

financial contents

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Analysis Of Earning Assets And Interest Bearing Liabilities

In Thousands of Dollars

ASSETS	2007			2006		
	Avg. Balance	Interest	Yield/Rate	Avg. Balance	Interest	Yield/Rate
Loans						
Commercial (1)	\$ 16,265	\$ 1,326	8.15%	\$ 13,414	\$ 1,112	8.29%
Real Estate	275,375	19,480	7.07%	249,582	17,585	7.05%
Installment (2)	11,932	968	8.11%	11,639	964	8.28%
Total Loans	<u>\$ 303,572</u>	<u>\$ 21,774</u>	<u>7.17%</u>	<u>\$ 274,635</u>	<u>\$ 19,661</u>	<u>7.16%</u>
Securities (3)						
Taxable	106,464	4,925	4.63%	118,116	5,349	4.53%
Tax-Exempt (4)	6,342	458	7.22%	5,850	421	7.20%
Total Securities	<u>\$ 112,806</u>	<u>\$ 5,383</u>	<u>4.77%</u>	<u>\$ 123,966</u>	<u>\$ 5,770</u>	<u>4.65%</u>
Federal Funds Sold	31,378	1,563	4.98%	35,436	1,741	4.91%
Total Earning Assets	<u>\$ 447,756</u>	<u>\$ 28,720</u>	<u>6.41%</u>	<u>\$ 434,037</u>	<u>\$ 27,172</u>	<u>6.26%</u>
Cash and Due from Banks	17,573			18,239		
Premises and Equipment, Net	1,003			933		
Other Assets	3,253			2,895		
Allowance for Loan Losses	(3,015)			(2,862)		
Total Assets	<u>\$ 466,570</u>			<u>\$ 453,242</u>		
LIABILITIES AND SHAREHOLDERS' EQUITY						
Interest Bearing Deposits						
Super NOW and MMDA	\$ 90,967	\$ 1,373	1.51%	\$ 100,723	\$ 1,455	1.44%
Savings	18,527	185	1.00%	19,659	196	1.00%
Time	247,497	12,257	4.95%	226,635	9,718	4.29%
Total Interest Bearing Deposits	<u>\$ 356,991</u>	<u>\$ 13,815</u>	<u>3.87%</u>	<u>\$ 347,017</u>	<u>\$ 11,369</u>	<u>3.28%</u>
Long-Term Borrowings	0	0	0%	0	0	0%
Total Interest Bearing Liabilities	<u>\$ 356,991</u>	<u>\$ 13,815</u>	<u>3.87%</u>	<u>\$ 347,017</u>	<u>\$ 11,369</u>	<u>3.28%</u>
Noninterest Bearing Deposits	43,844			44,360		
Accrued Expenses and Other Liabilities	2,498			1,950		
Equity	<u>63,237</u>			<u>59,915</u>		
Total Liabilities and Equity	<u>\$ 466,570</u>			<u>\$ 453,242</u>		
Net Interest Margin	\$ 447,756	\$ 14,905	3.33%	\$ 434,037	\$ 15,803	3.64%

(1) Includes loans on nonaccrual status.

(2) Net of unearned interest.

(3) Represents amortized value.

(4) Tax-exempt income converted to a fully tax-equivalent basis assuming a federal tax rate of 34% and a state tax rate of 8.75%.

Rate Sensitivity Analysis As Of December 31, 2007

In Thousands of Dollars

REPRICING INTERVAL	Three Months Or Less	Three To Twelve Months	One To Three Years	Three To Five Years	Five To Fifteen Years	Over Fifteen Years
ASSETS						
Total Loans (1)	\$ 56,373	\$ 16,238	\$ 42,441	\$ 46,279	\$ 78,456	\$ 71,718
Investment Securities (2)	30,879	32,904	31,367	6,301	2,616	3,027
Federal Funds Sold	<u>35,000</u>	<u>0</u>	<u>0</u>	<u>0</u>	<u>0</u>	<u>0</u>
Total Selected Assets	\$ 122,252	\$ 49,142	\$ 73,808	\$ 52,580	\$ 81,072	\$ 74,205
LIABILITIES						
Interest Bearing Deposits (3)	\$ 160,581	\$ 72,660	\$ 26,305	\$ 100	\$ 0	\$ 0
Borrowed Funds	<u>0</u>	<u>0</u>	<u>0</u>	<u>0</u>	<u>0</u>	<u>0</u>
Total Selected Liabilities	\$ 160,581	\$ 72,660	\$ 26,305	\$ 100	\$ 0	\$ 0
Differences	<u>(38,329)</u>	<u>(23,518)</u>	<u>47,503</u>	<u>52,480</u>	<u>81,072</u>	<u>74,205</u>
Cumulative Differences	<u>\$ (38,329)</u>	<u>\$ (61,847)</u>	<u>\$ (14,344)</u>	<u>\$ 38,136</u>	<u>\$ 119,208</u>	<u>\$ 193,413</u>

(1) Does not include loans on nonaccrual status.

(2) Does not include Federal Reserve Stock or securities on nonaccrual status. Reported HTM securities at amortized cost and AFS securities at fair value.

(3) Does not include Super NOW, Money Market Deposit Accounts or traditional savings deposits.

Management's Discussion and Analysis Of Financial Condition And Results Of Operation

Summary

Putnam Bancshares, Inc., and its wholly owned subsidiary, Putnam County Bank, exhibited favorable growth in various financial indicators in 2007.

The year was consumed by a great deal of stress on the national economy as brought about by the subprime mortgage debacle. This has caused the meltdown of many mortgage loan companies as liquidity in the market for purchases of mortgages has been dramatically changed. Many mortgages originated and sold in the secondary markets were of poor credit quality and some were caused by fraudulent broker and underwriting practices. These mortgages were the source of significant income to those institutions and were the reason why they pushed to originate these loans. One year ago, this crisis was not a major concern...it is now. Washington lawmakers and policymakers are working hard to find an answer, however the breadth of the problem is massive.

The direct effect of this crisis was averted by many community banks. Credit underwriting standards of federally- and state-chartered banks come under considerable scrutiny for the types of loan products offered and, as a result, were not largely responsible in the origination of such credits. Nonetheless, the impact of greater stress brought about by the mortgage crisis in the economy, combined with rising energy prices has impacted major industries and suppliers of consumer goods.

In addition, Federal Reserve policymakers have been working hard to balance an economy which is slowing. Challenges will be to manage an economy which is stressed by rising energy prices and the continuing costs of maintaining the current military presence in the Middle East. With the candidates of the Presidential primaries suggesting answers for the nation's economic concerns, there are many questions about their knowledge of economic policy.

Statewide, West Virginia has not felt the severe effects of the national mortgage crisis in an overall respect. States which have seen wide variances in real estate values and have experienced significant changes in employment have felt great pain. West Virginia continues to promote "clean coal" technologies as a way of promoting the industry. Continued improvements in the local system of highways are a priority and are necessary to advance the state's economic standing.

Locally, the development of U. S. Route 35 is continuing with portions slated for completion in late-2008.

West Virginia averaged 4.6% unemployment during 2007 dropping from 5.1% in January to 4.1% in November, ending at 4.5% in December. While West Virginia ranks level with the nation in unemployment statistics, Putnam is lower. The average unemployment for Putnam County was 3.7% in 2007.

The following description of the operating income and financial condition of Putnam Bancshares, Inc. (referred throughout as "the Company") should be read in conjunction with the Consolidated Balance Sheets, Statements of Income, Changes in Shareholders' Equity, Statements of Cash Flows, and Notes to Consolidated Financial Statements (beginning on page F- 1 and ending on page F- 28). References also will be made to Putnam Bancshares' wholly-owned subsidiary, Putnam County Bank ("the Bank"). In addition, various graphs, charts and analyses have been provided throughout the Annual Report to supplement management's analysis.

The Federal Financial Institutions Examination Council (FFIEC) is a governmental organization comprised of the Board of Governors Federal Reserve System, Federal Deposit Insurance Corporation and the Office of the Comptroller of the Currency. The federal regulatory bodies collect financial data from commercial banks through their quarterly Call Reports and Summary of Deposits reports. The compilation of this data and resulting statistical analysis is culminated in a Uniform Bank Performance Report ("UBPR") which also designates a national "peer group" based upon asset size and number of branches. The Bank's "peer group" consists of all commercial banks having assets between \$300 million and \$1 billion. As of December 31, 2007 there were 1,172 banks in the same group as the Bank. Of the banks in this group, three are based in West Virginia. When analyzing peer group statistics, it is necessary to view each bank's economic environment and operating philosophy as well as other available information (such as their Annual Reports) which may indicate how their statistical information compares to peers. Uniform Bank Performance Reports may be obtained on any financial institution regulated its member regulatory bodies by accessing www.ffiec.gov.

