

PIONEER BANK

2001 Annual Report



*A 100 Year Legacy
A Commitment to a New Century*

MISSION STATEMENT

Pioneer Bank's mission is to provide superior banking products and services to our customers.

We will continue to maintain goals that will enable Pioneer to be a leader in the communities we serve, increase profitability, strive for growth and improvement, provide the highest quality of service to our customers, and sustain integrity, confidence, and success for our stockholders, customers, and employees.



PIONEER BANK

Dear Pioneer Bank Stockholder:

Our 100th year of service to Southern New Mexico was positively impacted by declining interest rates, near record levels of loan production, and increased net income. Net income, totaling \$2,853,972, increased 12.7% over last year. These earnings occurred after a \$508,000 write-down, net of tax, of our interest rate caps, pursuant to FAS-133 ("Accounting for Derivative Instruments and Hedging Activities," Note A of Financial Statements). Loan production totaled approximately \$170.2 million, up 102% over year-2000 loan closings of \$84.2 million. After payment of dividends of \$1.05 per share, stockholders equity increased 12.7% to \$25 million (\$25.10 per share).

In spite of the very positive operating results, the assets of your Bank increased a modest 2.7% to \$372.9 million. Total deposits declined 2.6% (\$6.3 million), due to a decrease in collateralized public fund deposits. On the positive side, checking account deposits increased significantly, which reflects continued growth in our retail deposit base. Loan servicing for other investors grew to \$361.2 million, a direct result of greater loan production. Our servicing portfolio showed a fair value, as determined by an independent nationally-recognized investment banker, of approximately \$800,000 in excess of our carrying value of \$3.2 million.

In November 2001, I announced my plan to retire as President from the Bank effective May 31, 2002. However, I do plan to remain on the Board of Directors, at least until the expiration of my current term in 2004. At my retirement, I shall have served as President in excess of 22 years and shall have been employed by the Bank approximately 25 years. After a search by the Board of Directors, Executive Vice President Jon Hitchcock was selected to succeed me as President and Chief Executive Officer. Jon is a very experienced and capable banker who has served with Pioneer since 1980 and has been a director since 1982. Our stockholders and customers should anticipate no significant change in the lending or operating philosophy of Pioneer in the succeeding years. Pioneer Bank's mission will be to continue to serve Southern New Mexico as a regional community bank providing superior banking products and services to our customers, and increased profitability, growth, and stability for our stockholders.

Pioneer's 2002 business plan projects another year of increased profits and growth in market share in all of our branch communities. We expect that interest rates will continue to remain low which should have a positive impact on our net interest margin. At year-end, we had no foreclosed real estate and our mortgage loan delinquencies remained below national averages. None of our market areas appear to have been negatively impacted by the much publicized national recession. Despite predictions of a slow national economic recovery, we are confident that Pioneer will continue to grow and prosper. Our new transaction facility in Las Cruces began operation in the fall of 2001, and we will continue to look for expansion opportunities in Southern New Mexico and West Texas.

For one hundred years the men and women of Pioneer Bank and its predecessor namesakes have dedicated their efforts to the improvement of Southern New Mexico. Our pledge to you is to continue to respect this heritage and to improve the profitability of your Bank and increase the value of our investment. The Board of Directors and officers appreciate the hard work of our dedicated staff, and we thank you, our stockholders and customers, for your continued support.

Sincerely,
PIONEER BANK

George W. Mitchell
President

Roswell, New Mexico
March 25, 2002

CONSOLIDATED STATEMENTS OF FINANCIAL CONDITION

PIONEER BANK AND SUBSIDIARY

	December 31,	
	2001	2000
ASSETS:		
Cash and cash equivalents - Note B.....	\$ 11,168,783	\$ 12,881,319
Investment and mortgage securities - Note C		
Available-for-sale.....	129,681,151	122,167,373
Held-to-maturity.....	1,207,185	7,018,254
Loans held for sale, net - Note D.....	37,051,775	15,510,131
Loans, net - Note D	169,945,244	183,342,583
Federal Home Loan Bank (FHLB), Fannie Mae (FNMA) and other stock.....	8,483,700	7,067,784
Office properties and equipment, net - Note E.....	6,333,981	5,306,479
Mortgage servicing rights, net - Note F.....	3,210,502	3,154,595
Accrued interest receivable.....	1,557,152	1,730,573
Interest rate cap agreements.....	271,547	1,666,934
Other assets.....	3,990,628	3,116,136
TOTAL ASSETS	\$ 372,901,648	\$ 362,962,161
LIABILITIES:		
Deposits - Note G.....	\$ 237,759,862	\$ 244,024,868
FHLB advances and other borrowings - Note H.....	99,796,743	86,895,692
Official checks.....	4,038,684	3,453,572
Deferred tax liabilities, net - Note I.....	1,665,411	1,963,271
Advance payments for taxes and insurance.....	1,563,368	1,452,898
Accrued interest payable.....	545,481	753,850
Accounts payable and other liabilities.....	2,208,295	1,953,030
TOTAL LIABILITIES	347,577,844	340,497,181
COMMITMENTS AND CONTINGENCIES - Note K		
STOCKHOLDERS' EQUITY - Note J:		
Capital stock, \$1 par value, 2,000,000 shares authorized; shares issued and outstanding: 2001 - 1,008,920; 2000 - 1,008,485.....	1,008,920	1,008,485
Additional paid-in capital.....	56,918	47,085
Retained earnings.....	24,153,338	22,358,675
Accumulated other comprehensive income (loss) - Note C.....	104,628	(949,265)
TOTAL STOCKHOLDERS' EQUITY	25,323,804	22,464,980
TOTAL LIABILITIES AND STOCKHOLDERS' EQUITY	\$ 372,901,648	\$ 362,962,161

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

CONSOLIDATED STATEMENTS OF INCOME

PIONEER BANK AND SUBSIDIARY

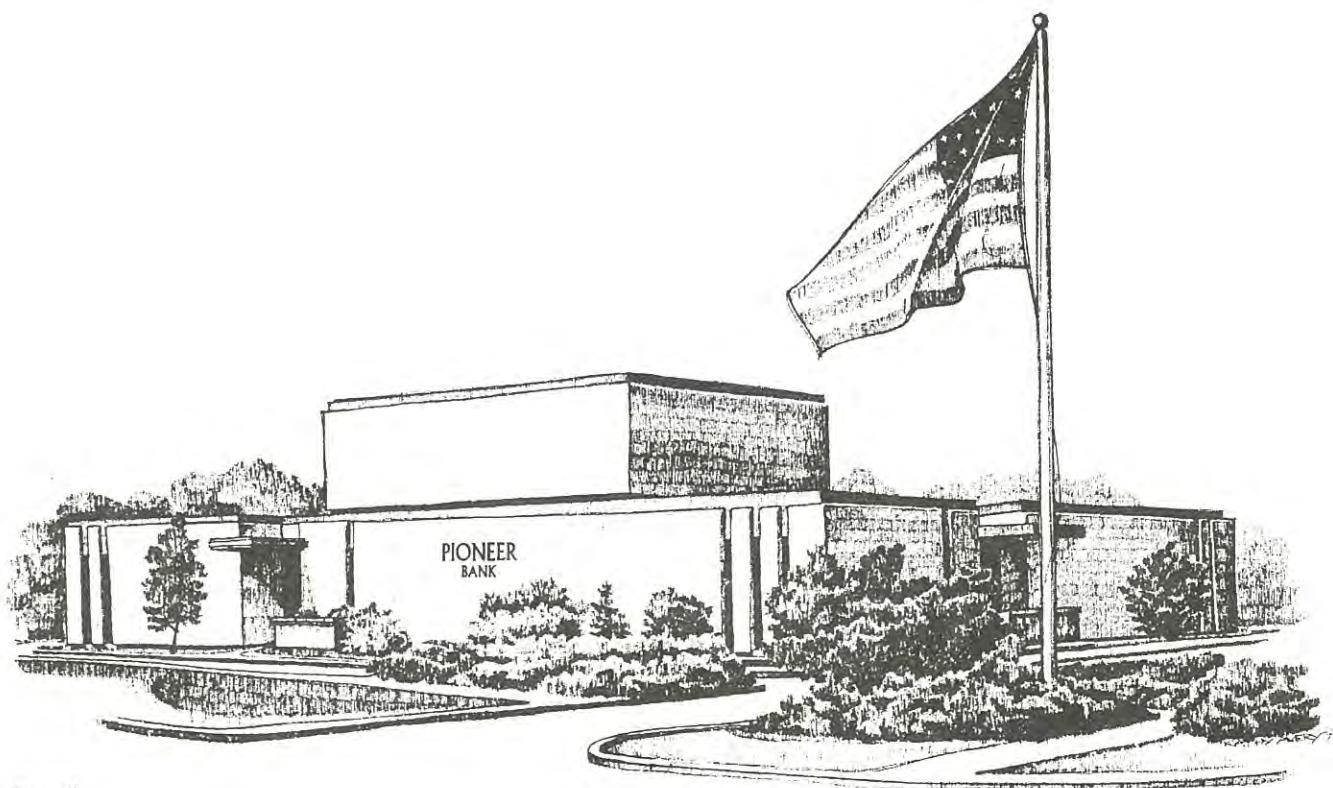
	Years Ended December 31,	
	2001	2000
INTEREST INCOME:		
Loans - Note D.....	\$ 14,518,276	\$ 15,532,833
Mortgage securities.....	7,879,761	6,226,295
Investment securities and other.....	257,916	1,006,023
	<u>22,655,953</u>	<u>22,765,151</u>
INTEREST EXPENSE:		
Deposits - Note G.....	8,572,184	10,827,242
FHLB advances and other borrowings.....	5,321,345	4,648,851
	<u>13,893,529</u>	<u>15,476,093</u>
NET INTEREST INCOME	8,762,424	7,289,058
LOAN LOSS PROVISION - Note D.....	(19,315)	36,000
NET INTEREST INCOME AFTER LOAN LOSS PROVISION.....	8,781,739	7,253,058
OTHER INCOME:		
Gain on sale of loans, net - Note D	2,153,093	1,042,720
Loan administration and service fees.....	834,710	1,456,326
Deposit account fees.....	748,487	767,249
Gain on sale of investment and mortgage securities, net - Note C.....	657,140	115,534
Dividends on FHLB, FNMA and other stock.....	365,566	375,439
Gain on sale of investment in real estate.....	10,803	199,974
Other.....	284,187	267,940
	<u>5,053,986</u>	<u>4,225,182</u>
OTHER EXPENSES:		
Compensation and employee benefits - Note M.....	4,884,362	4,383,243
Equipment.....	669,401	575,417
Data processing.....	664,646	632,674
Occupancy.....	597,139	569,210
Stationery, printing and office supplies.....	299,866	280,583
Professional and supervisory.....	263,114	226,208
Postage and transportation.....	246,282	239,245
Advertising and public relations.....	242,781	253,652
Telephone.....	171,759	173,585
Deposit insurance premiums.....	45,990	51,794
Other.....	340,438	262,535
	<u>8,425,778</u>	<u>7,648,146</u>
INCOME BEFORE INCOME TAX EXPENSE AND CUMULATIVE EFFECT OF CHANGE IN ACCOUNTING PRINCIPLE.....	5,409,947	3,830,094

