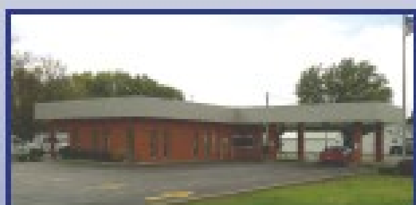
First National Bank



First Bancshares, Inc. | Bellevue, Ohio

2019 Annual Report

First Bancshares, Inc.

Bellevue, Ohio

First Bancshares, Inc. is a one-bank holding company. Its principal subsidiary, First National Bank, is a full-service bank with offices in Bellevue, Catawba, Clyde, Fremont, Port Clinton, Put-in-Bay and Sandusky, Ohio.

The Annual Meeting
of Shareholders of

First Bancshares, Inc.

will be held
Wednesday, April 29, 2020
2:00 P.M.
at
First National Bank
120 North Street
Bellevue, Ohio

First Bancshares, Inc. ~ ~ A Great Investment

Dividend Reinvestment Program

This program was adopted in 2012 to allow First Bancshares, Inc. investors the opportunity to direct their dividend payments each quarter to purchase additional shares.

The program is available to all shareholders with open enrollment at any time.

First Bancshares, Inc.
Dividend History

Holding Company Stock Issued - 5/31/1983

	1983	1984	1985	1986	1987	1988	1989	1990	1991	1992	1993	1994
4th Quarter	$0.00	$0.00	$0.00	$0.00	$0.00	$0.00	$0.40	$0.40	$0.40	$0.40	$0.40	$0.50
Stock Split: 2-for-1, effective 5/31/83												
1st Quarter	0.00	0.625	0.70	0.75	0.75	0.75	0.40	0.40	0.40	0.40	0.40	0.50
2nd Quarter	0.525	0.00	0.00	0.00	0.00	0.40	0.45	0.45	0.45	0.50	0.60	0.60
3rd Quarter	0.525	0.625	0.75	0.80	0.85	0.45	0.45	0.45	0.55	0.65	0.75	0.60
Subtotal	**$1.05**	**$1.25**	**$1.45**	**$1.55**	**$1.60**	**$1.60**	**$1.70**	**$1.70**	**$1.80**	**$1.95**	**$2.15**	**$2.20**
Extra Dividend	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00
Total Cash Dividend	**$1.05**	**$1.25**	**$1.45**	**$1.55**	**$1.60**	**$1.60**	**$1.70**	**$1.70**	**$1.80**	**$1.95**	**$2.15**	**$2.20**

	1995	1996	1997	1998	1999	2000	2001	2002	2003	2004	2005	2006
4th Quarter	$0.55	$0.60	$0.65	$0.70	$0.75	$0.55	$0.55	$0.60	$0.60	$0.60	$0.70	$0.70
			Stock Split: 2-for-1, effective 2/1/99									
1st Quarter	0.55	0.60	0.65	0.70	0.40	0.55	0.60	0.60	0.60	0.60	0.70	0.70
2nd Quarter	0.55	0.60	0.65	0.70	0.40	0.55	0.60	0.60	0.60	0.60	0.70	0.50
3rd Quarter	0.55	0.60	0.65	0.70	0.40	0.55	0.60	0.60	0.60	0.60	0.70	0.50
Subtotal	**$2.20**	**$2.40**	**$2.60**	**$2.80**	**$1.95**	**$2.20**	**$2.35**	**$2.40**	**$2.40**	**$2.40**	**$2.80**	**$2.40**
Extra Dividend	0.10	0.25	0.20	0.20	0.20	0.20	0.20	0.20	0.20	0.30	0.20	0.00
Total Cash Dividend	**$2.30**	**$2.65**	**$2.80**	**$3.00**	**$2.15**	**$2.40**	**$2.55**	**$2.60**	**$2.60**	**$2.70**	**$3.00**	**$2.40**
(Split-Adjusted)					**$3.55**							

	2007	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018
4th Quarter	$0.50	$0.50	$0.50	$0.30	$0.30	$0.30	$0.40	$0.45	$0.17	$0.18	$0.20	$0.24
					Stock Split: 3-for-1, effective 12/29/14							
1st Quarter	0.50	0.50	0.50	0.30	0.15	0.35	0.40	0.45	0.17	0.18	0.20	0.25
2nd Quarter	0.50	0.50	0.30	0.30	0.15	0.35	0.40	0.45	0.17	0.18	0.22	0.26
3rd Quarter	0.50	0.50	0.30	0.30	0.20	0.35	0.45	0.50	0.17	0.18	0.22	0.27
Subtotal	**$2.00**	**$2.00**	**$1.60**	**$1.20**	**$0.80**	**$1.35**	**$1.65**	**$1.85**	**$0.68**	**$0.72**	**$0.84**	**$1.02**
Extra Dividend	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00
Total Cash Dividend	**$2.00**	**$2.00**	**$1.60**	**$1.20**	**$0.80**	**$1.35**	**$1.65**	**$1.85**	**$0.68**	**$0.72**	**$0.84**	**$1.02**

	2019
4th Quarter	$0.28
1st Quarter	0.28
2nd Quarter	0.29
3rd Quarter	0.30
Subtotal	**$1.15**
Extra Dividend	0.00
Total Cash Dividend	**$1.15**

Message to Shareholders

February 17, 2020

Dear Shareholder:

As we start a new decade in the year 2020, we're excited to note that this will be the 145th anniversary of First National Bank opening for business. As the actual date approaches this fall, we plan to recognize this great milestone with customer appreciation promotions and other appropriate ways. It's a testament to our loyal shareholders that we have been able to survive through some serious economic times in an industry that is so highly regulated. The staff continues to work hard to support the community banking model that has worked well for us for so many years.