Net Interest Margin

The compression of net interest margins was a common theme in banking circles in 2007. Competitive pressures continued to

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fuel the need to pay loan and deposit rates to maintain their market share. Aggressive competition among banks, credit unions, mortgage companies, brokerages and insurance companies give the consumers a wide array of options. The net interest margin is the difference between the tax equivalent interest income and interest expense divided by the average earning assets and is a primary way to gauge profitability. The Company's net interest margin declined from 3.64% in 2006 to 3.33% in 2007. The peer's net interest margin was 4.21% in 2006 and 4.02% in 2007. The reason for this decline was higher rates paid on deposit accounts combined with paying market rates for loans. The Company's cost of funds was 3.28% in 2006 compared with 3.87% in 2007. The cost of funds is calculated by dividing the interest expense by the annual average of total deposits. The peer group's cost of funds was 3.27% in 2006 and 3.76% in 2007. The yield on earning assets was 6.41% in 2007 and 6.26% in 2006. Total loan yields remained relatively unchanged, however compared with peers, they declined slightly. The yield on investment securities increased slightly in 2007 from 4.65% to 4.77%.

Interest Income

Interest income increased \$1.5 million or 6% from year-end 2006 to year-end 2007. The Federal Open Market Committee (FOMC) lowered the target fed funds rate beginning in September a total of 100 basis points over the remainder of 2007. This was in contrast to a 100 basis point increase in the target in 2006. Concerns over financial markets, tighter credit and uncertainty in the economy led the Committee to these actions. The Bank had 17% of its loan portfolio indexed to the Wall Street Journal prime rate as of year-end 2007. The average total loans increased \$28.9 million or 11% from year-end 2006 to year-end 2007. This compares with a \$30.3 million or 12% increase during the prior year. This continued increase reflects dedicated efforts of the lending group to provide credit in an efficient manner with a focus on customer needs. Continued growth does not reflect a weakening of credit standards to generate income. Total income from loans increased \$2.1 million or 11% at year-end 2007, compared with a \$2.6 million increase at year-end 2006. The Company's average earning assets increased \$13.7 or 3% from year-end 2006 to year-end 2007. The income on average earning assets increased \$1.5 million or 6% from year-end 2006 to year-end 2007. This contrasts with a \$3.1 million or 13% increase for the period between year-end 2005 and year-end 2006. Declining market rates during the second half of 2007

combined with a higher cost of funds dampened income growth.

Interest income on real estate loans contributed the greatest increase in loan income growing \$1.9 million or 11% in 2007 compared with \$2.3 million or 15% in 2006. Real estate lending continues to be a very viable business in our market. The Bank considers such lending to be very competitive so efficient turnaround and closing is an important piece that is marketed. In addition, the Bank does not book their loans with the intent to sell them in the secondary market.

Income on commercial lending grew \$214 thousand or 19% in 2007, compared with \$314 thousand or 39% in 2006. Average total commercial loans increased \$2.8 million or 21% in 2007 compared with \$2.6 million or 24% in 2006. A consistent growth in commercial lending is evident; however lower rates in 2007 account for a reduction in income.

Income on consumer lending grew \$4 thousand in 2007 compared with an \$8 thousand increase in 2006. The average total of consumer loans in 2007 increased \$293 thousand or 3%. In 2006, the average total increased \$88 thousand. While there remains to be a highly competitive market for consumer lending, such as automobile loans, the Bank has been successful in cultivating customer relationships to grow this segment of lending.

Income on investments (on a tax effective basis) declined \$387 thousand or 7% from year-end 2006 to year-end 2007. In addition, average total investments declined \$11 million or 9% in the same period. This is in contrast to 2006 showing an increase in investment income of \$473 thousand or 9%. Also during this period, average total investments declined \$16 million or 11%. The decline in income was related to a shift in funding from investments to loans. The Company's tax equivalent yield on investments rose slightly between 2006 and 2007. Nonetheless, the Bank's yield continues to be lower than peer institutions because of the composition of the portfolio. The portfolio continues to be highly composed of U. S. Treasury and U. S. Federal Agency securities. This is a strategy which has not changed since 2006. The Bank also continues to invest in three- and six-month Treasury Bills in the Treasury's weekly auction. The income on Federal Funds Sold at year-end 2007 declined \$178 thousand or 10% with average total balances declining \$4 million or 11%. As in the case with investments, this decline funded increases in

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lending. The yield on Federal Funds Sold remained relatively steady between the years of 2006 and 2007. While the percentage of funds sold to average assets remains high in comparison to peers, the volume of such funds has declined in the past four years. Federal funds represent excess liquidity which the Bank is able to sell to correspondent banks at an interest rate which is subject to daily change. At year-end 2007, all municipals are West Virginia securities. In 2007, The Bank invested in two municipal securities issues of the Putnam County Building Commission which total \$1.6 million. These are revenue securities to fund the refinance and improvements to Teays Valley Manor, a home for low-income senior citizens and those with disabilities in Scott Depot. While these revenue securities are non-rated, they still meet the Bank's tests for creditworthiness. In addition, the investment in this project represents an opportunity for the Bank to address community needs, as mandated in the federal Community Reinvestment Act of 1977. The remainder of the Bank's municipal securities (\$5.6 million) are investment grade and are rated A or better by Moody's and/or Standard and Poor's ratings services. Of the municipal securities portfolio, 15% are general obligations with the remainder being revenue obligations.

Interest Expense

Interest expense on deposits increased \$2.4 million or 21% from year-end 2006 to 2007. This compares with an increase of \$3.7 million or 48% in the previous year. The yield on total deposits was 3.87% for 2007 representing an increase of 59 basis points from 2006. For our peer group, the yield is 3.76% for 2007 representing an increase of 49 basis points. In both cases, the yield in 2007 and 2006 compares closely to the median of the peer group. However, with respect to large time deposits (over \$100,000) the Bank's yield has moved to the 79th percentile of the peer group in 2007 compared with the 69th percentile in 2006. The average total of deposits increased \$10 million or 3% in the current year compared to \$8 million or 2% in the previous year. The competitive pricing of deposits during the year has resulted in net interest margin compression in many financial institutions nationwide. Management has made adjustments in an effort to better control deposit pricing mechanisms in an effort to prevent further declines in the margin. Nonetheless, the Bank has historically paid higher rates to depositors. The Bank does not actively solicit deposits from outside its market area and does not solicit brokered deposits.

Asset and Liability Management (Interest Rate Sensitivity and Liquidity)

Putnam County Bank's Asset/Liability Committee (ALCO) meets on a quarterly basis and is comprised of four outside directors and members of senior management. Reports are presented depicting historical and projected findings concerning profitability and risk, such as market risk, credit risk and liquidity risk. The experience and views of outside directors bring a perspective of how the customer may view pricing strategies. In addition, an officers' ALCO meets on a monthly basis to analyze similar data and discussions are forwarded to the board's ALCO. Some of the items on the agenda for discussion include projected loan and deposit growth or decline, the impact of rate changes, liquidity maintenance and trends in the economy and competition.

In an effort to monitor interest rate sensitivity, management must gauge interest rate risk and its effects upon financial statements. The variables include the maturities of instruments, repricing characteristics and the "imprecise" effects of prepayments on loans and withdrawals on deposits. The Rate Sensitivity Report (See page F2) provides for the maturity of instruments and takes into consideration the repricing characteristics, but not possible repayment or withdrawal scenarios. Assumptions related to changes in interest rates will affect prepayments and withdrawals and are discussed in the ALCO meetings.

While there exists several sources of liquidity, growth in lending during 2007 reduced liquidity through declines in investments and Federal Funds sold. The Bank's loan-to-deposit ratio continued to increase to 76.04% in 2007 from 72.82% in 2006. The peer group ratio was 89.46% in 2007 and 86.83% in 2006. Federal Funds sold and short-term investments remain the primary areas for liquidity. The Bank continues to be comparatively conservative with regards to investments as it invests in U. S. Treasury and Government Agency securities and "in state" municipal securities.

Another measure of liquidity is the Bank's net non-core funding dependence ratio. This measures how much of the Bank's long-term assets are funded with non-core funding. Non-core funding is characterized as time deposits in excess of \$100,000 which are considered to be more sensitive to rate changes than other deposits. As of year-end 2007, the ratio was 14.28% compared with 15.17% at year-end 2006. This

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is well below the peer group ratios of 25.72% and 24.46%, respectively.

Nonperforming Assets

Nonperforming assets include all loans which are past due ninety days or more and any loans in nonaccrual status. Loans are required to be reported in nonaccrual status when principal and interest are in default for ninety days or more, unless the loan is well secured and in process of collection. Loans are in nonaccrual status due to loss of the primary source of repayment and all payments are reflected on a cash basis. The total of nonperforming loans at the end of 2007 was \$3 million or .97% of total loans compared with \$2 million or .68% at year-end 2006. This compares with peer ratios of .103% and .55% respectively. The increase in nonperforming was related to a local real estate developer whose loans exceeded ninety days past due. These loans are well secured and in process of collection. The existing \$2 million represents exposure to a local businessperson who is in bankruptcy where the Bank expects to recover full value in 2008.

The Bank had a balance of \$90 thousand in other real estate owned at year-end 2007 compared with none in 2006.