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

CONSOLIDATED STATEMENTS OF INCOME - Continued

PIONEER BANK AND SUBSIDIARY

	Years Ended December 31,	
	2001	2000
INCOME BEFORE INCOME TAX EXPENSE AND CUMULATIVE EFFECT OF CHANGE IN ACCOUNTING PRINCIPLE.....	5,409,947	3,830,094
INCOME TAX EXPENSE - Note I.....	2,047,975	1,298,633
INCOME BEFORE CUMULATIVE EFFECT OF ACCOUNTING CHANGE.....	3,361,972	2,531,461
Cumulative effect on prior years of adopting SFAS 133, (net of tax benefit of \$332,947).....	(508,000)	-
NET INCOME.....	<u>\$ 2,853,972</u>	<u>\$ 2,531,461</u>
Weighted average number of capital stock shares outstanding.....	<u>1,008,756</u>	<u>1,008,485</u>
Income per share before cumulative effect of accounting change.....	\$ 3.33	\$ 2.51
Cumulative effect of accounting change.....	(0.50)	-
Net income per share.....	<u>\$ 2.83</u>	<u>\$ 2.51</u>
Dividends per share.....	<u>\$ 1.05</u>	<u>\$ 1.05</u>



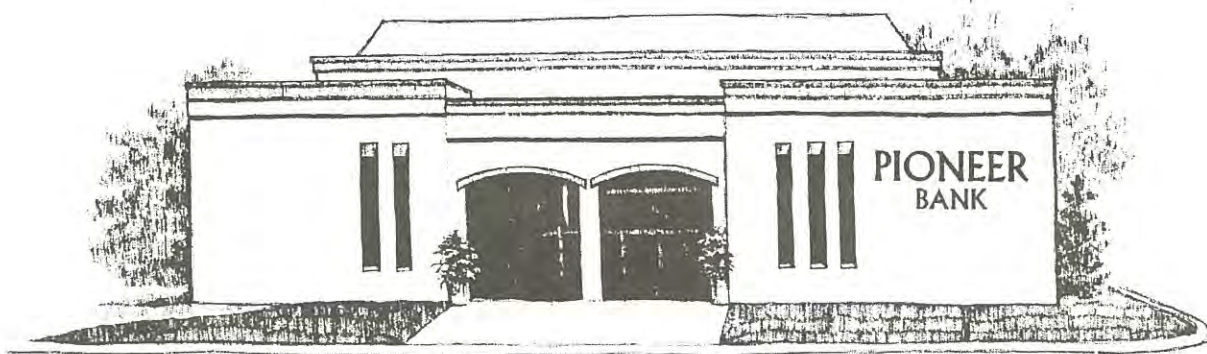
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The accompanying notes to consolidated financial statements are an integral part of these statements.

CONSOLIDATED STATEMENTS OF CASH FLOWS

PIONEER BANK AND SUBSIDIARY

	Years Ended December 31,	
	2001	2000
CASH FLOWS FROM OPERATING ACTIVITIES:		
Net Income.....	\$ 2,853,972	\$ 2,531,461
Cumulative effect of change in accounting principle.....	508,000	-
Adjustments to reconcile net income to net cash provided by operating activities:		
Amortization (accretion) of:		
Mortgage servicing rights.....	757,044	424,513
Premiums and discounts on investment and mortgage securities, net.....	(24,823)	(134,802)
Interest rate cap agreements.....	554,440	543,233
Loan loss provision.....	(19,315)	36,000
Change in mortgage servicing rights impairment allowance.....	448,715	(47)
Net (gain) loss on sales of:		
Loans.....	(2,153,093)	(1,042,720)
Office properties and equipment.....	-	17,361
Investments in real estate.....	(10,803)	(199,974)
Investment and mortgage securities available-for-sale.....	(657,140)	(115,534)
Federal Home Loan Bank stock dividends.....	(243,900)	(264,800)
Depreciation of office properties and equipment.....	464,948	420,803
Origination of mortgage loans held for sale.....	(81,215,596)	(15,358,261)
Changes in operating assets and liabilities:		
Accrued interest receivable.....	173,421	(217,928)
Other assets.....	(874,492)	(446,311)
Official checks.....	585,112	1,061,110
Deferred tax liabilities, net of tax effect of unrealized losses.....	(595,178)	(10,093)
Accrued interest payable.....	(208,369)	88,294
Accounts payable and other liabilities, net of dividends declared, not paid.....	255,026	564,056
Net cash used in operating activities.....	(79,402,031)	(12,103,639)



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

CONSOLIDATED STATEMENTS OF CASH FLOWS -- Continued

PIONEER BANK AND SUBSIDIARY

	Years Ended December 31,	
	2001	2000
CASH FLOWS FROM INVESTING ACTIVITIES:		
Loan originations and principal payments on loans, net.....	\$ 13,366,961	\$ 7,857,093
Investment and mortgage securities held-to-maturity:		
Maturities and principal reductions.....	188,018	353,970
Investment and mortgage securities available-for-sale:		
Purchases.....	(84,452,777)	(60,886,253)
Sales.....	100,235,386	44,925,911
Maturities and principal reductions.....	45,258,164	9,995,751
Purchases of interest rate cap agreements.....	-	(1,388,000)
Purchases of office properties and equipment.....	(1,492,450)	(886,969)
Proceeds from sales of office properties and equipment.....	-	7,100
Net purchases of FHLB, FNMA and other stock.....	(1,172,016)	(2,686,967)
Proceeds from sales of investments in real estate.....	60,496	351,781
Net cash provided by (used in) investing activities.....	71,991,782	(2,356,583)
CASH FLOWS FROM FINANCING ACTIVITIES:		
Net decrease in deposits.....	(6,265,006)	(10,995,205)
Additions to FHLB advances and other borrowings.....	70,168,051	55,600,000
Payments on FHLB advances and other borrowings.....	(57,267,000)	(28,643,015)
Net decrease in advance payments for taxes and insurance.....	110,470	(194,655)
Sales of capital stock.....	10,268	15
Payments of cash dividends.....	(1,059,070)	(1,058,909)
Net cash provided by financing activities.....	5,697,713	14,708,231
Increase in cash and cash equivalents.....	(1,712,536)	248,009
Cash and cash equivalents beginning of year.....	12,881,319	12,633,310
Cash and cash equivalents end of year.....	\$ 11,168,783	\$ 12,881,319
SUPPLEMENTAL DISCLOSURES OF CASH FLOW INFORMATION:		
Cash paid (received) during the year for:		
Interest.....	\$ 13,547,458	\$ 15,387,799
Income taxes.....	2,820,000	2,360,000
Income tax refunds.....	-	(972,259)
SUPPLEMENTAL SCHEDULE OF NON-CASH INVESTING AND FINANCING ACTIVITIES:		
Dividends declared, not paid.....	\$ 554,906	\$ 554,667
Loan securitizations transferred to AFS securities.....	60,565,379	15,521,074
Transfer of securities to available-for-sale from held-to-maturity.....	5,623,051	-
Transfer from loans to other real estate owned.....	49,693	-

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

CONSOLIDATED STATEMENTS OF STOCKHOLDERS' EQUITY

PIONEER BANK AND SUBSIDIARY

	Capital Stock \$1 par	Additional Paid-In Capital	Retained Earnings	Accumulated Other Comprehensive Income (Loss)	Total
Balance, December 31, 1999.....	\$ 1,008,485	\$ 47,070	\$ 20,886,123	\$ (3,419,855)	\$ 18,521,823
Capital stock issued.....	-	15	-	-	15
Comprehensive income:					
Net income.....	-	-	2,531,461	-	
Net change in unrealized losses on investment securities, net of tax.....	-	-	-	2,470,590	
Total comprehensive income					5,002,051
Dividends - \$1.05 per share.....	-	-	(1,058,909)	-	(1,058,909)
Balance, December 31, 2000.....	1,008,485	47,085	22,358,675	(949,265)	22,464,980
Capital stock issued.....	435	9,833	-	-	10,268
Comprehensive income:					
Net income.....	-	-	2,853,972	-	
Net change in unrealized losses on investment securities, net of tax.....	-	-	-	1,053,893	
Total comprehensive income					3,907,865
Dividends - \$1.05 per share.....	-	-	(1,059,309)	-	(1,059,309)
Balance, December 31, 2001.....	<u>\$ 1,008,920</u>	<u>\$ 56,918</u>	<u>\$ 24,153,338</u>	<u>\$ 104,628</u>	<u>\$ 25,323,804</u>

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

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

PIONEER BANK AND SUBSIDIARY

NOTE A – SUMMARY OF OPERATIONS AND SIGNIFICANT ACCOUNTING POLICIES

NATURE OF OPERATIONS: Pioneer Bank, "the Bank", operates six full customer service facilities, three savings branches and two loan production offices in the geographic area of the Southwest region of the United States, primarily New Mexico and West Texas. There are no concentrations of credit risk to any one industry. The Bank's primary sources of revenue are from providing loans to customers and servicing mortgage loans for others.

