COMMUNITY BANKSHARES INC /SC/
Form 10-Q
November 14, 2001

SECURITIES AND EXCHANGE COMMISSION

WASHINGTON, D. C. 20549

FORM 10-Q

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

For the quarterly period ended Sept. 30, 2001  Commission File number: 000-22054

COMMUNITY BANKSHARES, INC.
(Exact Name of Registrant as Specified in its Charter)

| | |
|---|---|
| South Carolina | 57-0966962 |
| (State or Other Jurisdiction of Incorporation or Organization) | (IRS Employer Identification Number) |

791 Broughton St., Orangeburg, South Carolina 29115
(Address of Principal Executive Office, Zip Code)

(803) 535-1060
(Registrant's telephone number, including area code)

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the Registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days.     Yes [X] No [ ]

State the number of shares outstanding of each of the issuer's classes of common equity, as of the latest practicable date: 3,299,674 shares of common stock outstanding as of November 1, 2001.

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Part I. Item 1. Financial Statements

COMMUNITY BANKSHARES, INC. - CONSOLIDATED BALANCE SHEETS

($ amounts in thousands)

ASSETS

Cash and due from other financial institutions:

Non-interest bearing ...
Federal funds sold ...

Total cash and cash equivalents ...
Interest bearing deposits in other banks ...
Investment securities:
Securities held to maturity ...
Securities available for sale ...
Loans held for resale ...
Loans ...
Less, allowance for loan losses ...

Net loans ...
Premises and equipment ...
Accrued interest receivable ...
Deferred income taxes ...

| | |
|---|---|
| Other real estate owned ........................................................................ | |
| Other assets ........................................................................ | |
| Total assets ........................................................................ | |
| **LIABILITIES AND SHAREHOLDERS' EQUITY** | |
| Deposits: | |
| Non-interest bearing ........................................................................ | |
| Interest bearing ........................................................................ | |
| Total deposits ........................................................................ | |
| Federal funds purchased and securities sold under agreements to repurchase ........................................ | |
| Federal Home Loan Bank advances ........................................................................ | |
| Other liabilities ........................................................................ | |
| Total liabilities ........................................................................ | |
| Shareholders' equity: | |
| Common stock | |
| No par, authorized shares 12,000,000, issued and outstanding 3,204,220 in 2001 and 3,199,180 in 2000 ............................ | |
| Retained earnings ........................................................................ | |
| Accumulated other comprehensive income (loss) ........................................ | |
| Total shareholders' equity ........................................................................ | |
| Total liabilities and shareholders' equity ........................................ | |

THE ACCOMPANYING NOTES ARE AN INTEGRAL PART OF THE FINANCIAL STATEMENTS



COMMUNITY BANKSHARES, INC. - CONSOLIDATED STATEMENTS OF
CHANGES IN SHAREHOLDERS' EQUITY
for the nine months ended September 30, 2001 and 2000 (Unaudited)
($ amounts in thousands)

| | Common Stock | | Retai |
|---|---|---|---|
| | Shares | Amount | Earni |
| | | (dollar amount | |
| Balances at Dec. 31, 1999 ................................ | 3,191,462 | $ 14,207 | $ 6 |
| Comprehensive income: | | | |
| Net income ........................................ | | | 2 |
| Other comprehensive income (loss) net of tax: | | | |
| Unrealized gain (loss) on securities ................ | | | |
| Cash-in-lieu of shares in connection with Jan. 31, 2000 stock dividend................................ | (137) | | |

| | | | |
|---|---|---|---|
| Market value of shares issued in five percent stock dividend........................ | - | 1,709 | (1 |
| Shares issued under option agreement .................... | 2,520 | 19 | |
| Costs of stock dividend ................................ | | (10) | |
| Dividends paid ......................................... | - | - | |
| Balances at Sept. 30, 2000 .............................. | 3,193,845 | $ 15,925 | $ 6 |
| Balances at Dec. 31, 2000 ............................... | 3,199,180 | $ 15,928 | $ 7 |
| Comprehensive income: | | | |
| Net income ......................................... | | | 2 |
| Other comprehensive income (loss) net of tax: | | | |
| Unrealized gain (loss) on securities ............... | | | |
| Shares issued under option agreement .................... | 5,040 | 39 | |
| Dividends paid ......................................... | - | - | |
| Balances at September 30, 2001 .......................... | 3,204,220 | $ 15,967 | $ 9 |