Provision and Allowance for Loan Losses

The Bank made total provisions to the allowance for loan losses totaling \$1.1 million in 2007 compared to \$150 thousand in 2006. The increased provisions in 2007 were related to a credit to a local museum. Loan loss recoveries in 2007 totaled \$352 thousand compared with \$550 thousand in 2006. Gross loan losses increased from \$670 thousand in 2006 to \$801 thousand in 2007. The majority of this loss was related to the credit to the local museum, which was recognized as loss in its entirety.

Net loan losses were \$449 thousand in 2007 and \$120 thousand in 2006. Higher net losses were due to increased losses combined with lower recoveries. While net losses were higher, the Bank's ratio of net loss to average total loans was .15% compared to .18% for the peer group. In addition, the volume of recoveries has made the ratio of recoveries to total loans compare significantly higher than peer (.12% compared to .04%). As of year-end 2007, the allowance for loan loss was \$3.4 million or 1.09% of total loans compared to \$2.7 million or .94% of total loans at year-end 2006. The

peer ratios of allowance to total loans were 1.20% in 2007 and 1.20% in 2006. While the Bank's ratios are lower than peer, the allowance level is reflective of many factors which include underwriting practices, local economic conditions and quality of collateral evaluations. While many factors must be assessed in determining the adequacy of the allowance, each institution's evaluation is specialized to its own unique characteristics. Along with a well-qualified loan staff, the Bank also has a Loan Committee composed of outside Directors meeting with senior officers to discuss topics involving the loan portfolio on a monthly basis. The adequacy of the allowance is subject to review by the Company's internal auditors, external auditors, Federal Reserve Bank and the West Virginia Division of Banking.

Noninterest Income

Total noninterest income (excluding gross securities gains) totaled \$326 thousand representing an increase of \$39 thousand or 14% in 2007 over 2006. Noninterest income grew \$10 thousand or 4% between 2006 and 2005. The most significant increase was in VISA debit card income as a result of our customers' increased usage of the Bank's VISA debit cards. Other sources of noninterest income remained relatively unchanged.

The Bank continues to be a low-cost provider of banking services. In 2007, the percentage of noninterest income to average assets for the Bank is .07% compared to the peer ratio of .82%. In 2006, the Bank's ratio was .06% with the peer ratio being .83%.

Noninterest Expense

Total noninterest expense (excluding gross securities losses) increased \$39 thousand or less than one percent from year-end 2006 to year-end 2007 compared with an increase of \$604 thousand or 9% between years ending 2006 and 2005. Noninterest expenses are composed of expenses relating to personnel, occupancy and other operating.

Total personnel expenses increased \$367 thousand or 8% in 2007 compared with \$495 thousand or a 13% increase in 2006. Officer and employee salary expense increased \$108 thousand or 3% in 2007 compared with a \$402 thousand increase or 13% in 2006. Salary increases typically represent increases for existing Bank personnel. Staffing levels for the Bank were 79 in 2007 and 75 in 2006. Employee group health

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and life insurance increased \$59 thousand or 13% in 2007 and is commensurate with medical inflation rates nationwide. This compares with an increase of \$67 thousand or 17% in 2006. Management has been working to provide cost-effective insurance programs which still provide good service to our employees. The most significant personnel expense increase was found in employee retirement funding. This expense increased from \$242 thousand in 2006 to \$439 thousand in 2007. The Bank's retirement plan is administered by the West Virginia Bankers Association as a noncontributory pension plan with independent actuaries making the determination of contributions made by its members. Management is actively seeking alternatives to their existing plan.

Total occupancy expense includes the costs to maintain the Bank's premises and equipment. These expenses increased a modest \$14 thousand or 3% in 2007 compared with a decrease of \$24 thousand or 5% in 2006. The Bank continues to operate facilities at 2761 Main Street, 300 Hurricane Creek Road and 3058 Mount Vernon Road.

Total other operating expense declined from \$2.7 million in 2006 to \$2.4 million in 2007. A significant decline in expense was related to a rebate of FDIC insurance premiums to the Bank in the amount of \$444 thousand as a result of deposit insurance reforms due to excess amounts in the deposit insurance fund. At the end of 2007, the Bank had a remaining credit of \$297 thousand. Future FDIC premiums will expense against this credit. Additional decreases were noted in postage and telephone expenses. Savings in the amount of \$53 thousand in postage were recognized as a result of image statements, termination of mailing notices of electronic credits and electronic delivery of statements. Savings of \$32 thousand in telephone expense were a result of the efforts of the accounting department in finding waste and unnecessary duplication in fees assessed to the Bank. These savings were offset by increases in fees paid to accountants and state business franchise taxes. Fees assessed by accountants rose by \$21 thousand due to increased complexity and regulatory requirements related to banking. The increase in business franchise taxes relate to a prepayment of nearly \$45 thousand which will be applied to future liability. As such, these taxes declined by \$17 thousand in 2007.

The Company reported a net gain of \$8 thousand on the sale of securities held as available for sale in 2007 compared to a net loss of \$167 thousand in 2006. Gains and losses are derived from the sale of securities classified as "available for

sale" which are reflected on the financial statements at the fair market value and may be sold at any time at the discretion of management. Management considers several factors before making a decision to sell such as changing interest rates, liquidity, availability and alternative investments with the projected change on the Bank's asset/liability structure. All sales are carefully evaluated by management and reviewed by the Board. All of the Company's investment in U. S. Treasury Bills is classified as "held to maturity" and the remainder of the portfolio is classified as "available for sale". The Company does not speculate by "trading" in the portfolio and does not utilize any interest rate hedging or derivative products in its investment strategies.

Taxes

The Company's federal and state tax provision decreased from \$2.8 million in 2006 to \$2.2 million in 2007. The decrease was due to lower taxable income and higher deferred tax benefit in 2007. The deferred benefit was nearly \$300 thousand higher in 2007 compared with 2006.

The Bank invests in municipal securities issued in West Virginia which are "bank qualified" and are exempt from federal and state taxation.

Equity and Capital Ratios

Putnam Bancshares' equity increased \$3.7 million or 6% in 2007 to \$65 million. The change in equity during 2007 was reflective of \$4.0 million in net income less \$1.2 million in dividends and an increase of \$830 thousand in comprehensive income. The book value per outstanding share rose from \$102.31 in 2006 to \$108.43 in 2007. The Company's return on average equity was 6.39% in 2007.

Banking regulatory bodies mandate the risk-weighting of assets and off-balance sheet items to more accurately assess capital adequacy. Tier 1 capital (equity capital less the tax equivalent of unrealized gains or losses on available for sale securities) and total risk-based capital (Tier 1 capital plus the allowable portion of the allowance for loan losses) comprise two vital measures of capital adequacy. As of year-end 2007, the Bank's Tier 1 risk-based capital-to-total risk-weighted assets was 22.98% compared to 23.89% in 2006. The peer bank ratios were 11.63% and 11.75% in 2007 and 2006 respectively. As of year-end 2007, the Bank's total risk-based capital-to-total risk-weighted assets were 24.19% compared

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to 24.95% in 2006. The peer bank ratios were 12.74% and 12.90% in 2007 and 2006 respectively. Both measures rank the Bank in the 97th percentile in comparison with peers. Using the federal guidelines for capital adequacy, these ratios suggest the Bank is well capitalized.

Dividends

The Company paid dividends of \$1.2 million in 2007 compared with \$1.0 million in 2006, reflective of a 20% increase. This equates to a dividend payout (dividends to net income) ratio of 30%. The peer ratio for 2007 was 49%. This conservative dividend payment strategy has produced a stronger equity base for the Company. Regular dividends were paid in June and December of 2007.

For a further discussion of dividends, please refer to "Note 13 – Regulatory Matters" and the Consolidated Statements of Changes in Shareholders' Equity in the Consolidated Financial Statements.

Statement of Management Responsibility

The financial statements, related financial data and other information found in this report are the responsibility of the management of Putnam Bancshares, Inc. and its sole subsidiary, Putnam County Bank. The financial statements have been prepared in conformance with generally accepted accounting principles appropriate for the circumstances to mirror, in all material respects, reportable events and transactions.

The accounting systems of Putnam Bancshares, Inc. and its wholly-owned subsidiary, Putnam County Bank, record, summarize and report financial data. The Bank uses internal controls and procedures to provide reasonable assurance (the cost involved should not exceed related benefits) to the reliability of the financial records. Reliance on the accounting system and internal controls by management is enhanced with written policies, internal audits and continuous training of accounting personnel in order to present fair and accurate statements.

The Audit Committee of Putnam County Bank, composed solely of outside directors, meets on a monthly basis to review various issues relating to audit, including coverage, findings and responses. The selection of Rollins, Cleavenger and Rollins as the Company's external auditors is recommended by the Board of Directors and ratified by the shareholders of Putnam Bancshares, Inc.