PRINCIPLES OF CONSOLIDATION: The consolidated financial statements include the accounts of the Bank and its wholly owned subsidiary, Pioneer Mortgage Company and its wholly owned subsidiary, Pioneer Property Management Company. Significant intercompany transactions and balances are eliminated in consolidation.

USE OF ESTIMATES IN THE PREPARATION OF FINANCIAL STATEMENTS: The preparation of financial statements, in conformity with accounting principles generally accepted in the United States of America, 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. The principal areas involving use of estimates and assumptions are the allowance for loan losses, allowance for losses on investments in real estate, the valuation allowance for impairment of mortgage servicing rights, and estimates of fair value of financial instruments. Actual results could differ from those estimates.

CASH AND CASH EQUIVALENTS: The Bank considers all cash on hand, due from banks and federal funds sold as cash and cash equivalents for purposes of the financial statement presentation.

INVESTMENT AND MORTGAGE SECURITIES AND FEDERAL HOME LOAN BANK STOCK: The Bank's investments are classified in two categories and accounted for as follows: "held-to-maturity," reported at amortized cost, adjusted for premiums and discounts that are recognized in income using the interest method over the period to maturity; and "available-for-sale," reported at fair value, with unrealized gains and losses, net of taxes, reported as a net amount in accumulated other comprehensive income. Realized gains and losses on investment and mortgage securities available-for-sale are recognized as determined by the specific identification basis upon disposition. Management has the ability and positive intent to hold securities categorized as held-to-maturity until maturity.

Investment securities consist of U.S. Treasury obligations. Mortgage securities consist of Government National Mortgage Association (GNMA) mortgage-backed securities, Federal National Mortgage Association (FNMA) pass-through certificates and Federal Home Loan Mortgage Corporation (FHLMC) participation certificates. Also included are collateralized mortgage obligations consisting of FNMA and FHLMC real estate mortgage investment conduits. Adjustments made to mortgage securities amortization and accretion related to changes in prepayments are recorded on a current basis. Federal Home Loan Bank Stock is carried at cost.

LOANS HELD FOR SALE: Mortgage loans originated and intended for sale in the secondary market are carried at the lower of cost or estimated fair value in the aggregate. Net unrealized losses are recognized in a valuation allowance by charges to income.

LOANS: Loans that management has the intent and ability to hold for the foreseeable future or until maturity or payoff are stated at their unpaid principal balances, less the allowances for loan losses, net deferred loan fees, and unearned discounts.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS -- Continued

PIONEER BANK AND SUBSIDIARY

NOTE A – SUMMARY OF OPERATIONS AND SIGNIFICANT ACCOUNTING POLICIES-Continued

ALLOWANCE FOR LOAN LOSSES: Each period the loan loss provision in the consolidated statements of income results from the combination of an estimate by management of probable loan losses that occurred during the current period and the ongoing adjustment of prior estimates of losses occurring in prior periods. In addition, certain regulatory agencies, as an integral part of their examination process, periodically review the Bank's allowance for loan losses for adequacy. Such agencies may require the Bank to change the allowance based on their judgment about information available to them at the time of their examination.

To serve as a basis for making this provision each quarter, the Bank maintains a risk monitoring process that considers several factors including: current economic conditions affecting the Bank's customers, the payment performance of individual large loans and pools of homogeneous small loans, portfolio seasoning, changes in collateral values, and detailed reviews of specific large loan relationships. For large loans deemed to be impaired due to an expectation that all contractual payments will probably not be received, impairment is measured by comparing the Bank's recorded investment in the loan to the present value of expected cash flows discounted at the loan's effective interest rate, the fair value of the collateral, or the loan's observable market price.

The loan loss provision increases the allowance for loan losses, a valuation account that is netted against loans on the balance sheet. As the specific customer and amount of a loan loss is confirmed by gathering additional information, taking collateral in full or partial settlement of the loan, bankruptcy of the borrower, and other factors, the loan is written down, thereby reducing the allowance for loan losses. If, subsequent to a write-down, the Bank is able to collect additional amounts from the customer or obtain control of collateral worth more than earlier estimated, a recovery is recorded, thereby increasing the allowance for loan losses.

OFFICE PROPERTIES AND EQUIPMENT: Office properties and equipment are stated at historical cost. Depreciation is computed by the straight-line method over the estimated useful lives of the assets, which range from 3 to 50 years. Leasehold improvements are amortized over the life of the asset or the term of the lease, whichever is shorter. Repairs and maintenance not extending the useful life of the asset are expensed.

MORTGAGE SERVICING RIGHTS: The Bank recognizes, as separate assets, rights to service mortgage loans for others, whether the rights are acquired through purchase or result from the sale or securitization of loans with servicing rights retained. In the case where the mortgage loan is originated and sold, the total cost of the mortgage loan is allocated to the mortgage servicing right and the loan based on their relative fair values.

The carrying amount of mortgage servicing rights, and the amortization thereon, is periodically evaluated in relation to estimated fair value. The Bank stratifies the underlying mortgage portfolio by certain risk characteristics, such as loan type, interest rate and maturity, for purposes of measuring impairment. The Bank estimates the fair value of each stratum by calculating the discounted present value of future net servicing income based on management's best estimate of remaining loan lives. The Bank has determined that the primary risk characteristic of the mortgage servicing rights is the contractual interest rate of the underlying mortgage loans.

The carrying value of mortgage servicing rights is amortized in proportion to, and over the period of, estimated net servicing revenues.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS -- Continued

PIONEER BANK AND SUBSIDIARY

NOTE A – SUMMARY OF OPERATIONS AND SIGNIFICANT ACCOUNTING POLICIES-Continued

INVESTMENTS IN REAL ESTATE: Foreclosed real estate is initially recorded at fair value upon acquisition, establishing a new cost basis. After foreclosure, real estate is carried at the lower of carrying amount or estimated fair value, less estimated selling costs, which is generally determined by an independent appraisal. Subsequent to acquisition, management periodically re-evaluates the properties and provides allowances for any differences.

DERIVATIVES: All derivative instruments are recorded at their fair values. If derivative instruments are designated as hedges of fair values, both the change in the fair value of the hedge and the hedged item are included in current earnings. Fair value adjustments related to cash flow hedges are recorded in other comprehensive income and reclassified to earnings when the hedged transaction is reflected in earnings. Ineffective portions of hedges are reflected in earnings as they occur.

The operations of the Bank are subject to risk of interest rate fluctuations to the extent there are differences between the amount of the Bank's interest-earning assets and interest-bearing liabilities that mature or reprice in specified periods. To the extent that the Bank is unable to naturally hedge its interest-earning assets and interest-earning liabilities, the Bank uses, among other strategies, interest rate cap agreements. The Bank has entered into interest rate cap agreements to reduce the impact of increases in short-term interest rates affecting deposits and short-term borrowings. The interest rate cap agreements are not for speculative purposes.

INTEREST AND FEES ON LOANS: Interest on loans is accrued and credited to income on a level yield basis. The accrual of interest on impaired loans is discontinued after the loan is 90 days past due or when in management's opinion, the borrower may be unable to meet payments as they become due. When interest accrual is discontinued, all unpaid accrued interest is reversed. Interest income is subsequently recognized only to the extent cash payments are received. Loan origination fees, net of direct origination costs, are deferred and amortized and recognized as an adjustment to the yield of the related loan. If the loan is held for sale, the loan origination fees are deferred until the loan is sold.

GAIN OR LOSS ON SALE OF LOANS AND LOAN PARTICIPATIONS: Gains and losses on sales of mortgage loans and mortgage loan participations are based on the difference between allocated amortized book value of the loans sold and sales proceeds.

INCOME TAXES: The Bank files a consolidated income tax return with its subsidiary Pioneer Mortgage Company and, as agreed, the income taxes of Pioneer Mortgage Company determined to be currently payable are remitted to the Bank. The calculation of taxes payable is based on Pioneer Mortgage Company's respective contribution to consolidated taxable income.

Deferred tax expenses or benefits result from changes in deferred tax liabilities and assets. Deferred tax liabilities and assets are recognized for the estimated future tax effects attributable to temporary differences between the basis of assets and liabilities for tax and financial statement purposes. As explained in Note I, it is not necessary to provide deferred taxes on the portion of the allowance for loan losses for tax purposes that arose in years prior to 1988. Deferred tax liabilities or assets are determined using the current marginal rate in effect at the end of each period.