THE ACCOMPANYING NOTES ARE AN INTEGRAL PART OF THE FINANCIAL STATEMENTS

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COMMUNITY BANKSHARES, INC. - CONSOLIDATED STATEMENTS OF INCOME (Unaudited)

| | Nine months ended Sept. | |
|---|---|---|
| | 2001 | 2000 |
| ($ amounts in thousands) | | |
| Interest and dividend income: | | |
| Interest and fees on loans ................................ | $ 13,694 | $ 12,18 |
| Deposits with other financial institutions ................ | 144 | 5 |
| Investment securities: | | |
| Interest - U. S. Treasury and U. S. Government Agencies ............................ | 1,602 | 2,15 |
| Dividends ............................................. | 118 | 9 |
| Total investment securities .......................... | 1,720 | 2,25 |
| Federal funds sold and securities purchased under agreements to resell .................... | 642 | 25 |
| Total interest and dividend income ................... | 16,200 | 14,74 |
| Interest expense: | | |
| Deposits: | | |
| Certificates of deposit of $100,000 or more ............. | 1,912 | 1,66 |
| Other .................................................. | 5,089 | 4,47 |

| | | |
|---|---|---|
| Total deposits | 7,001 | 6,13 |
| Federal funds purchased and securities sold under agreements to repurchase | 212 | 11 |
| Federal Home Loan Bank advances | 861 | 86 |
| Total interest expense | 8,074 | 7,11 |
| Net interest income | 8,126 | 7,62 |
| Provision for loan losses | 457 | 49 |
| Net interest income after provision for loan losses | 7,669 | 7,13 |
| Non-interest income: | | |
| Service charges on deposit accounts | 1,490 | 1,05 |
| Gain on sale of securities | 14 | |
| Other | 483 | 29 |
| Total non-interest income | 1,987 | 1,34 |
| Non-interest expense: | | |
| Salaries and employee benefits | 3,172 | 2,83 |
| Premises and equipment | 703 | 69 |
| Other | 1,447 | 1,33 |
| Total non-interest expense | 5,322 | 4,85 |
| Net income before taxes | 4,334 | 3,63 |
| Provision for income taxes | 1,541 | 1,29 |
| Net income | $ 2,793 | $ 2,34 |
| Basic earnings per common share: | | |
| Weighted average shares outstanding | 3,201,560 | 3,194,68 |
| Net income per common share | $ 0.87 | $ 0.7 |
| Diluted earnings per common share: | | |
| Weighted average shares outstanding | 3,222,456 | 3,216,20 |
| Net income per common share | $ 0.87 | $ 0.7 |

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COMMUNITY BANKSHARES, INC. - CONSOLIDATED STATEMENTS OF CASH FLOWS (Unaudited)

Cash flows from operating activities:

Net income ....................................................................................

Adjustments to reconcile net income to net cash provided (used) by operating activities

Depreciation ..........................................................................

Provision for loan losses ....................

Accretion of discounts and amortization of premiums - investment securities - net ....................

Changes in assets and liabilities:

Proceeds of sale of loans held for resale ....................

Origination of loans held for resale ....................

(Increase) decrease in interest receivable ....................

Decrease in other assets ....................

Increase in other liabilities ....................

Net cash provided by operating activities ....................

Cash flows from investing activities:

Net (increase) in interest bearing deposits ....................

Proceeds from maturities of investment securities - held to maturity ....................

Purchases of investment securities - held to maturity ....................

Proceeds from maturities of investment securities - available for sale ....................

Purchases of investment securities - available for sale ....................

Net (increase) in loans to customers ....................

Purchase of premises and equipment ....................

Net (increase) in other real estate ....................

Net cash (used) in investing activities ....................

Cash flows from financing activities:

Net increase in demand, savings, and time deposits ....................

Net increase in federal funds purchased and securities sold under agreements to repurchase ....................

(Decrease) in Federal Home Loan Bank advances ....................

Common stock issued under option plan ....................

Dividends paid in cash ....................

Net cash provided by financing activities ....................

Net increase (decrease) in cash and cash equivalents ....................

Cash and cash equivalents-beginning of period ....................

Cash and cash equivalents-end of period ....................

THE ACCOMPANYING NOTES ARE AN INTEGRAL PART OF THE FINANCIAL STATEMENTS

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Notes to Unaudited Consolidated Financial Statements

Summary of Significant Accounting Principles

A summary of significant accounting policies and the audited financial statements for 2000 are included in Corporation's Annual Report on Form 10-K for the year ended December 31, 2000.

Principles of Consolidation

The consolidated financial statements include the accounts of Community Bankshares, Inc. (CBI), the parent company, and Orangeburg National Bank, Sumter National Bank and Florence National Bank, its wholly owned subsidiaries. All significant intercompany items have been eliminated in the consolidated statements.

Management Opinion

The interim financial statements in this report are unaudited. In the opinion of management, all the adjustments necessary to present a fair statement of the results for the interim period have been made. Such adjustments are of a normal and recurring nature.

The results of operations for any interim period are not necessarily indicative of the results to be expected for an entire year. These interim financial statements should be read in conjunction with the annual financial statements and notes thereto contained in the 2000 Annual Report on Form 10-K.

