$25,000.00. Alfonso W. Belden, President. Interest Rate is 4.00%, paid on Certificates of Deposit. Deposits are \$14,208.26.
- 1902:** J.J. Rose, President. Deposits are \$91,659.39.
- 1914:** World War 1 begins.
- 1920:** Joe E. Johnson, President.
- 1929:** The national stock market crashed and The Great Depression begins.
- 1933:** The Bank closes its doors temporarily, as directed by President Franklin D. Roosevelt, nationally called a "Bank Holiday."
- 1934:** The bank reopens with assets of \$218,406. Hugh G. Johnson is President.
- 1941:** Attack on U.S. base at Pearl Harbor. This marks the US involvement in World War II.
- 1943:** Total assets break the million mark at \$1,320,821.
- 1950:** Total assets of \$3.0 million.
- 1963:** Dale McClurg is President. First of several building expansions begin.
- 1981:** Robert E. Stewart is President.
- 1985:** West Branch of Middlefield Banking Company opens. Total bank assets are \$50 million.
- 1986:** Joseph P. Robb is President. Garrettsville Branch of Middlefield Banking Company is opened.
- 1988:** Formation of Middlefield Banc Corp.
- 1993:** Construction of Middlefield Village Center, housing the expanded Middlefield Banking Company as its Main Office. Bank assets total \$100 million.
- 1994:** First offering of MAC ATM cards.
- 1995:** Thomas G. Caldwell is President.
- 1998:** Mantua Branch opens. Data Systems Conversion. \$150 million in assets.
- 1999:** Relocation of Garrettsville Branch to newly constructed facility.
- 2000:** Introduce *EasyLine*, telephone banking.
- 2001:** Open Chardon Branch. Becomes an SEC reporting company. Introduce *EasyLink*, online banking through the Internet.



From Humble Beginnings...

Recognizing the need for a local bank within the community, a group of local business men met in early 1901 to fulfill this need. On September 16, 1901, The Middlefield Banking Company was opened with an authorized capital of \$25,000.

The organizers of the bank were: Joe E. Johnson, A. W. Belden, W. S. Hodges, F. P. Work, C. E. Lampson and E. H. Brigden. Organization was completed by electing the original Board of Directors: C. E. Lampson, J. J. Rose, William Pinks, W. S. Hodges, E. G. Norris, A. W. Belden, C. F. Harrison, Henry Thompson and William Cromwell. This

newly elected Board of Directors selected A. W. Belden as President, J. J. Rose as Vice President and Henry Thompson as Secretary/Treasurer. Walter E. Norris was elected as Cashier of the bank and charged with its proper opening and operation.

From these humble beginnings, the bank has continued to grow and expand in an effort to better serve the community. To

this end, a branch office was established in 1985 on West High Street in Middlefield. The establishment of this office was necessitated by the inability to acquire sufficient land to expand the main office. However, in the early 1990s, additional land became available and in 1993 a newly expanded Main Office facility was opened. In conjunction with this move, the bank constructed Middlefield Village Center.

This project represented a major redevelopment of a key section of Middlefield and represented the bank's commitment to its community. Expansion opportunities

presented themselves in other areas also and were coupled closely with an expanding customer base. An office in Garrettsville, in Portage County, was opened in November of 1986. This office was relocated in January 1999 to a newly constructed facility designed to accommodate the growth of the area and to provide maximum customer service. In November of 1998, an office was opened in the Portage County community of Mantua. Chardon, the county seat of Geauga County, became home to the bank's fifth office in 2001.

In an effort to better position the bank for the future, the Board of Directors, in 1988, formed Middlefield Banc Corp. This Bank Holding Company became the parent of The Middlefield Banking Company through the one-for-one exchange of shares by stockholders in January 1989.

The growth and success of The Middlefield Banking Company and Middlefield Banc Corp. may be attributed to the association of many dedicated men and women who have served as Directors, Officers and Employees. Throughout our 100 year history, only eight individuals have had the distinction to serve as president. They are:

1901 - 1902	<i>Alfonso W. Belden</i>
1902 - 1920	<i>J. J. Rose</i>
1920 - 1933	<i>Joe E. Johnson</i>
1934 - 1963	<i>Hugh G. Johnson</i>
1963 - 1981	<i>Dale McClurg</i>
1981 - 1985	<i>Robert E. Stewart</i>
1986 - 1995	<i>Joseph P. Robb</i>



...We Expand into the 21st Century

The Middlefield Banking Company operates with the general objective to remain a state-chartered independent commercial bank and to aggressively expand its asset base and market share. As a full-service, FDIC-insured commercial bank, The Middlefield Banking Company is proud to offer a full array of financial services.



THE
MIDDLEFIELD
BANKING
CO.

Our Anniversary Celebration

The sunny afternoon of September 15, 2001, ushered in the official 100th Birthday Celebration of The Middlefield Banking Company. After a full year of preparation, the hard-working bank staff saw their efforts rewarded as the community turned out to join in the fun. President and CEO Thomas G. Caldwell delivered a welcoming to the community. State Representative Tim Grendell presented Chairman of the Board of Directors, Don Hunter with a proclamation to commemorate the Bank's Centennial.