NET INCOME AND DIVIDENDS PER SHARE: Net income per share of capital stock has been computed on the basis of the weighted-average number of shares of capital stock outstanding. There were no other classes of stock or common stock equivalents at December 31, 2001 or 2000. Dividends are paid based on the actual number of shares outstanding on the day of record.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS -- Continued

PIONEER BANK AND SUBSIDIARY

NOTE A – SUMMARY OF OPERATIONS AND SIGNIFICANT ACCOUNTING POLICIES-Continued

ACCOUNTING STANDARD ADOPTED: On January 1, 2001, the Bank adopted new accounting and reporting standards for derivative instruments, including certain derivative instruments embedded in other contracts, and for hedging activities. It requires that an entity recognize all derivatives as either assets or liabilities in the consolidated statements of financial position and measure those instruments at fair value and only if certain conditions are met, it may be recognized as one of three hedging designations. The accounting for changes in the fair value of a derivative depends on the intended use of the derivative and the resulting designation. Special accounting for qualifying hedges allows derivative gains and losses to offset related results on the hedged item in the income statement, and requires that a company must formally document, designate, and assess the effectiveness of transactions that receive hedge accounting. The Bank has only limited involvement with derivative financial instruments and does not use them for trading purposes. They are used to manage well-defined interest rate and price risks. Management has adopted procedures for identifying derivative instruments and hedging activities as defined and is able to report these activities appropriately. Items identified as derivatives are the interest rate cap agreements that are used to manage interest rate risk and commitments to originate loans and sell mortgages and mortgage-backed securities. These commitments are subject to valuation changes between the commitment date and the delivery date.

As a result of adopting the new standards, the Bank reduced the carrying value of its interest rate caps to fair value on January 1, 2001. The impact of this change totaled \$508,000 after taxes and is reflected as the cumulative effect on prior years of adopting SFAS 133 in the 2001 consolidated statement of income.

NEW ACCOUNTING PRONOUNCEMENTS: A new Accounting standard requires all business combinations to be recorded using the purchase method of accounting for any transaction initiated after June 30, 2001. Under the purchase method, all identifiable tangible and intangible assets and liabilities of the acquired company must be recorded at fair value at date of acquisition, and the excess of cost over fair value of net assets acquired is recorded as goodwill. Identifiable intangible assets must be separated from goodwill. Identifiable intangible assets with finite useful lives will be amortized under the new standard, whereas goodwill, both amounts previously recorded and future amounts purchased, will cease being amortized starting in 2002. Annual impairment testing will be required for goodwill with impairment being recorded if the carrying amount of goodwill exceeds its implied fair value. Adoption of this standard on January 1, 2002 will not have a material effect on the Company's financial statements.

RECLASSIFICATIONS: Certain amounts in the 2000 consolidated financial statements have been reclassified to conform to the 2001 presentation.

NOTE B - CASH AND CASH EQUIVALENTS

Cash and cash equivalents, subject to regulatory reserve requirements, totaled approximately \$3,142,000 and \$1,955,000 at December 31, 2001 and 2000, respectively. Cash and cash equivalents consisted of the following:

	December 31,	
	2001	2000
Cash and due from banks	\$ 10,959,866	\$ 9,192,125
Interest bearing deposits	208,917	3,689,194
	<u>\$ 11,168,783</u>	<u>\$ 12,881,319</u>

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS -- Continued

PIONEER BANK AND SUBSIDIARY

NOTE C - INVESTMENT AND MORTGAGE SECURITIES

The amortized cost and estimated market values of investments in debt securities are as follows. Actual maturities may differ from contractual maturities because borrowers have the right to prepay obligations without prepayment penalties.

December 31, 2001					
	Contractual Maturity in Years	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Estimated Market Value
<u>Available-for-Sale Securities</u>					
U.S. Treasury securities	< 1	\$ 500,103	\$ -	\$ 103	\$ 500,000
	1 - 5	1,009,128	28,997	-	1,038,125
Mortgage-backed securities and collateralized mortgage obligations		<u>127,998,868</u>	<u>574,151</u>	<u>429,993</u>	<u>128,143,026</u>
Total Available-for-Sale securities		\$ <u>129,508,099</u>	\$ <u>603,148</u>	\$ <u>430,096</u>	\$ <u>129,681,151</u>
<u>Held-to Maturity Securities</u>					
Mortgage-backed securities and collateralized mortgage obligations		\$ <u>1,207,185</u>	\$ <u>26,475</u>	\$ <u>-</u>	\$ <u>1,233,660</u>

December 31, 2000					
<u>Available-for-Sale Securities</u>					
U.S. Treasury securities	1 - 5	\$ 1,517,880	\$ 6,426	\$ 8,681	\$ 1,515,625
	6 - 10	1,968,306	-	22,681	1,945,625
	11 - 30	2,098,925	-	116,425	1,982,500
Mortgage-backed securities and Collateralized mortgage obligations		<u>118,093,368</u>	<u>83,950</u>	<u>1,453,695</u>	<u>116,723,623</u>
Total Available-for-Sale securities		\$ <u>123,678,479</u>	\$ <u>90,376</u>	\$ <u>1,601,482</u>	\$ <u>122,167,373</u>
<u>Held-to Maturity Securities</u>					
Mortgage-backed securities and collateralized mortgage obligations		\$ <u>7,018,254</u>	\$ <u>7,479</u>	\$ <u>146,260</u>	\$ <u>6,879,473</u>

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS -- Continued

PIONEER BANK AND SUBSIDIARY

NOTE C - INVESTMENT AND MORTGAGE SECURITIES - Continued

Effective January 1, 2001, the Company adopted the provisions of Statement of Financial Accounting Standards ("SFAS") No. 133, *Accounting for Derivative Instruments and Hedging Activities*. As permitted by SFAS No. 133, the Company reclassified certain securities held-to-maturity to securities available-for-sale. The securities which were reclassified had a book value of \$5,623,051 and a fair value of \$5,564,241 at January 1, 2001.

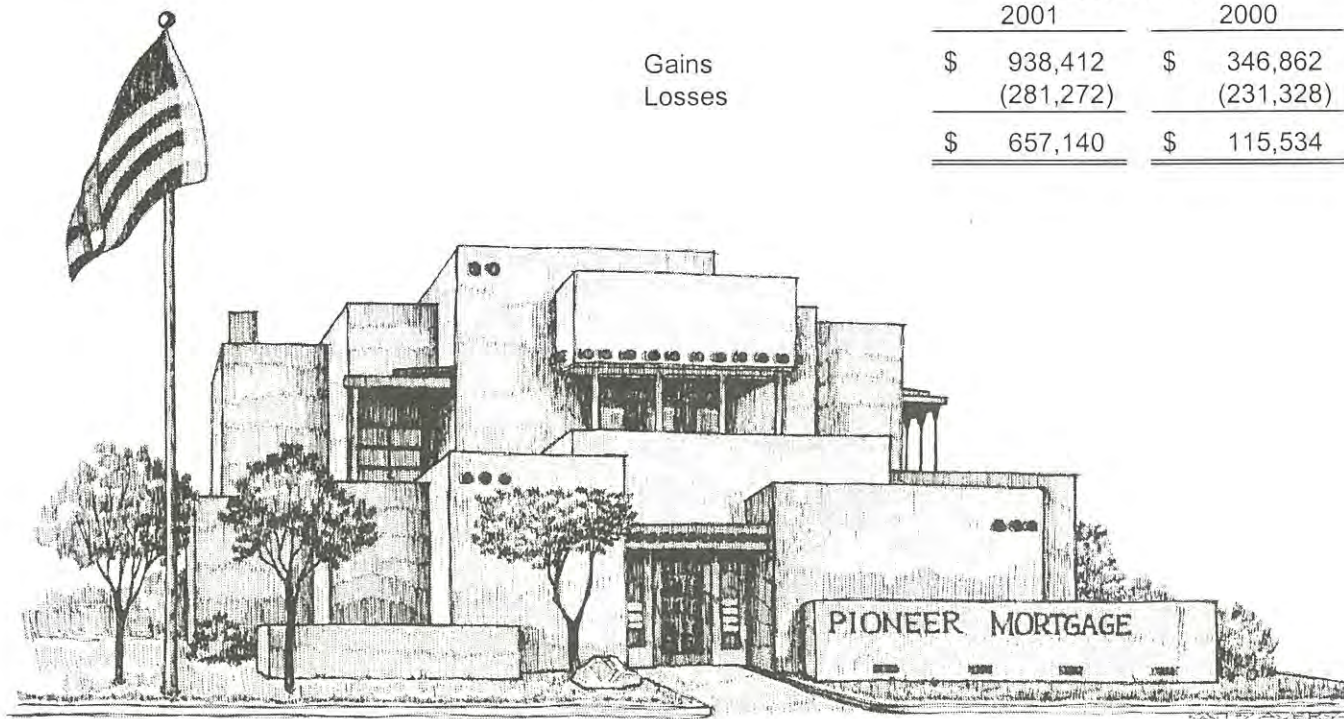
All components of accumulated other comprehensive loss for the Bank are directly related to investment securities activity. An analysis of changes in accumulated other comprehensive loss follows:

	December 31,	
	2001	2000
Net unrealized holding gains on investment securities arising during the period	\$ 2,341,298	\$ 4,201,185
Reclassification adjustment for realized gains included in net income	(657,140)	(115,534)
Income tax	(630,265)	(1,615,061)
	<u>\$ 1,053,893</u>	<u>\$ 2,470,590</u>

At December 31, 2001 and 2000, the Bank had pledged securities of approximately \$22,352,000 and \$29,411,000, respectively, to secure public unit deposits. At December 31, 2001 and 2000, securities having a par value of approximately \$500,000 and \$500,000, respectively, were pledged to secure the treasury tax and loan account.