Changes in Comprehensive Income Components

The Financial Accounting Standards Board's Statement of Financial Accounting Standards No. 130, "Reporting Comprehensive Income," effective for fiscal years beginning after December 15, 1997, establishes standards for reporting and display of comprehensive income and its components in a full set of general-purpose financial statements. Disclosure as required by the Statement is as follows:

| | Before-<br>Amoun |
|---|---|
| Unrealized gains (losses) on securities: | |
| Unrealized holding gains (losses) arising during period ............................ | $(640, |
| Other comprehensive income, Sept. 30, 2000 ........................................... | $(640, |
| Unrealized gains (losses) on securities: | |
| Unrealized holding gains (losses) arising during period ............................. | $176, |
| Other comprehensive income, Sept. 30, 2001 ........................................... | $176, |



COMMUNITY BANKSHARES, INC. - AVERAGE BALANCE SHEETS, YIELDS, AND RATES

| | Nine months |
|---|---|
| (Dollars in Thousands) | |
| | 2001 |

| Assets | Average Balance | Interest Income/ Expense | Yields/ Rates |
|---|---|---|---|
| Interest bearing deposits | $ 4,441 | $ 144 | 4.32% |
| Investment securities taxable | 36,490 | 1,699 | 6.21% |
| Investment securities--tax exempt | 746 | 21 | 5.69% |
| Federal funds sold | 19,514 | 642 | 4.39% |
| Loans receivable | 206,419 | 13,694 | 8.85% |
| Total interest earning assets | 267,610 | 16,200 | 8.07% |
| Cash and due from banks | 9,166 | | |
| Allowance for loan losses | (2,605) | | |
| Premises and equipment | 4,475 | | |
| Other assets | 3,058 | | |
| Total assets | $281,704 | | |
| Liabilities and Shareholders' Equity | | | |
| Interest bearing deposits | | | |
| Savings | $ 37,290 | $ 927 | 3.31% |
| Interest bearing transaction accounts | 23,389 | 165 | 0.94% |
| Time deposits | 136,836 | 5,909 | 5.76% |
| Total interest bearing deposits | 197,515 | 7,001 | 4.73% |
| Short term borrowing | 7,414 | 212 | 3.81% |
| FHLB advances | 19,773 | 861 | 5.81% |
| Total interest bearing liabilities | 224,702 | 8,074 | 4.79% |
| Noninterest bearing demand deposits | 30,779 | | |
| Other liabilities | 1,735 | | |
| Shareholders' equity | 24,488 | | |
| Total liabilities & shareholders' equity | $281,704 | | |
| Interest rate spread | | | 3.28% |
| Net interest income and net yield on earning assets | | $ 8,126 | 4.05% |

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

Forward Looking Statements

Statements included in Management's Discussion and Analysis of Financial Condition and Results of Operations which are not historical in nature are intended to be, and are hereby identified as 'forward looking statements' for purposes of the safe harbor provided by Section 21E of the Securities

Exchange Act of 1934, as amended. The Corporation cautions readers that forward looking statements, including without limitation, those relating to the Corporation's future business prospects, revenues, working capital, liquidity, capital needs, interest costs, and income, are subject to certain risks and uncertainties that could cause actual results to differ materially from those indicated in the forward looking statements, due to several important factors herein identified, among others, and other risks and factors identified from time to time in the Corporation's reports filed with the Securities and Exchange Commission.

RESULTS OF OPERATIONS FOR THE NINE MONTHS ENDED SEPTEMBER 30, 2001 COMPARED TO SEPTEMBER 30, 2000

Net Income

For the nine months ended September 30, 2001 CBI earned a consolidated profit of $2,793,000 compared to $2,342,000 for the comparable period in 2000, an increase of 19.3% or $451,000. Basic and diluted earnings per share were $.87 in the 2001 period compared to $.73 for the 2000 period.

For the 2001 period Orangeburg National Bank reported a profit of $1,869,000 compared to $1,687,000 for the 2000 period, an increase of 10.8% or $182,000.

For the 2001 period Sumter National Bank reported a profit of $849,000 compared to $634,000 for the 2000 period, an increase of 33.9% or $215,000. The Sumter bank began operation in September 1996.

For the 2001 period Florence National Bank reported a profit of $125,000 compared to $39,000 for the 2000 period, an increase of 220% or $86,000. The Florence bank began operation in July 1998.

As noted above, consolidated net income for the nine months ended September 30, 2001, increased from the prior year by 19.3% or $451,000. The major components of this increase are discussed below. Net interest income before provision for loan losses for the nine months ended September 30, 2001 increased to $8,126,000 compared to $7,625,000 for the same period in 2000, an increase of 6.6% or $501,000. For the 2001 period the provision for loan losses was $457,000 compared to $490,000 for the 2000 period, a decrease of 6.7% or $33,000. Non-interest income for the 2001 period was $1,987,000 compared to $1,349,000 for the 2000 period, a 47.3% or $638,000 increase. For the same periods, non-interest expense was $5,322,000 compared to $4,852,000, a 9.7% or $470,000 increase.

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Profitability

Profitability may be measured through the ROA (return on average assets) and the ROE (return on average equity). Return on assets is the income for the period divided by the average assets for the period, annualized. Return on equity is the income for the period divided by the average equity for the period, annualized. Operating results for the nine months ended September 30, 2001 and 2000 yield the results in the table shown below.