Independent Auditors' Report

To the Board of Directors and Shareholders
Putnam Bancshares, Inc. and Subsidiary
Hurricane, West Virginia

We have audited the accompanying consolidated balance sheets of Putnam Bancshares, Inc. and Subsidiary (a West Virginia corporation) as of December 31, 2007 and 2006, and the related consolidated statements of income, changes in shareholders' equity, and cash flows for the three years in the period ended December 31, 2007. These consolidated financial statements are the responsibility of the Bank's management. Our responsibility is to express an opinion on these consolidated 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 audits to obtain reasonable assurance about whether the consolidated financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the consolidated 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 Putnam Bancshares, Inc. and Subsidiary as of December 31, 2007 and 2006, and the results of its operations and its cash flows for the three years in the period ended December 31, 2007, in conformity with accounting principles generally accepted in the United States of America.



Certified Public Accountants

January 31, 2008

Consolidated Balance Sheets

DECEMBER 31, 2007 AND 2006

	<u>2007</u>	<u>2006</u>
ASSETS:		
Cash and Due from Banks	\$ 18,500,610	\$ 17,814,524
Federal Funds Sold	35,000,000	25,000,000
Available for Sale Securities	68,390,099	85,181,793
Held to Maturity Securities	38,703,017	38,598,917
Loans - Less Allowance for Credit Losses of \$3,401,326 and \$ 2,730,387, Respectively	309,509,071	287,261,802
Bank Premises and Equipment	1,101,244	904,555
Federal Reserve Bank Stock, at Cost	39,000	39,000
Other Assets	3,332,152	3,069,911
Total Assets	<u>\$ 474,575,193</u>	<u>\$ 457,870,502</u>
LIABILITIES AND SHAREHOLDERS' EQUITY		
LIABILITIES:		
Deposits:		
Noninterest Bearing	\$ 42,492,034	\$ 44,595,491
Interest Bearing	364,545,855	349,890,455
Total Deposits	<u>\$ 407,037,889</u>	<u>\$ 394,485,946</u>
Other Liabilities	2,480,437	1,997,621
Total Liabilities	<u>\$ 409,518,326</u>	<u>\$ 396,483,567</u>
Commitments and Contingent Liabilities (Note 11)		
SHAREHOLDERS' EQUITY:		
Common Stock, \$.50 Par Value, 1,200,000 Shares Authorized, 600,000 Shares Issued and Outstanding	\$ 300,000	\$ 300,000
Surplus	1,000,000	1,000,000
Retained Earnings	63,173,414	60,334,380
Accumulated Other Comprehensive Income	583,453	(247,445)
Total Shareholders' Equity	<u>\$ 65,056,867</u>	<u>\$ 61,386,935</u>
Total Liabilities and Shareholders' Equity	<u>\$ 474,575,193</u>	<u>\$ 457,870,502</u>

Consolidated Statements Of Income

FOR YEARS ENDED DECEMBER 31, 2007, 2006 AND 2005

	<u>2007</u>	<u>2006</u>	<u>2005</u>
INTEREST INCOME:			
Interest and Fees on Loans	\$ 21,773,955	\$ 19,660,919	\$ 17,086,628
Interest on Available for Sale Securities	3,354,525	3,791,469	3,991,334
Interest on Held to Maturity Securities	1,861,295	1,812,443	1,160,325
Interest Income on Federal Funds Sold	<u>1,562,719</u>	<u>1,741,299</u>	<u>1,679,516</u>
Total Interest Income	<u>\$ 28,552,494</u>	<u>\$ 27,006,130</u>	<u>\$ 23,917,803</u>
INTEREST EXPENSE:			
Interest on Deposits	<u>\$ 13,815,003</u>	<u>\$ 11,368,845</u>	<u>\$ 7,695,093</u>
Net Interest Income	<u>\$ 14,737,491</u>	<u>\$ 15,637,285</u>	<u>\$ 16,222,710</u>
Provision for Possible Loan Losses	<u>1,120,335</u>	<u>150,000</u>	<u>(1,388,519)</u>
Net Interest Income after Provision for Possible Credit Losses	<u>\$ 13,617,156</u>	<u>\$ 15,487,285</u>	<u>\$ 17,611,229</u>
OTHER INCOME:			
Service Charges and Commissions	<u>\$ 307,505</u>	<u>\$ 270,891</u>	<u>\$ 262,370</u>
Realized Gains on Sales of Available for Sale Securities	<u>79,801</u>	<u>-0-</u>	<u>289,506</u>
Other Operating Income	<u>18,069</u>	<u>15,702</u>	<u>13,614</u>
Total Other Income	<u>\$ 405,375</u>	<u>\$ 286,593</u>	<u>\$ 565,490</u>
OTHER EXPENSES:			
Salaries and Employee Benefits	<u>\$ 4,776,402</u>	<u>\$ 4,409,210</u>	<u>\$ 3,911,762</u>
Expenses of Premises and Equipment	<u>523,175</u>	<u>509,296</u>	<u>533,864</u>
Realized Losses on Sales of Available for Sale Securities	<u>72,224</u>	<u>167,416</u>	<u>990,188</u>
Other Operating Expenses	<u>2,378,989</u>	<u>2,721,323</u>	<u>2,589,736</u>
Total Other Expenses	<u>\$ 7,750,790</u>	<u>\$ 7,807,245</u>	<u>\$ 8,025,550</u>
Income before Income Taxes	<u>\$ 6,271,741</u>	<u>\$ 7,966,633</u>	<u>\$ 10,151,169</u>
Provision for Income Taxes	<u>2,232,707</u>	<u>2,848,880</u>	<u>3,656,943</u>
Net Income	<u>\$ 4,039,034</u>	<u>\$ 5,117,753</u>	<u>\$ 6,494,226</u>

The accompanying notes are an integral part of these consolidated financial statements.

Consolidated Statements Of Changes In Shareholders' Equity

FOR YEARS ENDED DECEMBER 31, 2007, 2006 AND 2005

	Common Stock	Surplus	Retained Earnings	Accumulated Other Comprehensive Income	Total Shareholders' Equity
BALANCES – JANUARY 1, 2005	\$ 300,000	\$ 1,000,000	\$50,642,401	\$ 950,692	\$ 52,893,093
COMPREHENSIVE INCOME					
Net Income			6,494,226		6,494,226
Other Comprehensive Income - Net of Tax:					
Change in Unrealized Gain (Loss) on Securities Available for Sale, Net of Deferred Income Tax (Benefit) of (\$937,285)				(1,620,807)	(1,620,807)
Add: Reclassification Adjustment, Net of Income Tax Benefits of \$256,730				443,952	443,952
Total Comprehensive Income					<u>5,317,371</u>
Cash Dividends (\$1.50 Per Share)			(900,000)		(900,000)
BALANCES – DECEMBER 31, 2005	\$ 300,000	\$ 1,000,000	\$56,236,627	\$ (226,163)	\$ 57,310,464
COMPREHENSIVE INCOME					
Net Income			5,117,753		5,117,753
Other Comprehensive Income - Net of Tax:					
Change in Unrealized Gain (Loss) on Securities Available for Sale, Net of Deferred Income Tax (Benefit) of (\$73,648)				(127,357)	(127,357)
Add: Reclassification Adjustment, Net of Income Tax Benefits of \$61,341				106,075	106,075
Total Comprehensive Income					<u>5,096,471</u>
Cash Dividends (\$1.70 Per Share)			(1,020,000)		(1,020,000)
BALANCES – DECEMBER 31, 2006	\$ 300,000	\$ 1,000,000	\$60,334,380	\$ (247,445)	\$ 61,386,935
COMPREHENSIVE INCOME					
Net Income			4,039,034		4,039,034
Other Comprehensive Income - Net of Tax:					
Change in Unrealized Gain (Loss) on Securities Available for Sale, Net of Deferred Income Tax of \$483,270				835,700	835,700
Less: Reclassification Adjustment, Net of Income Tax of (\$2,776)				(4,802)	(4,802)
Total Comprehensive Income					<u>4,869,932</u>
Cash Dividends (\$2.00 Per Share)			(1,200,000)		(1,200,000)
BALANCES – DECEMBER 31, 2007	<u>\$ 300,000</u>	<u>\$ 1,000,000</u>	<u>\$63,173,414</u>	<u>\$ 583,453</u>	<u>\$ 65,056,867</u>

The accompanying notes are an integral part of these consolidated financial statements.