Balloons, giveaways, prizes, performances, food and goodies were all plentiful in the day's festivities. Local businesses graciously donated items for daylong door prize drawings. The Bank held a "Guess The Pennies" contest, while several businesses and friends of The Middlefield Banking Company had displays in the Bank's front parking lot. Drawings with prizes were held by The Frank Agency, Western Reserve Title Company and LaMar Printing, Inc. Lucky winners went home with camping chairs, bikes, skates, shirts, mugs, magnets, pens and much more.

What would a party be without a little entertainment? The Cardinal High School Cardinares, under the direction of Mr. Dave Thomas, started our celebration with a patriotic tribute to New York City. Following their performance, entertainment was provided throughout the day by Northeast Ohio Flashettes Baton Group, Maple Town Square Dancers and karaoke. The Middlefield Public Library Puppeteers gave the little ones a show from their miniature stage. The Geauga County Sheriff Department's K-9 Unit also gave a demonstration. Classic car buffs displayed their shiny models in a "Cruisin' Day" car show in the back parking lot.

And food! The Middlefield Fire Department hosted a fish fry, the VFW grilled

hamburgers and hot dogs, and the Cardinares offered cheese on a stick all day long to appease the crowd. The afternoon was topped off with a beautifully decorated "birthday" cake by Saloma Hershberger. Guests were all smiles as pieces of the sweet treat were distributed.

Our celebration was crowned with DJ Dave Adams rockin' the parking lot throughout the evening followed by a spectacular fireworks display at the Cardinal High School football field to seal the first 100 years of operation. It was a full day of fun and celebration — an expression of gratitude to the community from The Middlefield Bank-

“We have just completed our 100th year of service to our community. It has been our pleasure and honor to build upon the commitment of the original far-sighted founders. The proud and talented individuals who now make up our staff are poised to carry us into our second century of service.”



What a Celebration!

September 15th was a beautiful day to show our gratitude to the community. A good time was had by all!



These Articles of Incorporation
 The Middlebury
 Witness
 all

Main Office

incorporation
 ing corpora
 fund raising
 of the Sta
 a corpora
 ral corpora
 hereby certifi
 d corporation
 Banking
 is to be
 a Grange
 cipal bus-



receiving deposits
 and conducting
 as authorized by a savings and
 conducted by a
 corporation. The capital stock of said
 corporation shall be twenty five
 thousand Dollars (\$25,000) divided
 into two hundred and fifty (250) shares
 of One hundred Dollars (\$100) each.
 of the Witness Whereof We have type-
 sets our hands this 12th
 day of March A. D. 1901.

J. E. Johnson
 A. W. Deedes
 W. S. Hodges
 J. P. Work
 E. E. Sampson
 E. H. Bigden



West Branch

Garrettsville Branch



Mantua Branch

Chardon Branch



Directors

Donald D. Hunter – 1977 Chairman
Co-Owner: H & H Hardware, Inc.

Donald E. Villers – 1987
Retired: Copperweld Steel

Thomas C. Halstead – 1988
Co-Owner: Settlers' Farm

George F. Hasman – 1989
Retired: Chairman & President
The Twinsburg Banking Company

Frances H. Frank – 1995
Secretary/Treasurer
The Frank Agency, Inc.

Thomas G. Caldwell – 1997
President & Chief Executive Officer
Middlefield Banc Corp.
The Middlefield Banking Company

Richard T. Coyne – 1997
General Manager
Jaco Products

Martin S. Paul – 1998
Vice President
Paul's Lumber

James R. Heslop, 2nd – 2001
Executive Vice President/Chief Operating Officer
Middlefield Banc Corp.
The Middlefield Banking Company

Officers

Thomas G. Caldwell – 1986
President and Chief Executive Officer

James R. Heslop, 2nd – 1996
Executive Vice President

Teresa M. Hetrick – 1996
Sharon R. Jarold – 2001
Senior Vice President
Operations/Administration

Jay P. Giles – 1998
Senior Vice President
Senior Commercial Lender

Donald L. Stacy – 1999
Chief Financial Officer

Nancy C. Snow – 1979
Vice President and Corporate
Secretary and West Branch Manager

Kathleen M. Johnson – 1971
Vice President
Chief Accounting Officer

Jack L. Lester – 1990
Vice President

Joann Vance – 1986
Vice President
Garrettsville Branch Manager

Vice President
Senior Retail Lender

William L. Douglass – 1997
Vice President/Lending

Vice President

Gail Neikirk – 1983
Assistant Vice President

Karen Branham – 1983
Assistant Vice President

Compliance and Security Officer

Assistant Vice President
Lending

Michael P. Korpita – 1984
Internal Auditor
Alfred F. Thompson, Jr. – 1996

Christine A. Polzer – 1989
Network Administrator

Thomas R. Neikirk – 1994
Banking Officer

R. E. West – 1998

Staff

Main Office

Karen Westover – 1983 – Head Teller
Louise Fenselon – 1984 – Teller
Bonnie Steele – 1985 – Customer Services
Coreen DeCaro – 1998 – Teller
Diana Koller – 1998 – Teller
Pamela Hummel – 1999 – Teller
Summer Phillips – 1999 – Customer Services
Elizabeth Pixley – 2001 – Teller *
Monica Szilagyi – 2001 – Teller*
Amanda Wright – 2001 – Teller*
Jessica Osburn – 2001 – Receptionist