Nine months ended Sept. 30,
2001 2000

| | ---- | ---- |
|---|---|---|
| | (dollars in thousands) | |
| Average assets ............ | $281,704 | $243,697 |
| ROA ....................... | 1.32% | 1.28% |
| Average equity ............ | $24,488 | $21,047 |
| ROE ....................... | 15.21% | 14.84% |
| Net income ................ | $2,793 | $2,342 |

Net interest income

Net interest income, the major component of CBI's income, is the amount by which interest and fees on interest earning assets exceeds the interest paid on interest bearing deposits and other interest bearing funds. During the first nine months of 2001 net interest income after provision for loan losses increased to $7,669,000 from $7,135,000, a 7.5% or $534,000 increase over the first nine months of 2000. This improvement was the result of a $38 million increase in the average volume of earning assets. The average yield on earning assets decreased to 8.07% for the 2001 period from 8.56% for the 2000 period. This decline was the result of market interest rate declines. During the first nine months of 2001 the prime lending rate declined from 9.0% to 5.50%. During the first nine months of 2000 the prime lending rate increased from 8.75% to 9.50%.

For the first nine months of 2001 the cost of funds averaged 4.79%, decreased from 4.90% for the first nine months of 2000. The effect of these changes was a net interest spread (yield on earning assets less cost of interest bearing liabilities) of 3.28% for the 2001 period, decreased from 3.66% for the 2000 period. CBI's net interest margin (net interest income divided by total earning assets) was 4.05% for the 2001 period compared to 4.43% for the 2000 period.

Interest Income

Elsewhere in this report is a table comparing the average balances, yields, and rates for the interest rate sensitive segments of the Corporation's balance sheets for the nine months ended September 30, 2001 and 2000. A discussion of that table follows.

Total interest income for the first nine months of 2001 was $16,200,000 compared with $14,744,000 for the same period in 2000, a 9.9% or $1,456,000 increase. The yield on average earning assets for the 2001 period was 8.07%, decreased from 8.56% for the 2000 period. The decline in yields was directly related to the overall decline in market interest rates. Total average interest earning assets for the 2001 period were $267,610,000 compared to $229,709,000 for the 2000 period, an increase of 16.5% or $37,901,000.



The loan portfolio earned $13,694,000 for the first nine months of 2001 compared to $12,184,000 for the same period of 2000, a 12.4% or $1,510,000 increase. The yield decreased to 8.85% for the 2001 period from 9.24% for the 2000 period. The average size of the loan portfolio was $206,419,000 for the 2001 period compared to $175,774,000 for the 2000 period, an increase of 17.4% or $30,645,000.

The taxable investment portfolio earned $1,699,000 for the first nine months in 2001 compared to $2,230,000 for the same period in 2000, a 23.8% or $531,000 decrease. The yield decreased to 6.21% in the 2001 period from 6.37% in the 2000 period. The average size of the portfolio was $36,490,000 in the 2001 period compared to $46,646,000 in the 2000 period, a decrease of 21.8% or $10,156,000. As bond market interest rates declined during 2001 the Corporation had numerous securities called prior to maturity.

The tax-exempt investment portfolio earned $21,000 for the first nine months in 2001 compared to $25,000 for the same period in 2000, a 16% or $4,000 decrease. The yield (on a taxable equivalent basis) on the portfolio was 5.69% for the 2001 period, decreased from 6.27% for the 2000 period. The average size of the portfolio was $746,000 for the 2001 period compared to $806,000 in the 2000 period, a decrease of 7.4% or $60,000.

Interest bearing deposits in other banks contributed $144,000 for the first nine months of 2001 compared to $53,000 for the same period in 2000, an increase of 172% or $91,000. The yield on these deposits decreased to 4.32% for the 2001 period from 6.10% in the 2000 period. CBI averaged $4,441,000 in the 2001 period compared to $1,159,000 in the 2000 period, an increase of 283% or $3,282,000. The increase in these deposits was the result of declining market interest rates, which caused numerous calls of investment securities prior to maturity. The funds resulting from these calls were temporarily invested in interest bearing deposits and federal funds.

Federal funds sold earned $642,000 the first nine months of 2001 compared to $252,000 for the same period in 2000, an increase of 155% or $390,000. Yields decreased to 4.39% for the 2001 period from 6.31% for the 2000 period. For the 2001 period CBI increased its average volume in federal funds sold to $19,514,000 compared to $5,324,000 for the 2000 period, a 267% or $14,190,000 increase.

Interest Expense

Interest expense for the first nine months of 2001 was $8,074,000 compared to the prior year's $7,119,000, a 13.4% or $955,000 increase. The average volume of interest bearing liabilities was $224,702,000 for the 2001 period compared to $193,799,000 for the 2000 period, a 15.9% or $30,903,000 increase. The average rate paid for interest-bearing liabilities during the 2001 period was 4.79%, decreased from 4.90% for the 2000 period.