Consolidated Statements Of Income

FOR YEARS ENDED DECEMBER 31, 2007, 2006 AND 2005

	<u>2007</u>	<u>2006</u>	<u>2005</u>
CASH FLOWS FROM OPERATING ACTIVITIES:			
Net Income	\$ 4,039,034	\$ 5,117,753	\$ 6,494,226
Adjustments to Reconcile Net Income to Net Cash Provided by Operating Activities:			
Depreciation	202,175	181,150	188,532
Provision for Credit Losses	1,120,334	150,000	(1,388,518)
Provision for Deferred Taxes	(352,928)	(54,950)	508,775
Net (Gain) Loss on Sale of Fixed Assets	-0-	-0-	5,476
Net Realized (Gains) Losses on Available for Sale Securities	(7,576)	167,416	700,682
Increase in Cash Value - Life Insurance	(9,870)	(10,013)	(12,673)
Amortization of Premiums and (Accretion) of Discounts on Available for Sale Securities - Net	5,189	7,566	425,416
(Increase) Decrease in Interest Receivable	2,582	47,015	(42,598)
(Increase) Decrease in Prepaid Expense	(289,657)	235,454	(283,501)
(Increase) Decrease in Other Assets	(2,862)	-0-	18,210
Increase (Decrease) in Accrued Interest	345,190	629,100	273,317
Increase (Decrease) in Other Liabilities	137,625	128,284	(31,891)
Net Cash Provided by Operating Activities	<u>\$ 5,189,236</u>	<u>\$ 6,598,775</u>	<u>\$ 6,855,453</u>
CASH FLOWS FROM INVESTING ACTIVITIES:			
(Increase) Decrease in Federal Funds Sold	\$ (10,000,000)	\$ 26,000,000	\$ 21,000,000
Proceeds from Sales and Maturities of Available for Sale Securities	24,903,125	15,389,063	74,746,879
Proceeds from Maturities of Held to Maturity Securities	102,138,706	102,187,557	102,839,675
Proceeds from Sales of Other Real Estate	-0-	-0-	94,941
Purchases of Available for Sale Securities	(6,797,650)	(19,617,509)	(60,984,395)
Purchase of Held to Maturity Securities	(102,242,805)	(102,115,822)	(102,690,653)
Purchase of Bank Premises and Equipment	(398,864)	(124,914)	(152,639)
Net (Increase) Decrease in Loans	(23,457,603)	(26,668,541)	(29,540,582)
Net Cash Provided by (Used in) Investing Activities	<u>\$ (15,855,091)</u>	<u>\$ (4,950,166)</u>	<u>\$ 5,313,226</u>

The accompanying notes are an integral part of these consolidated financial statements.

Consolidated Statements Of Cash Flows

FOR YEARS ENDED DECEMBER 31, 2007, 2006 AND 2005 (continued)

	<u>2007</u>	<u>2006</u>	<u>2005</u>
CASH FLOWS FROM FINANCING ACTIVITIES:			
Net Increase (Decrease) in			
Demand and Savings Deposits	\$ (10,207,995)	\$ (18,968,347)	\$ (7,152,540)
Increase (Decrease) in			
Certificates of Deposit	22,759,936	14,719,262	(6,755,786)
Dividends Paid	<u>(1,200,000)</u>	<u>(1,020,000)</u>	<u>(900,000)</u>
Net Cash Provided by (Used in)			
Financing Activities	<u>\$ 11,351,941</u>	<u>\$ (5,269,085)</u>	<u>\$ (14,808,326)</u>
Net Increase (Decrease) in Cash			
and Cash Equivalents	\$ 686,086	\$ (3,620,476)	\$ (2,639,647)
Cash and Cash Equivalents			
at Beginning of Year	<u>17,814,524</u>	<u>21,435,000</u>	<u>24,074,647</u>
Cash and Cash Equivalents			
at End of Year	<u>\$ 18,500,610</u>	<u>\$ 17,814,524</u>	<u>\$ 21,435,000</u>
SUPPLEMENTAL DISCLOSURES OF CASH FLOW INFORMATION:			
Cash Paid During the Year for:			
Interest	<u>\$ 13,469,813</u>	<u>\$ 10,739,745</u>	<u>\$ 7,421,775</u>
Income Taxes	<u>\$ 2,357,000</u>	<u>\$ 2,730,000</u>	<u>\$ 3,447,000</u>
SUPPLEMENTAL SCHEDULE OF SIGNIFICANT NONCASH ACTIVITIES:			
Transfer from Loans to Other			
Real Estate Owned	<u>\$ 90,000</u>	<u>\$ -0-</u>	<u>\$ -0-</u>

Notes To Consolidated Financial Statements For Years Ended December 31, 2007, 2006 And 2005

Note 1

Summary of Significant Accounting Policies:

The accounting and reporting policies of Putnam Bancshares, Inc. and its wholly-owned subsidiary conform to generally accepted accounting principles and general practices within the banking industry. Following is a summary of the more significant accounting policies:

Nature of Operations

Putnam County Bank operates under a state bank charter and provides full banking services, with the exception of trust services. As a state bank, the Bank is subject to regulation of the West Virginia Division of Banking, the Federal Reserve System, and the Federal Deposit Insurance Corporation. The area served by Putnam County Bank is Putnam County and its neighboring counties with services provided by the main office and two branch offices.

Principles of Consolidation

The consolidated statements include the accounts of Putnam Bancshares, Inc. and its wholly-owned subsidiary, Putnam County Bank. All significant intercompany balances and transactions have been eliminated.

Use of Estimates

The preparation of financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

Investment Securities

Securities that management has both the positive intent and ability to hold to maturity are classified as securities held to maturity and are carried at cost, adjusted for amortization of premium or accretion of discount using the interest method. Securities that may be sold prior to maturity for asset/liability management purposes, or that may be sold in response to changes in interest rates, changes in prepayment risk, to increase regulatory capital or other similar factors, are classified as securities available for sale and carried at fair value with any adjustments to fair value, after tax, reported as a separate component of shareholders' equity.

Interest and dividends from securities, including the amortization of premiums and the accretion of discounts, are reported in interest and dividends on securities using the interest method. Gains and losses on securities are determined using specific-identification method.

Declines in the fair value of individual held to maturity and available for sale securities below their cost that are other than temporary result in write-downs of the individual securities to their fair value. The related write-downs are included in earnings as realized losses. The Bank had no such losses for the years ended December 31, 2007, 2006, and 2005.

Revenue Recognition

Interest on loans is accrued and credited to operations based upon the principal amount outstanding. The accrual of interest income generally is discontinued when a loan becomes 90 days past due as to principal or interest. When interest accruals are discontinued, unpaid interest credited to income in the current year is reversed, and interest accrued in prior years is charged to the allowance for credit losses. Management may elect to continue the accrual of interest when the estimated net realizable value of collateral is sufficient to cover the principal balance and accrued interest, and the loan is in the process of collection.

Credit life insurance commissions on loans (principally short-term installment loans) are being recognized as collected. The use of this method of recognition does not produce results which are materially different from that which would have been produced if such commissions were deferred and amortized as an adjustment of loan yield over the life of the related loan.

Comprehensive Income

Effective January 1, 1999, the Bank adopted Statement of Financial Accounting Standards No. 130, "Reporting Comprehensive Income." Pursuant to this rule, the Consolidated Statements of Changes in Shareholders' Equity now include a new measure called "Comprehensive Income," which includes net income as well as certain items that are reported within a separate component of shareholders' equity that bypass net income. Currently, the Bank's only component of other comprehensive income is its unrealized gains (losses) on securities available for sale.

Notes To Consolidated Financial Statements For Years Ended December 31, 2007, 2006 And 2005 (continued)

Allowance for Credit Losses

The allowance for credit losses is maintained at a level considered adequate to provide for potential credit losses. The allowance is increased by provisions charged to operating expense and reduced by net charge offs. The level of the allowance is based on management's evaluation of potential losses in the loan portfolio, as well as prevailing and anticipated economic conditions.

A loan is considered impaired, based on current information and events, if it is probable that the Bank will be unable to collect the scheduled payments of principal and interest when due according to the contractual terms of the loan agreement. The reserve for possible credit losses related to loans that are identified for evaluation, in accordance with FAS No. 114, is based on discounted cash flows using the loan's initial effective interest rate or the fair value of the collateral for certain collateral dependent loans. If the valuation is less than the recorded value of the loan, an impairment reserve must be established for the difference. The adoption of this standard did not have, and is not expected to have, a material effect on the Bank's financial position, results of operations, accounting policies or the determination of the adequacy of the allowance for credit losses.

Bank Premises and Equipment

Bank premises and equipment are carried at original cost, less accumulated depreciation computed primarily on the modified accelerated cost recovery system over the estimated useful lives of the assets. Maintenance and repairs and minor improvements are charged to expense. Gains and losses on premises and equipment retired or sold are recognized currently in the statements of income.

Other Real Estate

Real estate acquired through foreclosure is carried at the lower of cost or market value. Any excess of the loan balance over the fair market value is charged to the allowance for credit losses. Expenses incurred in connection with other real estate subsequent to acquisition are charged to operating expense.

Income Taxes

The Bank follows the practice of accruing federal income taxes based on income reported for financial statement purposes. In the event income or expenses are recognized in different periods for tax, as opposed to financial purposes, deferred taxes are provided on such timing differences.

Pension Plan

The Bank accounts for its pension plan in accordance with Statement of Financial Accounting Standards No. 132, "Employer's Accounting for Pensions." Pension accounting information is disclosed in Note 8 to the consolidated financial statements.

Cash and Cash Equivalents

For the purpose of presentation in the statements of cash flows, cash and cash equivalents are defined as those amounts included in the balance sheet caption "Cash and Due from Banks."

Off-Balance Sheet Financial Instruments

In the ordinary course of business, the Bank has entered into off-balance sheet financial instruments consisting of commitments to extend credit, commercial letters of credit, and standby letters of credit. Such financial instruments are recorded in the financial statements when they become payable.

Note 2

Restrictions on Cash and Due from Banks:

Federal Reserve regulations require depository institutions to maintain cash reserves with the Federal Reserve Bank. The average amounts of required reserve balances were approximately \$6,017,000 and \$5,783,000 for the years ended December 31, 2007 and 2006, respectively.