The following table presents components of gains and losses realized on sales of available-for-sale investment securities:

	December 31,	
	2001	2000
Gains	\$ 938,412	\$ 346,862
Losses	(281,272)	(231,328)
	<u>\$ 657,140</u>	<u>\$ 115,534</u>



NOTES TO CONSOLIDATED FINANCIAL STATEMENTS -- Continued

PIONEER BANK AND SUBSIDIARY

NOTE D - LOANS

Loans consisted of the following:

	December 31,	
	2001	2000
Loans held for sale:		
Mortgage loans held for sale:		
Conventional	\$ 22,617,570	\$ 9,246,342
FHA insured and VA insured	14,498,319	6,289,084
Deferred loan (fees) costs, net	(64,114)	(25,295)
Loans held for sale, net	<u>\$ 37,051,775</u>	<u>\$ 15,510,131</u>
Loans:		
Mortgage loans held for investment:		
Conventional	\$ 93,033,501	\$ 97,778,649
FHA insured and VA guaranteed	49,386,981	62,947,275
Commercial	5,323,040	5,064,200
Construction and land	10,248,768	5,346,115
Loans in process	-	-
Deferred loan costs, net	58,312	149,309
Mortgage loans held for investment, net	<u>158,050,602</u>	<u>171,285,548</u>
Consumer loans:		
Installment and other loans	7,172,295	8,327,163
Second mortgages	867,868	683,685
Business	3,683,977	2,839,889
Savings account loans	555,945	631,307
Unearned discounts	(22,967)	(27,363)
Consumer loans, net	<u>12,257,118</u>	<u>12,454,681</u>
Allowance for loan losses	(362,476)	(397,646)
Loans, net	<u>\$ 169,945,244</u>	<u>\$ 183,342,583</u>

Net gains from sales of loans were \$2,153,093 and \$1,042,720 in 2001 and 2000, respectively.

At December 31, 2001 and 2000, approximately \$178,067,000 and \$175,724,000, respectively, of mortgage loans (including those held for sale) were pledged to secure Federal Home Loan Bank advances and other borrowings.

An analysis of the activity in the allowance for loan losses is as follows:

	December 31,	
	2001	2000
Balance at beginning of year	\$ 397,646	\$ 368,684
Recoveries	50,112	2,441
Loan loss provision	(19,315)	36,000
Charge-offs	(65,967)	(9,479)
Balance at end of year	<u>\$ 362,476</u>	<u>\$ 397,646</u>

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS -- Continued

PIONEER BANK AND SUBSIDIARY

NOTE D – LOANS - Continued

Recorded investments in impaired loans totaled approximately \$1,187,000 and \$1,243,000 at December 31, 2001 and 2000, respectively. Based on management analysis, there were no other impaired loans as of December 31, 2001 or 2000. The average recorded investment in impaired loans for the years ended December 31, 2001 and 2000 was \$1,213,000 and \$1,365,000, respectively. Management determined that a valuation allowance for impaired loans is not required as the collateral value of the impaired loans exceeded the Bank's recorded investment. The Bank had no outstanding commitments to lend additional funds to debtors with impaired loans.

Interest income that would have been recorded under the original terms of such loans and the interest income actually recognized are summarized below:

	December 31,	
	2001	2000
Interest income recognized	\$ 14,518,276	\$ 15,532,833
Interest income that would have been recorded	14,540,311	15,549,198
Interest income foregone, net	<u>\$ (22,035)</u>	<u>\$ (16,365)</u>

NOTE E - OFFICE PROPERTIES AND EQUIPMENT

Office properties and equipment consisted of:

	December 31,	
	2001	2000
Land	\$ 2,011,829	\$ 1,382,017
Buildings and leasehold improvements	4,416,925	4,051,819
Furniture, equipment and autos	3,796,092	3,065,873
Construction in progress	1,892	234,579
	<u>10,226,738</u>	<u>8,734,288</u>
Less accumulated depreciation	<u>(3,892,757)</u>	<u>(3,427,809)</u>
Office properties and equipment, net	<u>\$ 6,333,981</u>	<u>\$ 5,306,479</u>

The Bank leases office space for administrative offices and certain branch offices under various operating leases with terms ranging through 2004. Lease payments included in occupancy expense totaled \$219,148 and \$218,894 for the years ended December 31, 2001 and 2000, respectively. Future minimum lease payments under the non-cancelable operating leases are:

2002	\$ 218,392
2003	217,022
2004	<u>52,910</u>
	<u>\$ 488,324</u>

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS -- Continued

PIONEER BANK AND SUBSIDIARY

NOTE F - MORTGAGE SERVICING RIGHTS AND LOAN SERVICING

Mortgage loans serviced for others are not included in the accompanying consolidated statements of financial condition. The unpaid principal balances of these loans are:

	December 31,	
	2001	2000
Mortgage loans underlying pass-through securities:		
GNMA	\$ 140,811,497	\$ 124,925,863
FNMA	70,894,290	56,327,566
FHLMC	1,012,142	1,394,250
	<u>212,717,929</u>	<u>182,647,679</u>
Mortgage loan portfolios serviced for:		
FNMA	77,704,280	83,607,186
FHLMC	44,629,217	56,026,869
Other investors	26,169,327	18,991,993
	<u>148,502,824</u>	<u>158,626,048</u>
	<u>\$ 361,220,753</u>	<u>\$ 341,273,727</u>

Custodial balances on deposit at the Bank, in connection with the foregoing loan servicing, amounted to \$10,149,482 and \$9,476,535 at December 31, 2001 and 2000, respectively.

An analysis of changes in mortgage servicing rights follows:

	December 31,	
	2001	2000
Balance, beginning of year	\$ 3,154,595	\$ 3,182,473
Capitalized	1,261,666	396,588
Amortization	(757,044)	(424,513)
Change in impairment allowance	(448,715)	47
Balance, end of year	<u>\$ 3,210,502</u>	<u>\$ 3,154,595</u>

NOTE G - DEPOSITS

A comparative summary of deposits by term to maturity follows:

	December 31,	
	2001	2000
No contractual maturities	\$ 120,738,462	\$ 105,289,023
Under 12 months	95,750,117	114,551,961
13 months to 24 months	11,704,144	13,496,238
25 months to 36 months	2,516,742	4,660,313
37 months to 48 months	4,575,432	1,590,181
49 months to 60 months	2,474,965	4,437,152
	<u>\$ 237,759,862</u>	<u>\$ 244,024,868</u>

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS -- Continued

PIONEER BANK AND SUBSIDIARY

NOTE G – DEPOSITS - Continued

At December 31, 2001 and 2000, approximately \$22,352,000 and \$29,411,000, respectively, of mortgage securities were pledged to secure public unit deposits.

Time deposits of \$100,000 or more were \$36,281,000 and \$51,871,000 at year-end 2001 and 2000.

NOTE H - FEDERAL HOME LOAN BANK ADVANCES AND OTHER BORROWINGS

FHLB advances and other borrowings consist of fixed rate, fixed term advances that must be secured by mortgage loans or other assets acceptable to the FHLB. At December 31, 2001 and 2000, the Bank's advances were secured by a blanket assignment of mortgage loans with a market value greater than the amount of outstanding advances. At December 31, 2001 and 2000, securities of approximately \$500,000 and \$500,000, respectively, and mortgage loans of approximately \$178,067,000 and \$175,724,000, respectively, were pledged to secure FHLB advances and other borrowings. A summary of FHLB advances and other borrowings follows:

	Maturity Date	Rate	December 31,	
			2001	2000
FHLB Advances and Borrowings	1-02-01	6.430%	-	\$ 55,600,000
	9-03-01	5.130%	-	1,667,000
	1-02-02	2.030%	\$ 10,600,000	-
	1-07-02	1.950%	10,600,000	-
	9-01-03	5.440%	22,000,000	22,000,000
	4-19-04	5.100%	10,000,000	-
	4-20-04	5.185%	5,000,000	-
	5-20-04	3.566%	10,000,000	-
	1-17-05	5.710%	5,000,000	5,000,000
	1-26-05	5.510%	2,481,900	2,481,900
	4-19-05	5.272%	10,000,000	-
	4-10-06	5.249%	14,000,000	-
Treasury, Tax and Loan			114,843	146,792
			<u>\$ 99,796,743</u>	<u>\$ 86,895,692</u>

NOTE I - INCOME TAXES

The Bank records tax expense equal to the sum of deferred tax expense and income taxes currently payable or refundable. Total income tax expense in the accompanying consolidated statements of income are:

	December 31,	
	2001	2000
Current:		
Federal	\$ 2,184,034	\$ 1,232,204
State	459,119	76,522
Deferred:		
Federal	(479,178)	(8,681)
State	(116,000)	(1,412)
	<u>\$ 2,047,975</u>	<u>\$ 1,298,633</u>

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS -- Continued

PIONEER BANK AND SUBSIDIARY

NOTE I - INCOME TAXES - Continued

The differences between total tax expense and the amount computed by applying the applicable statutory federal income tax rate of 34% to income before income taxes were:

	December 31,	
	2001	2000
Computed "expected" tax expense	\$ 1,839,382	\$ 1,302,232
State income taxes	225,515	49,573
Other	(16,922)	(53,172)
	<u>\$ 2,047,975</u>	<u>\$ 1,298,633</u>

Deferred taxes are attributable to temporary differences, such as the use of accelerated depreciation methods for tax purposes, the excess of the allowance for loan losses for financial reporting purposes over the amount for tax purposes which arose after 1987, the exclusion from taxable income for certain stock dividends, the recognition of unrealized gains and losses on securities for tax purposes, the deduction of loan origination costs for tax purposes and the deferral of deductions for accrued liabilities under the Bank's medical and dental benefit plan. Certain unrealized gains and losses on available-for-sale securities, which are deferred for financial statement reporting purposes, are recognized currently for income tax purposes. Deferred taxes consisted of:

	December 31,	
	2001	2000
Deferred tax assets	\$ 803,087	\$ 478,548
Deferred tax liabilities	(2,468,498)	(2,441,819)
	<u>\$ (1,665,411)</u>	<u>\$ (1,963,271)</u>

The Bank has not recorded a valuation allowance with respect to the deferred tax assets because it is anticipated that the assets are fully realizable.