The cost of savings accounts was $927,000 in the first nine months in 2001 compared to $955,000 in the first nine months of 2000, a 2.9% or $28,000 decrease. Average savings deposit balances were $37,290,000 for the 2001 period compared to $32,650,000 for the 2000 period, an increase of 14.2% or $4,640,000. The average rate paid on these funds decreased to 3.31% from 3.90%.

Interest bearing transaction accounts cost $165,000 for the first nine months in 2001 compared to the prior year's $241,000, a decrease of 31.5% or



$76,000. The volume of these deposits was $23,389,000 for the 2001 period compared to $20,519,000 for the 2000 period, a 14% or $2,870,000 increase. The average rate paid on these funds in the 2001 period decreased to .94% from 1.57% in the 2000 period.

Time deposits cost $5,909,000 for the first nine months of 2001 compared to $4,943,000 for the first nine months of the prior year, an increase of 19.5% or $966,000. The volume was $136,836,000 for the 2001 period compared to $117,735,000 for the 2000 period, a 16.2% or $19,101,000 increase. The average rate paid on these funds increased to 5.76% for the 2001 period from 5.60% for the 2000 period. This increase runs contrary to market interest rates but reflects increased competition for time deposits in the Corporation's markets.

Short-term borrowings consist of federal funds purchased and securities sold under agreements to repurchase. This is a relatively small and volatile part of the balance sheet. It cost $212,000 for the first nine months in 2001 compared to $117,000 for the first nine months of 2000, an increase of 81.2% or $95,000. The volume of these funds was $7,414,000 in the 2001 period compared to $3,553,000 in the 2000 period, an increase of 109% or $3,861,000. The average rate paid on these funds decreased to 3.81% from 4.39%.

Borrowings from the Federal Home Loan Bank cost $861,000 for the first nine months in 2001 compared to $863,000 for the first nine months in 2000, virtually unchanged. The advances averaged $19,773,000 during the 2001 period compared to $19,342,000 for the 2000 period, a 2.2% or $431,000 increase. The average rate paid on these funds decreased to 5.81% from 5.95%.

Non-Interest Income

Non-interest income for the first nine months of 2001 grew to $1,987,000 compared to $1,349,000 in the first nine months of 2000, a 47.3% or $638,000 increase. Much of this increase resulted from the introduction of a new service, an automated overdraft courtesy line for customers. This service provides for a flat fee for paying customer checks in overdraft that is equivalent to the fee charged for returned checks. Customers who use this service are subject to other terms and conditions. Also, some of the increase was due to increased fee income from mortgages originated for sale into the secondary market.

Non-Interest Expense

For the first nine months of 2001 non-interest expenses were $5,322,000 compared to $4,852,000 for the first nine months of 2000, a 9.7% or $470,000 increase. This increase is related to higher levels of business activity and included the following components:

For the 2001 period personnel costs were $3,172,000 compared to $2,831,000 for the 2000 period, an increase of 12% or $341,000;

For the 2001 period premises and equipment expenses were $703,000 compared to $690,000 for the 2000 period, an increase of 1.9% or $13,000; and

For the 2001 period other costs were $1,447,000 compared to $1,331,000 for the 2000 period, an increase of 8.7% or $116,000.

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Income Taxes

CBI provided $1,541,000 for federal and state income taxes during the first nine months of 2001 compared to $1,290,000 for the same period in 2000, a 19.5% or $251,000 increase. The average tax rate for the 2001 period was 35.6% and for the 2000 period it was 35.5%.

RESULTS OF OPERATIONS FOR THE QUARTERS ENDED SEPTEMBER 30, 2001 AND 2000

Net Income

For the quarter ended September 30, 2001, CBI earned a consolidated profit of $962,000, compared to $865,000 for the comparable period of 2000, an increase of 11.2% or $97,000. Basic or diluted earnings per share were $.30 in the 2001 period, compared to $.27 for the 2000 period. The changes in the items comprising net interest income, which are discussed below, resulted from essentially the same factors discussed above regarding the results of operation for the nine months ended September 30, 2001.

Net interest income

Net interest income before provision for loan losses for the quarter ended September 30, 2001 increased to $2,770,000 compared to $2,648,000 for the same period in 2000, an increase of 4.6% or $122,000. For the same period the provision for loan losses was $180,000 compared to $152,000 for the 2000 period, an increase of 18.4% or $28,000.

Interest Income

Total interest income for the third quarter 2001 was $5,261,000 compared to $5,273,000 for the same period in 2000, virtually unchanged.

The loan portfolio earned $4,578,000 for the third quarter 2001 compared to $4,421,000 for the same period of 2000, a 3.6% or $157,000 increase.

The investment portfolio earned $457,000 for the third quarter 2001 compared to $763,000 for the same period of 2000 period, a 40.1% or $306,000 decrease.

Interest bearing deposits in other banks contributed $38,000 for the third quarter 2001 compared to $25,000 for the same period of 2000, an increase of 52% or $13,000.