Notes To Consolidated Financial Statements For Years Ended December 31, 2007, 2006 And 2005 (continued)

Note 3

Investment Securities:

The carrying amounts and approximate market values of investment securities at December 31, 2007 and 2006, are as follows:

	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
December 31, 2007				
Available for Sale Securities -				
U.S. Government and Agency Securities	\$ 60,216,812	\$ 895,688	\$ -0-	\$ 61,112,500
State and Municipal Securities	7,252,433	44,343	(19,177)	7,277,599
Totals	<u>\$ 67,469,245</u>	<u>\$ 940,031</u>	<u>\$ (19,177)</u>	<u>\$ 68,390,099</u>
Held to Maturity Securities -				
U.S. Government and Agency Securities	<u>\$ 38,703,017</u>	<u>\$ 47,132</u>	<u>\$ (774)</u>	<u>\$ 38,749,375</u>
	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
December 31, 2006				
Available for Sale Securities -				
U.S. Government and Agency Securities	\$ 79,933,392	\$ 206,824	\$ (591,779)	\$ 79,548,437
State and Municipal Securities	5,638,940	34,365	(39,949)	5,633,356
Totals	<u>\$ 85,572,332</u>	<u>\$ 241,189</u>	<u>\$ (631,728)</u>	<u>\$ 85,181,793</u>
Held to Maturity Securities -				
U.S. Government and Agency Securities	<u>\$ 38,598,917</u>	<u>\$ 15,458</u>	<u>\$ -0-</u>	<u>\$ 38,614,375</u>

Investment securities with carrying amounts of \$43,095,613 and \$36,683,945 and market values of \$43,678,483 and \$36,611,506, respectively, were pledged to secure public deposits and for other purposes as required or permitted by law at December 31, 2007 and 2006.

Gross realized gains and gross realized losses on sales of available for sale securities for the years ended December 31, 2007, 2006, and 2005, are as follows:

	2007	2006	2005
Gross Realized Gains:			
U.S. Government and Agency Securities	<u>\$ 79,801</u>	<u>\$ -0-</u>	<u>\$ 289,506</u>
Gross Realized Losses:			
U.S. Government and Agency Securities	<u>\$ 72,224</u>	<u>\$ 167,416</u>	<u>\$ 990,188</u>

The amortized cost and estimated market value of debt securities at December 31, 2007, by contractual maturities, are shown below. Expected maturities may differ from contractual maturities because borrowers may have the right to call or prepay obligations with or without call or repayment penalties.

	Available for Sale Securities		Held to Maturity Securities	
	Amortized Cost	Fair Value	Amortized Cost	Fair Value
Due in One Year or Less	\$ 24,998,545	\$ 25,079,688	\$ 38,703,017	\$ 38,749,375
Due from One Year to Five Years	36,851,243	37,667,863	-0-	-0-
Due from Five Years to Ten Years	285,000	294,613	-0-	-0-
Due after Ten Years	5,334,457	5,347,935	-0-	-0-
Totals	<u>\$ 67,469,245</u>	<u>\$ 68,390,099</u>	<u>\$ 38,703,017</u>	<u>\$ 38,749,375</u>

Notes To Consolidated Financial Statements For Years Ended December 31, 2007, 2006 And 2005 (continued)

Note 4

Loans:

Total loans at December 31, 2007 and 2006, by major loan categories are summarized as follows:

	<u>2007</u>	<u>2006</u>
Commercial	\$ 16,611,988	\$ 16,948,387
Real Estate - Construction and Mortgage	285,299,933	261,357,058
Installment	<u>11,071,618</u>	<u>11,832,766</u>
Gross Loans	\$ 312,983,539	\$ 290,138,211
Unearned Discount	<u>(73,142)</u>	<u>(146,022)</u>
Total Loans	\$ 312,910,397	\$ 289,992,189
Allowance for Credit Losses	<u>(3,401,326)</u>	<u>(2,730,387)</u>
Loans, Net	<u>\$ 309,509,071</u>	<u>\$ 287,261,802</u>

An analysis of the change in the allowance for credit losses follows:

	<u>2007</u>	<u>2006</u>	<u>2005</u>
Beginning Balances - January 1,	\$ 2,730,387	\$ 2,700,000	\$ 4,206,248
Loans Charged Off	(801,351)	(669,877)	(233,329)
Recoveries of Loans Previously Charged Off	351,955	550,264	115,600
Provision to Expense for Credit Losses	<u>1,120,335</u>	<u>150,000</u>	<u>(1,388,519)</u>
Ending Balances - December 31,	<u>\$ 3,401,326</u>	<u>\$ 2,730,387</u>	<u>\$ 2,700,000</u>

The provision for credit losses charged to expense is based upon credit loss experience and an evaluation of potential losses in the current loan and lease portfolio, including the evaluation of impaired loans under SFAS No.'s 114 and 118 (collectively, SFAS No. 114), "Accounting by Creditors for Impairment of a Loan" and "Accounting by Creditors for Impairment of a Loan - Income Recognition and Disclosures." All nonaccrual loans on which a specific reserve calculation is required and significant troubled debt restructurings are considered impaired. Impairment is primarily measured based on the fair value of the loan's collateral. Impairment losses are included in the provision for credit losses. Loans collectively evaluated for impairment include certain smaller balance commercial loans, consumer loans and residential real estate loans. SFAS No. 114 does not apply to large groups of smaller balance homogeneous loans that are collectively evaluated for impairment, except for those loans restructured under a troubled debt restructuring. A loan is considered restructured when certain concessions are made to a financially troubled debtor that are not normally considered.

The following summarizes impaired loan information at December 31, 2007, 2006, and 2005:

	<u>2007</u>	<u>2006</u>	<u>2005</u>
Impaired Loans with Related Allowance	\$ -0-	\$ -0-	\$ -0-
Impaired Loans with no Related Allowance	<u>1,944,695</u>	<u>1,969,477</u>	<u>-0-</u>
Total Impaired Loans	\$ 1,944,695	\$ 1,969,477	\$ -0-
Allowance on Impaired Loans	<u>\$ -0-</u>	<u>\$ -0-</u>	<u>\$ -0-</u>
Average Impaired Loans	<u>\$ 1,944,381</u>	<u>\$ 1,500,374</u>	<u>\$ 504,467</u>
Interest Income Recognized on Impaired Loans	<u>\$ -0-</u>	<u>\$ -0-</u>	<u>\$ -0-</u>

Notes To Consolidated Financial Statements For Years Ended December 31, 2007, 2006 And 2005 (continued)

Interest payments on impaired loans are typically applied to principal unless collectibility of the principal amounts is fully assured, in which case interest is recognized on the cash basis. Interest may be recognized on the accrual basis for certain troubled debt restructurings which are included in the impaired loan data above.

In the normal course of business, the Bank makes loans to executive officers and directors and related business interests on substantially the same terms, including interest rates and collateral, as those prevailing at the time for comparable transactions with unrelated persons and do not involve more than the normal risk of collectibility.

The following presents the activity with respect to loans to related parties for 2007 and 2006:

	<u>2007</u>	<u>2006</u>
Balances - January 1,	\$ 15,236,880	\$ 13,780,893
New Loans	707,011	3,614,936
Repayments	(747,477)	(2,158,949)
	<u>\$ 15,196,414</u>	<u>\$ 15,236,880</u>
Balances - December 31,		

Note 5

Bank Premises and Equipment:

Major classifications of bank premises and equipment at December 31, 2007 and 2006, are summarized as follows:

	<u>2007</u>	<u>2006</u>
Buildings and Improvements	\$ 2,045,588	\$ 1,856,588
Furniture and Fixtures	1,497,979	1,307,302
	<u>\$ 3,543,567</u>	<u>\$ 3,163,890</u>
Less: Accumulated Depreciation	2,642,783	2,459,795
	<u>\$ 900,784</u>	<u>\$ 704,095</u>
Land	200,460	200,460
	<u>\$ 1,101,244</u>	<u>\$ 904,555</u>
Bank Premises and Equipment, Net		

Depreciation expense for the years ended December 31, 2007, 2006, and 2005, was \$202,175, \$181,150, and \$188,532, respectively, and is included in expenses of premises and equipment on the statements of income.