As of January 1, 1996, Internal Revenue Code (IRC) Section 593, which allowed thrifts an 8% taxable income deduction for bad debts, was repealed. The Bank is required to recapture, over a six-year period, its bad debt reserve into income to the extent its reserve at December 31, 1995 exceeded its reserve recalculated without regard to IRC Section 593. As of December 31, 1995, the amount to be recaptured totaled \$679,379, for which a deferred tax liability had been recorded. The recapture was deferred for two years based upon the Bank's residential loan portfolio growth. In 1998 the bank began recapturing approximately \$113,000 of its bad debt reserves per year and as of December 31, 2001 the total amount recaptured was approximately \$452,000.

The permanent deferral of bad debt reserves prior to 1988 was not affected by the repeal of Section 593. The Bank's allowance for loan losses for tax purposes for which no deferred tax liability has been recognized and the corresponding unrecognized deferred tax liability, are \$1,597,000 and \$613,000, respectively as of December 31, 2001. Deferred tax liabilities are recognized for this temporary difference only if it is apparent that it will reverse and become taxable in the foreseeable future. This difference could become taxable in the future if the Bank fails to meet the definition of a qualifying financial institution for tax purposes, or if distributions are made to stockholders in excess of accumulated earnings for tax purposes. Management does not anticipate that any event resulting in the reversal of this difference will occur.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS -- Continued

PIONEER BANK AND SUBSIDIARY

NOTE J - REGULATORY MATTERS

The Bank is subject to certain restrictions on the amount of dividends it may declare without prior regulatory approval. The Bank is also subject to various regulatory capital requirements administered by the federal banking agencies. Failure to meet minimum capital requirements can initiate certain mandatory and possibly additional discretionary actions by regulators that, if undertaken, could have a direct material effect on the Bank's financial statements. Under capital adequacy guidelines and the regulatory framework for prompt corrective action, the Bank must meet specific capital guidelines that involve quantitative measures of its assets, liabilities, and certain off-balance sheet items as calculated under regulatory accounting practices. The capital amounts and classification are also subject to qualitative judgments by the regulators about components, risk-weightings and other factors.

Quantitative measures established by regulation to ensure capital adequacy require the Bank to maintain minimum amounts and ratios of Total and Tier 1 Capital (as defined by regulation) to Risk-Weighted Assets (as defined), and Core Capital (as defined) to Adjusted Total Assets (as defined). Management believes, as of December 31, 2001 and 2000 that the Bank met all regulatory capital adequacy requirements to which it is subject.

The most recent notifications from the OTS as of December 31, 2001 and 2000 categorized the Bank as well capitalized under the regulatory framework for prompt corrective action. To be categorized as well capitalized, the Bank must maintain minimum Total risk-based, Tier 1 risk-based, Tier 1 core and Tangible Capital ratios as set forth in the table. There are no conditions or events since that notification that management believes have changed the institution's category. The Bank's actual capital amounts and ratios are also presented in the table:

	Actual (\$ in thousands)		Amount Needed To Be Considered Adequately Capitalized (\$ in thousands)		Amount Needed To Be Considered Well Capitalized Under Prompt Corrective Action (\$ in thousands)	
	Amount	Ratio	Amount	Ratio	Amount	Ratio
As of December 31, 2001:						
Total Risk-Based Capital (to Risk-Weighted Assets)	\$ 25,582	19.3%	\$ 10,591	8.0%	\$ 13,239	10.0%
Tier 1 Risk-Based Capital (to Risk-Weighted Assets)	\$ 25,219	19.1%	\$ 5,296	4.0%	\$ 7,943	6.0%
Core Capital (to Adjusted Total Assets)	\$ 25,219	6.8%	\$ 14,912	4.0%	\$ 18,640	5.0%
As of December 31, 2000:						
Total Risk-Based Capital (to Risk-Weighted Assets)	\$ 23,625	18.9%	\$ 9,986	8.0%	\$ 12,483	10.0%
Tier 1 Risk-Based Capital (to Risk-Weighted Assets)	\$ 23,284	18.6%	\$ 4,993	4.0%	\$ 7,490	6.0%
Core Capital (to Adjusted Total Assets)	\$ 23,414	6.4%	\$ 14,556	4.0%	\$ 18,196	5.0%

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS -- Continued

PIONEER BANK AND SUBSIDIARY

NOTE K - COMMITMENTS AND CONTINGENCIES

In the ordinary course of business, the Bank may become a party to certain claims and legal actions. In the opinion of management, after consultation with legal counsel, the ultimate disposition of these matters is not expected to have a material effect on the consolidated financial condition of the Bank.

Also, the Bank has various outstanding commitments and contingent assets and liabilities that are not reflected in the accompanying consolidated financial statements. Those financial instruments with off-balance sheet risk are used to meet the financial needs of the Bank's customers and include commitments to extend credit and standby letters of credit. They involve, to varying degrees, elements of credit and interest-rate risk in excess of the amount recognized in the consolidated statements of financial condition. The contract or notional amounts of those instruments reflect the extent of involvement the Bank has in particular classes of financial instruments.

The Bank's exposure to credit loss in the event of nonperformance by the other party to the financial instrument for commitments to extend credit and standby letters of credit is represented by the contractual notional amount of those instruments. The Bank uses the same credit policies in making commitments and conditional obligations as it does for on-balance sheet instruments. The approximate contract or notional amounts of financial instruments whose contract amounts represent credit risk at December 31, 2001 are:

Undisbursed lines of credit and loans in process	\$ 9,362,000
Commitments to originate loans	\$ 2,915,000
Loans sold with recourse	\$ 122,000
Commitments to purchase loans	\$ 1,089,000
Commitments to sell mortgages and mortgage backed securities	\$ 12,340,000

Commitments to extend credit are agreements to lend to a customer as long as there is no violation of any condition established in the contract. Commitments generally have fixed expiration dates or other termination clauses and may require payment of a fee. At December 31, 2001, commitments to make loans at fixed rates totaled \$2,895,000. The fixed rate commitments have interest rates ranging from 7.00% to 8.50%.



Ruidoso

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS -- Continued

PIONEER BANK AND SUBSIDIARY

NOTE L - FAIR VALUE OF FINANCIAL INSTRUMENTS

Carrying amounts and estimated fair values of financial instruments were as follows at year-end.

	<u>2001</u>		<u>2000</u>	
	<u>Carrying Amount</u>	<u>Fair Value</u>	<u>Carrying Amount</u>	<u>Fair Value</u>
Financial Assets				
Cash and cash equivalents	\$ 11,168,783	\$ 11,168,783	\$ 12,881,319	\$ 12,881,319
Securities available for sale	129,681,151	129,681,151	122,167,373	122,167,373
Securities held to maturity	1,207,185	1,233,660	7,018,254	6,879,473
Loans held for sale	37,015,775	37,655,793	15,510,131	15,522,053
Loans, net	169,945,244	172,534,962	183,342,583	181,879,352
Federal Home Loan Bank and FNMA stock	8,483,700	8,483,700	7,067,784	7,067,784
Mortgage servicing rights	3,210,502	3,962,600	3,154,595	4,464,672
Accrued interest receivable	1,557,152	1,557,152	1,730,573	1,730,573
Interest rate cap agreements	271,547	271,547	1,666,934	825,987
Financial Liabilities				
Deposits	237,759,862	238,515,654	244,024,868	243,984,926
Federal Home Loan Bank advances	99,796,743	101,511,425	86,895,692	86,516,758
Advance payments for taxes and insurance	1,563,368	1,563,368	1,452,898	1,452,898
Accrued interest payable	545,481	545,481	753,850	753,850

The methods and assumptions used to estimate fair value are described as follows.

Carrying amount is the estimated fair value for cash and cash equivalents, short-term borrowings, Federal Home Loan Bank stock, accrued interest receivable and payable, demand deposits, short-term debt, and variable rate loans or deposits that reprice frequently and fully. Security fair values are based on market prices or dealer quotes, and if no such information is available, on the rate and term of the security and information about the issuer. For fixed rate loans or deposits and for variable rate loans or deposits with infrequent repricing or repricing limits, fair value is based on discounted cash flows using current market rates applied to the estimated life and credit risk. Fair values for impaired loans are estimated using discounted cash flow analysis or underlying collateral values. Fair value of loans held for sale is based on market quotes. Fair value of debt is based on current rates for similar financing. The fair value of commitments is based on the current fees or cost that would be charged to enter into or terminate such arrangements. The fair value of commitments is not materially different from the nominal value.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS -- Continued

PIONEER BANK AND SUBSIDIARY

NOTE M - RETIREMENT PLANS

The Bank has a qualified 401(k) retirement savings plan for employees. Matching contributions are optional at the discretion of the Board of Directors. The level of matching contributions made by the Bank to eligible employee compensation and plan expenses, included in compensation and employee benefits in the accompanying consolidated statements of income, were as follows for 2001 and 2000:

Year	Match	Compensation	Expense
2001	100%	5.0%	\$ 97,696
2000	100%	5.0%	\$ 98,817