Federal funds sold earned $188,000 the third quarter of 2001 compared to $64,000 for the same period, an increase of 194% or $124,000.

Interest expense

Interest expense for the third quarter of 2001 was $2,491,000 compared to $2,625,000 for the same period of 2000, a 5.1% or $134,000 decrease.

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Non-interest income and expense

Non-interest income for the 2001 period was $744,000 compared to $464,000 for the 2000 period, a 60.3% or $280,000 increase. This increase was mostly the result of the introduction of the new automated overdraft service. Non-interest expense was $1,833,000 compared to $1,625,000, a 12.8% or $208,000 increase.

CHANGES IN FINANCIAL POSITION

Investment portfolio

The investment portfolio is comprised of held to maturity securities and available for sale securities. CBI and its three banks usually purchase short-term issues (ten years or less) of U. S Treasury and U. S. Government agency securities for investment purposes. At September 30, 2001 the held to maturity portfolio totaled $2,149,000 compared to $12,371,000 at December 31, 2000, a decrease of 82.6% or $10,222,000. At September 30, 2001, the available for sale portfolio totaled $33,002,000 compared to $41,195,000 at December 31, 2000, a decrease of 19.9% or $8,193,000. Most of the decline in the banks' investment portfolios was due to the call of many securities during 2001, which resulted from the decline in bond market interest rates. The following chart summarizes the investment portfolios at September 30, 2001, and December 31, 2000.

| | Septem | |
|---|---|---|
| | Held to maturity | |
| | Amortized cost | Fair value |
| | (dollars | |
| U. S. Government and federal agencies ........................ | $2,149 | $2,157 |
| Tax exempt securities ......................................... | - | - |
| Other equity securities ....................................... | - | - |
| Total ......................................................... | $2,149 | $2,157 |
| Unrealized gain ............................................... | $ 8 | |

| | Decemb | |
|---|---|---|
| | Held to maturity | |
| | Amortized cost | Fair value |
| | (dollars | |
| U. S. Government and federal agencies ........................ | $12,371 | $12,217 |
| Tax exempt securities ......................................... | - | - |
| Other equity securities ....................................... | - | - |
| Total ......................................................... | $12,371 | $12,217 |
| Unrealized (loss) ............................................. | $ (154) | |



Loan portfolio

The loan portfolio is primarily consumer and small business oriented. At September 30, 2001 the loan portfolio was $219,125,000 compared to $195,077,000 at December 31, 2000, a 12.3% or $24,048,000 increase. The following chart summarizes the loan portfolio at September 30, 2001 and December 31, 2000.

| | Sept. 30, 2001 | Dec. 31, 2000 |
|---|---|---|
| | (dollars in thousands) | |
| Real estate | $138,258 | $113,543 |
| Commercial | 55,260 | 52,264 |
| Loans to individuals | 25,607 | 29,270 |
| Total | $219,125 | $195,077 |

Past Due and Non-Performing Assets and the Allowance for Loan Losses

CBI closely monitors past due loans and loans that are in non-accrual status and other real estate owned. Below is a summary of past due and non-performing assets at September 30, 2001 and December 31, 2000.

| | Sept. 30, 2001 | Dec. 31, 2000 |
|---|---|---|
| | (dollars in thousands) | |
| Past due 90 days + accruing loans | $101 | $ 93 |
| Non-accrual loans | $413 | $238 |
| Impaired loans (included in non-accrual) | $413 | $238 |
| Other real estate owned | $267 | $ - |

Management considers the past due and non-accrual amounts at September 30, 2001 to be reasonable in relation to the size of the portfolio and manageable in the normal course of business. The increase in non-accrual assets is associated with a small number of loans and is not indicative, in the opinion of management, of any trend.

CBI had no restructured loans during any of the above listed periods.

Allowance for Loan Losses

The Corporation operates three independent community banks in central South Carolina. Under the provisions of the National Bank Act each board of directors is responsible for determining the adequacy of its bank's loan loss allowance. In addition, each bank is supervised and regularly examined by the Office of the Comptroller of the Currency of the U. S. Treasury Department. As a normal part of a safety and soundness examination, the OCC examiners will assess and comment on the adequacy of a national bank's allowance for loan losses. The allowance presented in this discussion is on an aggregated basis.



The nature of community banking is such that the loan portfolios will be predominantly comprised of small and medium size business and consumer loans. As community banks, there is a natural geographic concentration of loans within the Banks' respective cities or counties. Management at each bank monitors the loan concentrations and loan portfolio quality on an ongoing basis including, but not limited to: quarterly analysis of loan concentrations, monthly reporting of past dues, non-accruals, and watch loans, and quarterly reporting of loan charge-offs and recoveries. These efforts focus on historical experience and are bolstered by quarterly analysis of local and state economic conditions, which is part of the Banks' assessment of the adequacy of their allowances for loan losses.