Putnam County Bank has entered into a noncancellable lease agreement (operating lease) with a related party for its Teays Valley branch. The minimum annual rental commitment under this lease, exclusive of taxes and other charges payable by the lessee at December 31, 2007, is as follows:

<u>Year</u>	<u>Amount</u>
2008	\$ 54,040
2009	55,894
2010	57,821
2011	59,826
2012	56,587
	<u>56,587</u>
Total	<u>\$ 284,168</u>

Notes To Consolidated Financial Statements For Years Ended December 31, 2007, 2006 And 2005 (continued)

Note 6

Deposits:

The major categories of deposits at December 31, 2007 and 2006, are as follows:

	<u>2007</u>	<u>2006</u>
Noninterest Bearing	\$ 42,492,034	\$ 44,595,491
Interest Bearing:		
Money Market	\$ 86,785,441	\$ 94,289,302
Savings	18,114,134	18,713,972
Time and Certificates of Deposit	110,457,165	104,206,115
Certificates of Deposit over \$100,000	<u>149,189,115</u>	<u>132,681,066</u>
Total Interest Bearing Deposits	<u>\$ 364,545,855</u>	<u>\$ 349,890,455</u>
Total Deposits	<u>\$ 407,037,889</u>	<u>\$ 394,485,946</u>

Scheduled maturities of time and certificates of deposits at December 31, 2007, are as follows:

2008	\$ 233,240,947
2009	21,101,583
2010	5,203,750
2011 and Thereafter	<u>100,000</u>
Total	<u>\$ 259,646,280</u>

The Bank has received deposits in the normal course of business from directors and officers of the Bank and their associates. Such related party deposits were accepted on substantially the same terms including interest rates and maturities as those prevailing at the time for comparable transactions with unrelated parties. The aggregate dollar amount of these deposits was approximately \$27,218,528 and \$40,776,041 at December 31, 2007 and 2006, respectively.

Note 7

Income Taxes:

The income tax provisions (benefits) included in the consolidated statements of income are summarized as follows:

	<u>2007</u>	<u>2006</u>	<u>2005</u>
Currently Payable:			
Federal	\$ 2,284,336	\$ 2,574,789	\$ 2,790,662
State	<u>301,299</u>	<u>329,042</u>	<u>357,506</u>
Totals	<u>\$ 2,585,635</u>	<u>\$ 2,903,831</u>	<u>\$ 3,148,168</u>
Deferred (Benefit):			
Federal	\$ (320,814)	\$ (48,951)	\$ 453,232
State	<u>(32,114)</u>	<u>(5,999)</u>	<u>55,543</u>
Totals	<u>\$ (352,928)</u>	<u>\$ (54,950)</u>	<u>\$ 508,775</u>
Total Applicable Income Taxes	<u>\$ 2,232,707</u>	<u>\$ 2,848,880</u>	<u>\$ 3,656,943</u>

Notes To Consolidated Financial Statements For Years Ended December 31, 2007, 2006 And 2005 (continued)

Timing differences in the recognition of income and expenses for tax and financial reporting purposes created the following components of deferred income taxes (benefit):

	<u>2007</u>	<u>2006</u>	<u>2005</u>
Bad Debts	\$ (352,939)	\$ (54,960)	\$ 508,754
Discount on Investment Securities	<u>11</u>	<u>10</u>	<u>21</u>
Totals	<u>\$ (352,928)</u>	<u>\$ (54,950)</u>	<u>\$ 508,775</u>

The following is a reconciliation of consolidated federal income tax to the amount computed at the statutory rate:

	<u>2007</u>		<u>2006</u>		<u>2005</u>	
	<u>Amount</u>	<u>%</u>	<u>Amount</u>	<u>%</u>	<u>Amount</u>	<u>%</u>
Tax on Income before Income Tax at the Top Statutory Income Tax Rate	\$ 2,132,392	34.00%	\$ 2,708,655	34.00%	\$ 3,451,398	34.00%
Increase (Decrease) Resulting from:						
State Income Tax, Net of Federal Benefit	177,662	2.83	213,209	2.68	272,611	2.69
Nontaxable Interest Income	(94,785)	(1.51)	(86,436)	(1.08)	(75,031)	(.74)
Nondeductible Interest Expense	13,181	.21	9,998	.13	5,926	.06
Other Items	<u>4,257</u>	<u>.07</u>	<u>3,454</u>	<u>.04</u>	<u>2,039</u>	<u>.02</u>
Tax on Income	<u>\$ 2,232,707</u>	<u>35.60%</u>	<u>\$ 2,848,880</u>	<u>35.77%</u>	<u>\$ 3,656,943</u>	<u>36.03%</u>

The approximate tax (benefit) effects of the net investment securities gains (losses) were \$2,776, (\$61,341), and (\$256,730) for the years 2007, 2006, and 2005, respectively.

Notes To Consolidated Financial Statements

For Years Ended December 31, 2007, 2006 And 2005 (continued)

Note 8

Pension Plan:

The Bank is a participant in a multiple employer non-contributory defined benefit pension plan covering the majority of employees. The retirement benefits are based on length of service and the employee's compensation during his/her time of service.

The following table shows the plan's funded status at December 31, 2007 and 2006:

	<u>2007</u>	<u>2006</u>
Accumulated Pension Benefit Obligation	\$ 3,751,776	\$ 3,585,999
Value of Future Salary Projections	<u>354,169</u>	<u>356,661</u>
Total Projected Pension Benefit Obligation	\$ 4,105,945	\$ 3,942,660
Fair Value of Plan Assets	<u>3,358,329</u>	<u>2,701,858</u>
Plan Assets in Excess (Deficient) of Projected Benefit Obligation	\$ (747,616)	\$ (1,240,802)
Unrecognized Prior Service Cost	-0-	(1,970)
Unrecognized Net Loss or (Gain)	1,005,877	1,316,116
Unrecognized Net Transition Liability or (Asset)	-0-	-0-
Accumulated Other Comprehensive Income	<u>(651,708)</u>	<u>(957,485)</u>
Unfunded (Accrued) or Prepaid Pension Cost	<u>\$ (393,447)</u>	<u>\$ (884,141)</u>

The components of pension (expense) income for the years ended December 31, 2007, 2006, and 2005, are as follows:

	<u>2007</u>	<u>2006</u>	<u>2005</u>
Service Cost-Benefits Earned During Year	\$ (179,889)	\$ (194,178)	\$ (137,972)
Interest Cost on Projected Benefit Obligation	(236,418)	(216,215)	(209,848)
Actual Return on Assets	239,208	218,730	206,583
Amortization of Net Gain (Loss)	(86,530)	(91,484)	(57,776)
Net Amortization and Deferral	<u>1,970</u>	<u>4,995</u>	<u>7,692</u>
Net Periodic Pension (Cost) Benefit	<u>\$ (261,659)</u>	<u>\$ (278,152)</u>	<u>\$ (191,321)</u>
Actuarial Assumptions:			
Weighted Average Discount Rate for Projected Benefit Obligation	6.00%	5.75%	6.50%
Weighted Average Rate of Compensation Increase	3.00%	3.00%	3.50%
Expected Long-Term Rate of Return on Plan Assets	8.50%	8.50%	8.50%

Notes To Consolidated Financial Statements For Years Ended December 31, 2007, 2006 And 2005 (continued)

Note 9

Parent Company Condensed Financial Information:

CONDENSED BALANCE SHEETS

	December 31,	
	2007	2006
ASSETS		
Investment in Subsidiary	\$ 65,055,421	\$ 61,383,822
Cash	1,446	3,112
Total Assets	<u>\$ 65,056,867</u>	<u>\$ 61,386,934</u>
LIABILITIES AND SHAREHOLDERS' EQUITY		
Total Liabilities	\$ -0-	\$ -0-
Shareholders' Equity	<u>\$ 65,056,867</u>	<u>\$ 61,386,934</u>
Total Liabilities and Shareholders' Equity	<u>\$ 65,056,867</u>	<u>\$ 61,386,934</u>

CONDENSED STATEMENTS OF INCOME

	For Years Ended December 31,		
	2007	2006	2005
INCOME	<u>\$ 1,225,234</u>	<u>\$ 1,047,592</u>	<u>\$ 915,379</u>
EXPENSES:			
Operating Expenses	<u>\$ 44,666</u>	<u>\$ 43,584</u>	<u>\$ 29,097</u>
Income before Income Tax Benefit and Equity in Undistributed Earnings of Subsidiary	<u>\$ 1,180,568</u>	<u>\$ 1,004,008</u>	<u>\$ 886,282</u>
Applicable Income Taxes (Benefit)	<u>(17,766)</u>	<u>(17,408)</u>	<u>(11,621)</u>
Income before Equity in Undistributed Earnings of Subsidiary	<u>\$ 1,198,334</u>	<u>\$ 1,021,416</u>	<u>\$ 897,903</u>
Equity in Undistributed Earnings of Subsidiary	<u>2,840,700</u>	<u>4,096,337</u>	<u>5,596,323</u>
Net Income	<u>\$ 4,039,034</u>	<u>\$ 5,117,753</u>	<u>\$ 6,494,226</u>

Notes To Consolidated Financial Statements

For Years Ended December 31, 2007, 2006 And 2005 (continued)

CONDENSED STATEMENTS OF CASH FLOWS

	For Years Ended December 31,		
	2007	2006	2005
CASH FLOWS FROM OPERATING ACTIVITIES:			
Net Income	\$ 4,039,034	\$ 5,117,752	\$ 6,494,226
Adjustments to Reconcile Net Income to Net Cash Provided by Operating Activities:			
Equity in Undistributed Earnings of Subsidiary	<u>(2,840,700)</u>	<u>(4,096,337)</u>	<u>(5,596,323)</u>
Net Cash Provided by Operating Activities	<u>\$ 1,198,334</u>	<u>\$ 1,021,415</u>	<u>\$ 897,903</u>
CASH FLOWS FROM FINANCING ACTIVITIES:			
Dividends Paid	<u>\$ (1,200,000)</u>	<u>\$ (1,020,000)</u>	<u>\$ (900,000)</u>
Net Cash Used in Financing Activities	<u>\$ (1,200,000)</u>	<u>\$ (1,020,000)</u>	<u>\$ (900,000)</u>
Net Change in Cash and Cash Equivalents	\$ (1,666)	\$ 1,415	\$ (2,097)
Cash and Cash Equivalents at Beginning of Year	<u>3,112</u>	<u>1,697</u>	<u>3,794</u>
Cash and Cash Equivalents at End of Year	<u>\$ 1,446</u>	<u>\$ 3,112</u>	<u>\$ 1,697</u>

Note 10

Related Party Transactions:

Some officers and directors (including their affiliates, families and related entities) of Putnam Bancshares, Inc. and its subsidiary are customers of the subsidiary and have had, and are expected to have, transactions with the subsidiary in the ordinary course of business. In addition, some officers and directors are also officers and directors of corporations which are customers of the Bank and have had, and are expected to have, transactions with the Bank in the ordinary course of business. In the opinion of management, such transactions are consistent with prudent banking practices and are within applicable banking regulations.