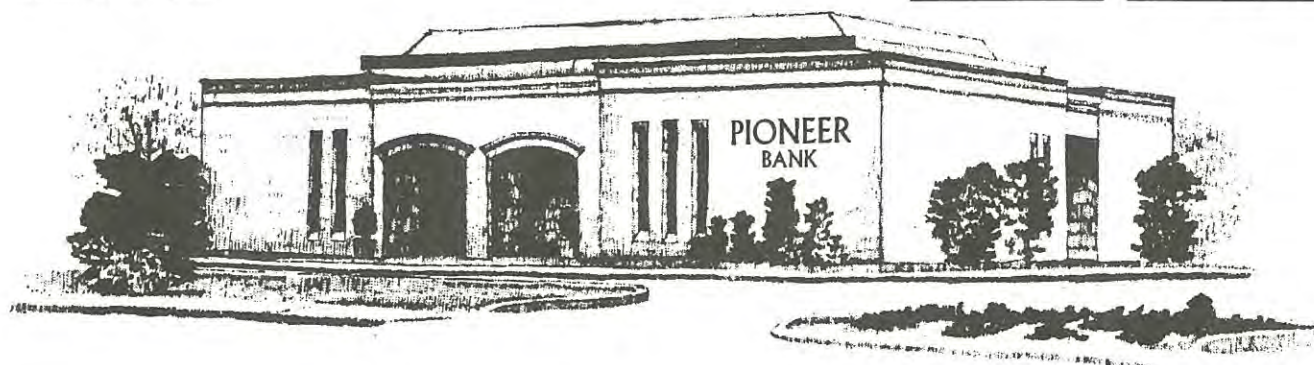
The Bank maintains a non-qualified retirement plan (hereinafter referred to as an Indexed Retirement Plan or "IRP") for certain key executive officers. At the time the IRP was established, the Bank purchased single premium life insurance policies having a total face value of \$800,000 on the lives of the participants. A death benefit for each executive has also been provided by endorsement of 80% of the non-at-risk insurance proceeds. Benefits are accrued under this plan to the extent that policy earnings exceed a cost of funds index tied to the Bank's cost of funds. The Bank has accrued benefits of \$241,060 and \$172,720, recorded in other liabilities, as of December 31, 2001 and 2000, respectively, under the IRP. As of December 31, 2001 and 2000, the cash surrender value of the life insurance policies under the IRP were approximately \$1,130,000 and \$1,082,000, respectively which are recorded in other assets.

NOTE N - RELATED PARTY TRANSACTIONS

It is the policy of the Bank to provide mortgage loans made in the ordinary course of business to its full-time officers and employees for the purpose of financing their personal residences. Any other loans made by the Bank to directors or officers are fully secured and are made in the ordinary course of business. All loans are made on the same terms, including interest rates and collateral, as those prevailing at the time for comparable transactions with other persons and none of the loans involve more than normal risk of collection or present other features unfavorable to the Bank.

An analysis of loans over \$60,000 to directors and executive officers is:

	Years Ended December 31,	
	2001	2000
Balance at beginning of year	\$ 273,341	\$ 283,110
Principal repayments	(209,631)	(9,769)
Balance at end of year	\$ 63,710	\$ 273,341



Alamogordo

REPORT OF INDEPENDENT PUBLIC ACCOUNTANTS

PIONEER BANK AND SUBSIDIARY



Board of Directors and Stockholders
Pioneer Bank and Subsidiary
Roswell, New Mexico

We have audited the accompanying consolidated statement of financial condition of Pioneer Bank and Subsidiary as of December 31, 2001 and the related consolidated statements of income, cash flows, and stockholders' equity for the year then ended. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audit. The 2000 financial statements of the Company were audited by other auditors whose report dated February 16, 2001 expressed an unqualified opinion on those financial statements.

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

In our opinion, the 2001 consolidated financial statements referred to above present fairly, in all material respects, the financial position of Pioneer Bank and Subsidiary as of December 31, 2001 and the results of their operations and their cash flows for the year then ended in conformity with accounting principles generally accepted in the United States of America.

As disclosed in Note A, during 2001 the Company adopted new accounting guidance on derivatives.



Crowe, Chizek and Company LLP

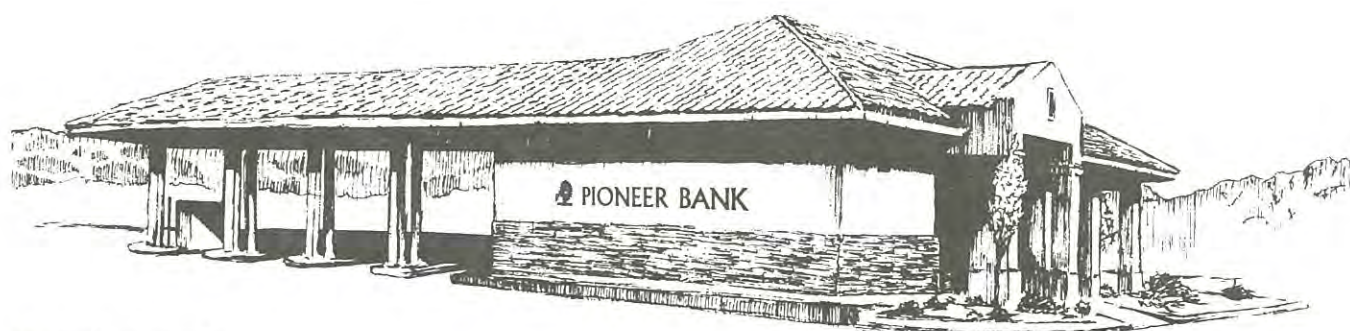
Oak Brook, Illinois
February 22, 2002

SELECTED FINANCIAL DATA -- Unaudited

PIONEER BANK AND SUBSIDIARY

The following table sets forth selected financial data for the last five years:

	2001	2000	1999	1998	1997
Interest income	\$ 22,655,953	\$ 22,765,151	\$ 22,063,276	\$ 18,330,476	\$ 17,514,029
Interest expense	13,893,529	15,476,093	13,633,862	11,150,099	10,684,399
Net interest income	8,762,424	7,289,058	8,429,414	7,180,377	6,829,630
Net income	3,869,972	2,531,461	2,808,132	3,601,198	3,386,211
Per share data:					
Net income	3.84	2.51	2.78	3.57	3.36
Dividends	1.05	1.05	1.10	1.15	1.05
Investment and mortgage securities	130,888,336	129,185,627	103,717,275	97,184,550	84,033,754
Loans	206,997,019	198,852,714	206,262,488	189,797,230	130,978,713
Total assets	372,901,648	362,962,161	341,548,512	312,175,994	238,503,512
Deposits	237,759,862	244,024,868	255,020,073	225,022,207	183,126,824
Borrowings	99,796,743	86,895,692	59,938,707	57,513,179	30,802,500
Stockholders' equity	26,339,804	22,464,980	18,521,823	20,068,720	17,741,082
Loans serviced for others	361,220,753	341,273,727	359,062,606	388,960,563	445,211,292
	2001	2000	1999	1998	1997
Customer service facilities:					
Full service facilities	6	6	6	6	6
Banking branches	3	2	2	2	-
Loan production offices	2	2	2	2	3



New Las Cruces Branch

SELECTED FINANCIAL DATA -- Unaudited

PIONEER BANK AND SUBSIDIARY

VOLUME AND RATE ANALYSIS (000's OMITTED)

2001 Compared to 2000:

	Average Balance		Average Rate		Interest		Interest Variance	Interest Variance Attributable to:	
	2001	2000	2001	2000	2001	2000		Volume	Rate
Interest income:									
Loans.....	\$ 194,785	\$ 205,729	7.45%	7.55%	\$ 14,518	\$ 15,533	\$ (1,015)	\$ (816)	\$ (199)
Mortgage securities.....	133,804	97,666	5.89%	6.37%	7,880	6,226	1,654	2,128	(474)
Investments.....	5,324	16,436	4.85%	6.12%	258	1,006	(748)	(538)	(210)
Total interest earning assets.....	<u>\$ 333,913</u>	<u>\$ 319,831</u>	<u>6.79%</u>	<u>7.12%</u>	<u>\$ 22,656</u>	<u>\$ 22,765</u>	<u>\$ (109)</u>	<u>\$ 774</u>	<u>\$ (883)</u>
Interest expenses:									
Deposits.....	\$ 236,522	\$ 245,203	3.62%	4.42%	\$ 8,572	\$ 10,827	\$ (2,255)	\$ (315)	\$ (1,940)
Borrowed funds.....	95,011	73,908	5.60%	6.29%	5,322	4,649	673	1,182	(509)
Total interest bearing liabilities.....	<u>\$ 331,533</u>	<u>\$ 319,111</u>	<u>4.19%</u>	<u>4.85%</u>	<u>\$ 13,894</u>	<u>\$ 15,476</u>	<u>\$ (1,582)</u>	<u>\$ 867</u>	<u>\$ (2,449)</u>
Net interest spread and income.....			<u>2.58%</u>	<u>2.27%</u>	<u>\$ 8,762</u>	<u>\$ 7,289</u>			
Ratio of net interest income to average interest earnings assets.....					<u>2.68%</u>	<u>2.29%</u>			