Management reviews its allowance for loan losses in three broad categories: commercial, real estate and installment loans. However, management does not believe it would be useful to maintain a separate allowance for each category. Instead management assigns an estimated risk percentage factor to each category in the computation of the overall allowance. In general terms, the real estate loan portfolio is subject to the least risk, followed by the installment loan portfolio, which in turn is followed by the commercial portfolio. The Banks' internal and external loan review programs will from time to time identify loans that are subject to specific weaknesses and such loans will be reviewed for a specific loan loss allowance.

Based on the current levels of non-performing and other problem loans, management believes that loan charge-offs in 2001 will at least approximate the 2000 levels as such loans progress through the collection process. Management believes that the allowance for loan losses, as of September 30, 2001 is sufficient to absorb the expected charge-offs and provide adequately for the inherent losses that remain in the loan portfolio. Management will continue to closely monitor the levels of non-performing and potential problem loans and address the weaknesses in these credits to enhance the amount of ultimate collection or recovery of these assets. Management considers the levels and trends in non-performing and past due loans in determining how historical loan loss rates are adjusted.

The aggregate allowance for loan losses of the banks and the aggregate activity with respect to those allowances are summarized in the following table.

| (Dollars in thousands) | Nine months ended Sept. 30, 2001 | Y D |
|---|---|---|
| Allowance at beginning of period ................................. | $2,424 | |
| Provision expense ................................................ | 457 | |
| Net charge offs .................................................. | (120) | |
| Allowance at end of period ....................................... | $2,761 | |
| Allowance / outstanding loans .................................... | 1.26% | |

In reviewing the adequacy of the allowance for loan losses at the end of each period, management of each bank considers historical loan loss experience, current economic conditions, loans outstanding, trends in non-performing and delinquent loans, and the quality of collateral securing problem loans. After charging off all known losses, management of each bank considers the allowance adequate to provide for estimated losses inherent in the loan portfolio at September 30, 2001.



Deposits

Deposits were $233,791,000 at September 30, 2001 compared to $218,811,000 at December 31, 2000, an increase of 6.8% or $14,980,000.

Time deposits greater than $100,000 were $48,708,000 at September 30, 2001 compared to $38,702,000 at December 31, 2000, an increase of 25.9% or $10,006,000.

Liquidity

Liquidity is the ability to meet current and future obligations through liquidation or maturity of existing assets or the acquisition of additional liabilities. Adequate liquidity is necessary to meet the requirements of customers for loans and deposit withdrawals in a timely and economical manner. The most manageable sources of liquidity are composed of liabilities, with the primary focus of liquidity management being the ability to attract deposits within the Orangeburg National Bank, Sumter National Bank, and Florence National Bank service areas. Core deposits (total deposits less certificates of deposit of $100,000 or more) provide a relatively stable funding base. Certificates of deposit of $100,000 or more are generally more sensitive to changes in rates, so they must be monitored carefully. Asset liquidity is provided by several sources, including amounts due from banks, federal funds sold, and investments available for sale.

CBI and its banks maintain an available for sale and a held to maturity investment portfolio. While all these investment securities are purchased with the intent to be held to maturity, such securities are marketable and occasional sales may occur prior to maturity as part of the process of asset/liability and liquidity management. Such sales will generally be from the available for sale portfolio. Management deliberately maintains a short-term maturity schedule for its investments so that there is a continuing stream of maturing investments. CBI intends to maintain a short-term investment portfolio in order to continue to be able to supply liquidity to its loan portfolio and for customer withdrawals.

CBI has substantially more liabilities (mostly deposits, which may be withdrawn) which mature in the next 12 months than it has assets maturing in the same period. However, based on its historical experience, and that of similar financial institutions, CBI believes that it is unlikely that so many deposits would be withdrawn, without being replaced by other deposits, that CBI would be unable to meet its liquidity needs with the proceeds of maturing assets.

CBI through its banking subsidiaries also maintains federal funds lines of credit with correspondent banks, and is able to borrow from the Federal Home Loan Bank and from the Federal Reserve's discount window.

CBI through its banking subsidiaries has a demonstrated ability to attract deposits from its markets. Deposits have grown from $30 million in 1989 to over $233 million in 2001. This base of deposits is the major source of operating liquidity.

CBI's long term liquidity needs are expected to be primarily affected by the maturing of long-term certificates of deposit. At September 30, 2001 CBI had approximately $24.7 million and $11.5 million in certificates of deposit and other interest bearing liabilities maturing in one to five years and over five

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years, respectively. CBI's assets maturing or repricing in the same periods were $124.8 million and $26.1 million, respectively. CBI expects to be able to manage its current balance sheet structure without experiencing any material liquidity problems.

In the opinion of management, CBI's current and projected liquidity position is adequate.

Capital resources

As summarized in the table below, CBI maintains a strong capital position.

| | Sept. 30, 2001 | D |
|---|---|---|
| Tier 1 capital to average total assets ............................ | 8.89% | |
| Tier 1 capital to risk weighted assets ............................ | 11.77% | |
| Total capital to risk weighted assets .............................. | 12.95% | |

In the opinion of management, the Corporation's current and projected capital positions are adequate.