West Branch

Patti Russo – 1982 – Customer Services
Rachel Lilly – 1985 – Head Teller
Kelly Gibney – 1987 – Teller
Pam Malcuit – 1989 – Customer Services
Lori Sheridan – 2000 – Teller*
Stacy Siracki – 2000 – Teller
Lisa Sanborn – 2000 – Teller
Tabitha White – 2001 – Teller*
Ellen Wilson – 2001 – Teller

Garrettsville Branch

Marian Nichols – 1986 – Teller*
Kathy Vanek – 1998 – Customer Services
Colleen Steele – 1998 – Teller*
Vickie Moss – 1998 – Teller
Melissa Smith – 2000 – Teller
Michelle Ruoff – 2001 – Teller
Jennifer Hoffman – 2001 – Teller*
Jeremy Bailey – 2001 – Teller*

Mantua Branch

Michele Tushar – 2001 – Head Teller/CSR
Sara Hedge – 2000 – Teller
Samantha Macik – 2001 – Teller*

Chardon Branch

Lori Graham – 1998 – Branch Supervisor
Lisa Schleger – 2000 – Teller
Amanda Miller – 2001 – Teller
Susan Fenshaw – 2001 – Head Teller
Gretchen Mihalic – 2001 – Teller*

Loan Department

Helen Stowe – 1985 – Loan Administrative Assistant
Jennifer Sponseller – 1997 – Loan Administrative Assistant
Jane Armstrong – 1998 – Loan Administrative Assistant
Vivian Helmick – 1998 – Loan Administrative Assistant
Marlin J. Moschell – 2000 – Loan Officer
Carolyn Fackler – 2001 – Loan Administrative Assistant
Susan Biley – 2001 – Loan Department Receptionist

Operations

Donna Barnett – 1971 – Proof Operator
Donna Williams – 1990 – Bookkeeper
Carole Triplett – 1993 – Bookkeeper
Lauren Harth – 1995 – Audit Clerk*
Tara Morgan – 1997 – Bookkeeper
Derrick Pilarczyk – 1999 – Facility Maintenance
Ashley Durst – 2001 – Bookkeeper
Kristina McGuire – 2001 – Network Support

* Part Time



Shareholder Information

CORPORATE HEADQUARTERS

The Corporation's headquarters is located at:

Middlefield Banc Corp.
15985 East High Street
P. O. Box 35
Middlefield, Ohio 44062
(440) 632-1666 (888) 801-1666

FORM 10-K AND 10-Q AVAILABILITY

A copy of Middlefield Banc Corp.'s Annual Report on Form 10-K and Quarterly Reports on 10-Q filed with the Securities and Exchange Commission will be furnished to any shareholder, free of charge, upon written or e-mail request to:

Donald L. Stacy
Treasurer and CFO
Middlefield Banc Corp.
P. O. Box 35
Middlefield, Ohio 44062
Or
dstacy@middlefieldbank.com

STOCK TRADING

The symbol for Middlefield Banc Corp. common stock is MBCN and the CUSIP is 596304204.

Sweney Cartwright & Co.
George Geissbuhler
17 South High Street
Columbus, Ohio 43215
(614) 228-5391
(800) 334-7481

Robert W. Baird & Co., Incorporated
Rolly Rastetter / Richard W. Comstock
3875 Embassy Parkway, Suite 300
Akron, Ohio 44333
(330) 670-0350
(877) 792-7868

INDEPENDENT AUDITORS

S. R. Snodgrass, A.C.
1000 Stonewood Drive, Suite 200
Wexford, PA 15090-8399
(724) 934-0344

TRANSFER AGENT AND REGISTRAR

The Middlefield Banking Company
Shareholder Relations Department
P. O. Box 35
Middlefield, Ohio 44062

INTERNET INFORMATION

Information on The Middlefield Banking Company's products and services is available on the Internet at www.middlefieldbank.com.

DIVIDEND PAYMENT DATES

Subject to action by the Board of Directors, Middlefield Banc Corp. will pay dividends in March, June, September and December.

DIRECT DEPOSIT OF DIVIDENDS

The direct deposit program, which is offered at no charge, provides for automatic deposit of quarterly dividends directly to a checking or savings account with The Middlefield Banking Company. For information regarding this program, please call 1-888-801-1666.

ANNUAL MEETING

The Annual Meeting of Shareholders will be held at 1:00 p.m. on Wednesday, May 15, 2002, at Grandview Inn, 13404 Old State Road, Middlefield, Ohio.



www.middlefieldbank.com

Photographs were courtesy of the archives of Mr. Richard Roose and The Middlefield Banking Co.