2000 Compared to 1999:

	Average Balance		Average Rate		Interest		Interest Variance	Interest Variance Attributable to:	
	2000	1999	2000	1999	2000	1999		Volume	Rate
Interest income:									
Loans.....	\$ 205,729	\$ 205,315	7.55%	7.45%	\$ 15,533	\$ 15,286	\$ 247	\$ 31	\$ 216
Mortgage securities.....	97,666	102,735	6.37%	6.15%	6,226	6,315	(89)	(323)	234
Investments.....	16,436	8,722	6.12%	5.30%	1,006	462	544	472	72
Total interest earning assets.....	<u>\$ 319,831</u>	<u>\$ 316,772</u>	<u>7.12%</u>	<u>6.96%</u>	<u>\$ 22,765</u>	<u>\$ 22,063</u>	<u>\$ 702</u>	<u>\$ 180</u>	<u>\$ 522</u>
Interest expenses:									
Deposits.....	\$ 245,203	\$ 240,027	4.42%	4.01%	\$ 10,827	\$ 9,625	\$ 1,202	\$ 229	\$ 973
Borrowed funds.....	73,908	74,440	6.29%	5.39%	4,649	4,009	640	(33)	673
Total interest bearing liabilities.....	<u>\$ 319,111</u>	<u>\$ 314,467</u>	<u>4.85%</u>	<u>4.34%</u>	<u>\$ 15,476</u>	<u>\$ 13,634</u>	<u>\$ 1,842</u>	<u>\$ 196</u>	<u>\$ 1,646</u>
Net interest spread and income.....			<u>2.27%</u>	<u>2.63%</u>	<u>\$ 7,289</u>	<u>\$ 8,429</u>			
Ratio of net interest income to average interest earnings assets.....					<u>2.29%</u>	<u>2.97%</u>			

CORPORATE INFORMATION

PIONEER BANK AND SUBSIDIARY

GENERAL INFORMATION

Pioneer Bank is a federally chartered stock savings bank. The Bank's deposits are insured by the Federal Deposit Insurance Corporation through the Savings Association Insurance Fund. The principal business of the Bank is to finance the purchase, construction or improvements of residential real estate.

The Bank has one subsidiary, Pioneer Mortgage Company, which is involved in residential construction and mortgage lending, primarily in West Texas.

CORPORATE OFFICES

Pioneer Bank
306 North Pennsylvania
P.O. Box 130
Roswell, NM 88202-0130

INDEPENDENT PUBLIC ACCOUNTANTS

Crowe, Chizek and Company LLP
One Mid America Plaza
P.O. Box 3697
Oak Brook, IL 60522-3697

GENERAL COUNSEL

Sanders, Bruin, Coll & Worley, P.A.
701 W Country Club Rd.
Roswell, NM 88201

REGISTRAR AND TRANSFER AGENT

Pioneer Bank

ANNUAL MEETING

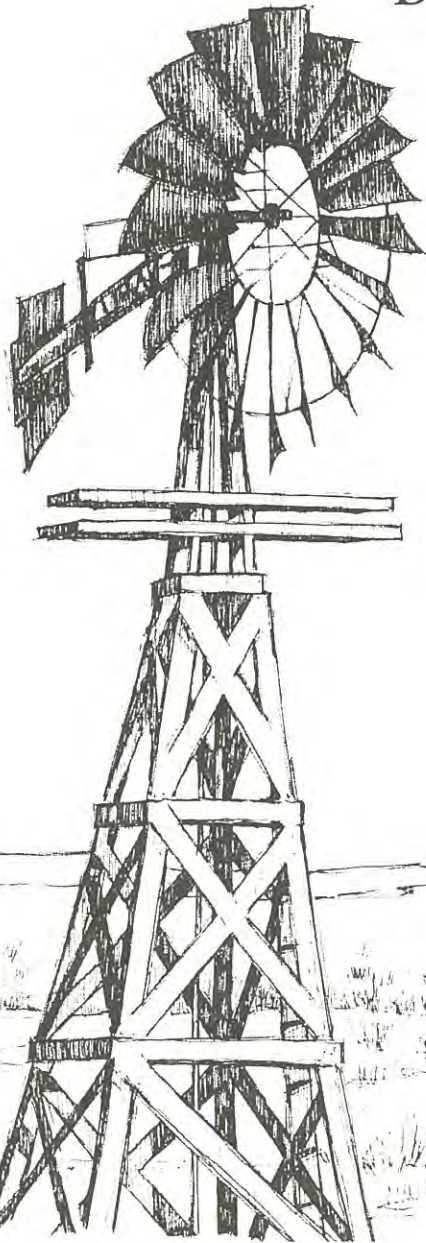
The annual meeting of shareholders of Pioneer Bank will be held at 2:00 P.M. on April 16, 2002 at the Sally Port Inn, 2000 North Main, Roswell, New Mexico.

MARKET FOR CAPITAL STOCK

The capital stock of Pioneer Bank is not traded on any exchange nor is there a market maker in the stock. The market for the stock is limited and sporadic. There are no accurate quarterly high bid and low bid quotations available; accordingly, such bid information by quarter is not shown. Recent trade issued and outstanding stock have ranged from \$20.00 to \$24.25 per share. As of December 31, 2001, there were approximately 350 holders of record of Pioneer capital stock. Dividends of \$1.05 per share were declared in 2001 and 2000.

PIONEER BANK

1901 - 2001



Between 1869 and 1891 Roswell grew from a small adobe trading post to a prosperous cattle town. In 1891 the town of Roswell was incorporated under the leadership of Captain Joseph C. Lea, a former Confederate officer. After 1895, Roswell grew rapidly, creating a need for capital to finance home construction.

In 1899 a group of citizens developed a plan to create a building and loan association. On February 19, 1901, Pioneer Bank was organized as "Roswell Building & Loan Association." D. S. Rosenwald was unanimously elected as President of the association during the first meeting of the Board of Directors. The Board then elected W. T. Jones as Vice President, J. M. Hervey as Secretary, and L. K. McGaffey as Treasurer. Nathan Jaffa, George Bixby, L. W. Martin, E. A. Cahoon, E. P. Rasmussen, Charles W. Haynes and W. T. Jones were elected as Directors.

The capital goal had originally been set at \$100,000, however, by September 1, 1901, the founders had raised \$200,000. During the 20th century steady progress and success allowed the bank to add branches throughout Southern New Mexico and establish Pioneer Mortgage Company in West Texas. In July 1976, Pioneer converted from a mutual association to a stock association, issuing common stock. On April 18, 2000 a name change to Pioneer Bank was adopted in order to reflect the full range of banking services offered to Pioneer's communities. By the end of 2001, the original capital raised 100 years ago had grown to over \$25.3 million.

Over the years, Pioneer employees have worked with enthusiastic dedication and determination to honor the integrity and goals of the original founders—a persistence and devotion that Pioneer Bank will continue into the future.

PIONEER BANK

Proud of Our Products and Services

- NOW Checking
- Super NOW Checking
- 55+ Checking
- No Frills Checking
- Free Checking
- Commercial Checking
- Savings Accounts
- Super Savings Accounts
- Money Market Accounts
- Certificates of Deposit
- Easy Access CD
- IRA Accounts
- Mortgage Loans
- Business Loans
- Consumer Loans
- 24-Hour Banking Services Line
(800) 375-1088
- Internet Banking
www.pioneerbnk.com

BOARD OF DIRECTORS

PIONEER BANK AND SUBSIDIARY

G. Eugene Bell

Vice President – Bell Gas

Jon E. Hitchcock

Executive Vice President & Treasurer -
Pioneer Bank

James L. Bruin

Attorney

Timothy Z. Jennings

State Senator & Rancher

Patricia J. Cooper

Investments

Arthur R. McQuiddy

President – McQuiddy Communications & Energy, Inc.

Dan P. Funchess

Director – Owner
Denton-Funchess Funeral Home

George W. Mitchell

President – Pioneer Bank

James D. Harris

Owner – Charles Garland and Harris
Agency

C.W. Ritter

President – Ritter Enterprises, Inc.

OFFICERS

Pioneer Bank

President & Chief Executive Officer

Chairman of the Board

George W. Mitchell

Vice President

John Dick-Peddie
Suzi K. Glass
Daniel A. Hostetler
Alan W. Johnson
Susan F. Keohane
Robert W. Mays
Scott E. Mohrhauser
Dee Ann Nunez
Rosalyn Robinson
Rebecca E. Underation
Robert D. Vie
Mike Vineyard
Debe M. Wagner

**Executive Vice President
& Treasurer**

Jon E. Hitchcock, C.P.A.

Senior Vice President

Britt Donaldson
Stephen P. Puntch

Secretary

Barba N. McCampbell

Assistant Treasurer

Pamela D. McClain

Assistant Vice President

Patricia M. Barresi
Charlotte Y. Gipson
Jennifer Scheller
Nancy L. Smith
Debra M. Young

Assistant VP & Controller

Gayla I. Morris

Assistant Secretary

Anna K. Ritchey
Jessica L. Rodriguez
Dawn L. Selter
Kendall Tomlinson

Pioneer Mortgage Company

Vice President

Freida J. Goodrum
Pamela A. Sparks

PIONEER BANK

306 North Pennsylvania Avenue, P.O. Box 130, Roswell, New Mexico 88201
300 South Sunset Avenue, Roswell, New Mexico 88203
3301 North Main Street, Roswell, New Mexico 88201
(505) 624-5200

1095 Mechem Drive, P.O. Box 910, Ruidoso, New Mexico 88345
(505) 258-5858

1020 10th Street, P.O. Box 1707, Alamogordo, New Mexico 88310
(505) 437- 9075

111 North Canal Street, P.O. Box S, Carlsbad, New Mexico 88220
(505) 887-6551

1020 North Turner Street, P.O. Box 177, Hobbs, New Mexico 88240
(505) 393-2102

1155 South Telshor Boulevard - Suite 100, P.O. Box 609, Las Cruces, New Mexico 88004
(505) 522-3300

2900 Roadrunner Parkway, P.O. Box 609, Las Cruces, New Mexico 88011
(505) 532-0639

PIONEER MORTGAGE COMPANY

6068 Gateway East, El Paso, Texas 79905
(915) 778-4100

3000 North Garfield Street - Suite 180, Midland, Texas 79705
(915) 570-0777