Notes To Consolidated Financial Statements For Years Ended December 31, 2007, 2006 And 2005 (continued)

Note 11

Commitments and Contingent Liabilities:

The Bank's consolidated financial statements do not reflect various commitments and contingent liabilities that arise in the normal course of business and that involve elements of credit risk, interest rate risk, and liquidity risk. These commitments and contingent liabilities are commitments to extend credit, commercial letters of credit, and standby letters of credit. A summary of the Bank's commitments and contingent liabilities at December 31, 2007, is as follows:

	<u>Notional Amount</u>
Commitments to Extend Credit	\$ 33,071,000
Commercial Letters of Credit	-0-
Standby Letters of Credit	591,000

Commitments to extend credit, commercial letters of credit, and standby letters of credit all include exposure to some credit loss in the event of nonperformance of the customer. The Bank's credit policies and procedures for credit commitments and financial guarantees are the same as those for extension of credit that are recorded on the consolidated balance sheets. Because these instruments generally have fixed maturity dates, they do not generally present any significant liquidity risk to the Bank.

In the ordinary course of business, Putnam Bancshares, Inc. and its subsidiary are sometimes parties to various legal proceedings and claims. While any litigation contains an element of uncertainty, management is unaware of any legal proceedings at December 31, 2007, of which the result would have a material adverse effect upon the consolidated financial statements.

Note 12

Concentrations of Credit Risk:

Cash due from correspondent banks, based on bank balances, exceeded federally insured limits by approximately \$7,911,000 at December 31, 2007. Federal funds sold are generally unsecured by the correspondent banks.

The majority of the Bank's loans, commitments, and commercial and standby letters of credit have been granted to customers in the Bank's market area. The rest are to customers from the area that have since relocated to other areas. Most of such customers are depositors of the Bank. Investments in state and municipal securities and loans to governmental entities are within the Bank's home state. The concentrations of credit by type of loan are set forth in Note 4. The distribution of commitments to extend credit approximates the distribution of loans outstanding. Commercial and standby letters of credit were granted primarily to commercial borrowers.

Note 13

Regulatory Matters:

Putnam Bancshares, Inc.'s principal source of funds for future dividend payments to shareholders will be from dividend payments received from its wholly-owned subsidiary, Putnam County Bank.

The Bank, as a state chartered member bank of the Federal Reserve System, is subject to the dividend restrictions set forth by the West Virginia Division of Banking as well as the Federal Reserve Board. Under such restrictions, the Bank may not, without the prior approval of the West Virginia Division of Banking and the Federal Reserve Board, declare dividends in excess of the sum of the current year's earnings (as defined) plus the retained net profits (as defined) from the prior two years. The Bank normally restricts dividends to a lesser amount. The dividends as of December 31, 2007, that the Bank could declare without the approval of the West Virginia Division of Banking and the Federal Reserve Board, amounted to approximately \$6,937,000.

The Bank is also subject to various regulatory capital requirements administered by federal and state banking agencies. Failure to meet the minimum capital requirements can initiate certain actions by regulators that, if undertaken, could have a material effect on the Bank and the consolidated financial statements. Capital adequacy guidelines require minimum ratios of 4.00% for Tier 1 risk-based capital, 8.00% for total risk-based capital, and 4.00% for Tier 1 leverage capital. To be considered well capitalized under the regulatory framework for prompt corrective actions, the ratios must be at least 6.00%, 10.00%, and 5.00%, respectively.

Notes To Consolidated Financial Statements For Years Ended December 31, 2007, 2006 And 2005 (continued)

Capital amounts and classifications are also subject to qualitative judgments by the regulators about components, risk-weighting of assets and certain off-balance sheet items, and other factors. As of December 31, 2007 and 2006, the Bank has met all capital adequacy requirements and had regulatory capital ratios in excess of the levels established for well capitalized institutions. There are no conditions or events since the most recent notification that management believes have changed the Bank's prompt corrective action category.

The Bank's actual ratios as well as a comparison of the period-end capital balances with the related amounts established by the regulatory agencies are as follows:

	Ratios	Capital Amounts		
		Actual	Minimum	Well Capitalized
As of December 31, 2007:				
Tier 1 Risk-Based Capital	22.98%	\$ 64,473,000	\$ 11,223,000	\$ 16,834,000
Total Risk-Based Capital	24.19	67,874,000	22,446,000	28,057,000
Tier 1 Leverage Capital	13.54	64,473,000	19,048,000	23,811,000
As of December 31, 2006:				
Tier 1 Risk-Based Capital	23.89%	\$ 61,634,000	\$ 10,320,000	\$ 15,480,000
Total Risk-Based Capital	24.95	64,364,000	20,640,000	25,800,000
Tier 1 Leverage Capital	13.43	61,634,000	18,362,000	22,953,000

The Bank executed a written agreement on November 19, 2003, with the Federal Reserve Bank of Richmond and the West Virginia Division of Banking to take corrective measures to enhance and improve its programs and procedures for complying with the Bank Secrecy Act of the U.S. Department of the Treasury and with the anti-money laundering provisions of the Board of Governors of the Federal Reserve System. This agreement was terminated by Federal Reserve System and West Virginia Division of Banking on November 6, 2007, by a letter dated November 3, 2007.

Note 14

Disclosures about Fair Value of Financial Instruments:

At December 31, 1995, the Bank adopted Financial Accounting Standards Board Statement No. 107, which requires disclosure of fair value information about financial instruments, whether or not recognized in the balance sheet, for which it is practicable to estimate that value. In cases where quoted market prices are not available, fair values are based on estimates using present value or other valuation techniques. Those techniques are significantly affected by the assumptions used, including the discount rate and estimates of future cash flows. In that regard, the derived fair value estimates cannot be substantiated by comparison to independent market settlement of the instruments. Statement 107 excludes certain financial instruments and all nonfinancial instruments from its disclosure requirements. Accordingly, the aggregate fair value amounts presented do not represent the underlying value of the Bank.

Notes To Consolidated Financial Statements For Years Ended December 31, 2007, 2006 And 2005 (continued)

The following methods and assumptions were used by the Bank in estimating its fair value disclosures for financial instruments.

Cash and Due from Banks: The carrying amount reported in the balance sheet for cash and due from banks approximates that asset's fair value.

Federal Funds Sold: The carrying amount reported in the balance sheet for federal funds sold approximates that asset's fair value.

Investment Securities: Fair values for investment securities are based on quoted market prices where available. If quoted market prices are not available, fair values are based on quoted market prices of similar instruments.

Loans: The fair values of fixed rate commercial, real estate, and consumer loans are estimated using discounted cash flow analysis, using interest rates currently being offered for loans with similar terms to borrowers of similar credit quality. For variable rate loans that reprice frequently and with no significant change in credit risk, fair values are based on carrying values.

Deposits: The estimated fair values of demand deposits (i.e. interest and noninterest checking, passbook savings, and certain types of money market accounts) are, by definition, equal to their carrying amounts. Fair values for fixed-rate certificates of deposit are estimated using a discounted cash flow calculation that applies interest rates, currently being offered on certificates, to a schedule of aggregated expected monthly maturities on time deposits.

The estimated fair values of the Bank's financial instruments at December 31, 2007 and 2006, are as follows:

	2007		2006	
	Carrying Amounts	Fair Value	Carrying Amounts	Fair Value
Financial Assets:				
Cash and Due from Banks	\$ 18,500,610	\$ 18,500,610	\$ 17,814,524	\$ 17,814,524
Federal Funds Sold	35,000,000	35,000,000	25,000,000	25,000,000
Investment Securities	107,093,116	107,139,474	123,780,710	123,796,168
Loans	312,910,397	299,814,207	289,992,190	274,295,444
Financial Liabilities:				
Deposits	\$ 407,039,335	\$ 407,834,880	\$ 394,489,058	\$ 394,996,453