Dividends

CBI declared and paid a quarterly cash dividend of seven cents per share during the first three quarters of 2001, for a total of 21 cents per share. The total cost of these dividends was $672,000.

Subsequent event

On October 31, 2001, CBI completed its previously announced acquisition of Resource Mortgage, Inc., a mortgage company headquartered in Columbia, SC. Consideration for the acquisition was 95,454 shares of CBI common stock, of which 63,636 are being held in escrow pending the attainment of certain earnings goals by the subsidiary. The subsidiary, which was renamed Community Resource Mortgage, Inc., has 29 employees and has offices in Columbia, Sumter and Anderson, SC. The subsidiary originates and sells residential mortgage loans.

In connection with the acquisition, CBI has guaranteed a $9 million line of credit with an unaffiliated lender for the subsidiary's general working capital purposes.

Commitments

Sumter National Bank has entered into a contract to construct a new branch bank. This building is currently under construction near the corner of Liberty Street and Wedgefield Highway in Sumter. The contracted cost of the building is $567,681.



Item 3. Quantitative and Qualitative Disclosures about Market Risk

Market risk is the risk of loss from adverse changes in market prices and rates. The Corporation's market risk arises principally from interest rate risk inherent in its lending, deposit and borrowing activities. Management actively monitors and manages its interest rate risk exposure. Although the

Corporation manages other risks, such as credit quality and liquidity risk in the normal course of business, management considers interest rate risk to be its most significant market risk and this risk could potentially have the largest material effect on the Corporation's financial condition and results of operations. Other types of market risks such as foreign currency exchange risk and commodity price risk do not arise in the normal course of community banking activities.

Achieving consistent growth in net interest income is the primary goal of the Corporation's asset/liability function. The Corporation attempts to control the mix and maturities of assets and liabilities to achieve consistent growth in net interest income despite changes in market interest rates. The Corporation seeks to accomplish this goal while maintaining adequate liquidity and capital. The Corporation's asset/liability mix is sufficiently balanced so that the effect of interest rates moving in either direction is not expected to be significant over time.

The Corporation's Asset/Liability Committee uses a simulation model to assist in achieving consistent growth in net interest income while managing interest rate risk. The model takes into account interest rate changes as well as changes in the mix and volume of assets and liabilities. The model simulates the Corporation's balance sheet and income statement under several different rate scenarios. The model's inputs (such as interest rates and levels of loans and deposits) are updated on a quarterly basis in order to obtain the most accurate projection possible. The projection presents information over a twelve-month period. It reports a base case in which interest rates remain flat and reports variations that occur when rates increase and decrease 100 and 200 basis points. According to the model as of September 30, 2001 the Corporation is positioned so that net interest income would be expected to increase $242,000 and net income would be expected to increase $149,000 in the next twelve months if interest rates rise 100 basis points. Conversely, net interest income would be expected to decline $242,000 and net income would be expected to decline $149,000 in the next twelve months if interest rates decline 100 basis points. Computation of prospective effects of hypothetical interest rate changes are based on numerous assumptions, including relative levels of market interest rates and loan prepayment, and should not be relied upon as indicative of actual results. Further, the computations do not contemplate any actions the Corporation could undertake in response to changes in interest rates.

As of September 30, 2001 there was no significant change from the interest rate sensitivity analysis for the various changes in interest rates calculated as of December 31, 2000. The foregoing disclosures related to the market risk of the Corporation should be read in connection with Management's Discussion and Analysis of Financial Position and Results of Operations included in the 2000 Annual Report on Form 10-K.



Part II--Other Information

Item 2. Changes in Securities and Use of Proceeds

(c) On October 31, 2001, CBI issued 95,454 shares of its common stock as consideration for the purchase of 100% of the outstanding shares of Resource Mortgage, Inc. Of the total number of shares, 63,636 are being held in escrow pending the attainment of certain earnings goals by the subsidiary. Issuance of the shares by CBI was exempt from registration pursuant to Section 4(2) of the Securities Act of 1933 because no public offering was involved.

Item 6. Exhibits and Reports on Form 8-K

(a) Exhibits

| Exhibit No.(from item 601 of S-B) | Description |
|---|---|
| 10.1 | Loan Agreement, dated November 1, 2001, among Community Bankshares, Inc., Resource Mortgage Inc., and Branch Bank and Trust Company. |
| 10.2 | Guaranty, dated as of November 1, 2001 by Community Bankshares, Inc. of obligations of Resource Mortgage Inc. to Branch Bank and Trust Company. |

b) Reports on Form 8-K. None.



Signatures

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

DATED: November 12, 2001

COMMUNITY BANKSHARES, INC.

By: s/ E. J. Ayers, Jr.,

E. J. Ayers, Jr.,
Chief Executive Officer

By: s/ William W. Traynham

William W. Traynham
President and Chief Financial Officer
(Principal Accounting Officer)

EXHIBIT INDEX

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