This annual report provides the results of another solid year for the company. Our audited statements are included along with all the required supporting schedules. The actual operating results were quite similar to 2018. The main difference in the bottom line is due to an adjustment to our income tax expense that was substantially lower a year ago. That lower tax payment provided for a record year of earnings for First Bancshares, Inc. in 2018.

Some detailed highlights for 2019 show a slight increase in total assets with a year-end total in excess of $227 million, which is roughly 2% higher than last year. Of this total, we did see a small drop in total loan balances of less than $1mm and an increase in deposit balances of over $9mm equating to an increase of 5%. This shift in our balance sheet helped our liquidity position by lowering our loan to deposit ratio and allowing us to add balances in our investment portfolio.

At we prepared for 2019, all indications were that interest rates would continue to rise throughout the year. This scenario was favorable for our budget as our balance sheet was well positioned to take advantage of this. As we all know, the very opposite occurred as the Federal Reserve lowered the Fed Funds target rate three times over the year. Fortunately, we were able to make necessary adjustments, which actually resulted in net interest income exceeding 2018 results by over 2.6%. Noninterest income was down slightly from the prior year and expenses were up roughly 2.6%. Net income before taxes was less than $2,000 lower than the prior year. The income tax liability in 2019 was significantly higher than 2018 which accounted for the major difference in reportable earnings. Given the challenge we faced with the change in interest rate direction, we are pleased with the overall results for the year.

Early last year we started an addition and complete renovation of the main office facility. At times, it was quite dusty and noisy but our staff and customers were very accommodating during this time. We are now in the final stages and the work should be finished by the annual meeting date. In addition, we have started some minor sprucing up to the office building we purchased in Perkins Township, Sandusky so it will be ready to open in August of this year. Please stop in to see the updated lobby and new configuration when you are in town.

The first page of the annual report provides the details of the annual meeting, which is open to all shareholders. On behalf of the board and staff, we appreciate your support of First Bancshares and will continue to work hard toward our success.

Sincerely,

Steven L. Mays, DVM
Chairman of the Board

Dean J. Miller
President and CEO

DIXON, DAVIS, BAGENT & COMPANY
CERTIFIED PUBLIC ACCOUNTANTS
1205 WEAVER DRIVE • GRANVILLE, OHIO 43023 • 740-321-1000 • FAX 740-321-1100

INDEPENDENT AUDITOR'S REPORT

The Audit Committee of the Board of Directors
First Bancshares, Inc.
Bellevue, Ohio

We have audited the accompanying consolidated financial statements of First Bancshares, Inc., which comprise the consolidated balance sheets as of December 31, 2019 and 2018, and the related consolidated statements of income, changes in equity, and cash flows for the years then ended, and the related notes to the financial statements.

Management's Responsibility for the Financial Statements

Management is responsible for the preparation and fair presentation of these financial statements in accordance with accounting principles generally accepted in the United States of America; this includes the design, implementation, and maintenance of internal control relevant to the preparation and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error.

Auditor's Responsibility

Our responsibility is to express an opinion on these financial statements based on our audits. We conducted our audits in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audits to obtain reasonable assurance about whether the financial statements are free of material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

Opinion

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of First Bancshares, Inc. as of December 31, 2019 and 2018, and the results of their operations and their cash flows for the years then ended in accordance with accounting principles generally accepted in the United States of America.

Dixon, Davis, Bagent & Co.

Dixon, Davis, Bagent & Company
Granville, Ohio
February 17, 2020

Consolidated Balance Sheet

	December 31, 2019	December 31, 2018
Assets		
Cash and due from banks (Note 2)	$ 3,768,314	$ 5,986,783
Federal funds sold	-	-
Interest-bearing deposits in banks	-	-
Total cash and cash equivalents	3,768,314	5,986,783
Investment securities – Available for sale (Note 3)	26,810,710	20,404,477
Investment securities – Held to maturity (Note 3)	-	1,628,283
Other securities (Note 3)	1,301,017	1,223,617
Loans – Net of allowance for loan losses of $2,111,283 and $2,015,692 in 2019 and 2018, respectively (Note 4)	181,767,267	182,218,476
Foreclosed assets	-	74,997
Premises and equipment (Note 5)	6,838,562	4,154,343
Accrued interest receivable	856,782	821,611
Cash surrender value of life insurance	4,637,608	4,532,657
Other assets (Note 12)	1,120,907	1,486,334
Total assets	$ 227,101,167	$ 222,531,578
Liabilities and Stockholders' Equity		
Liabilities		
Deposits (Note 6)		
Noninterest-bearing	$ 38,941,434	$ 36,041,296
Interest-bearing	157,607,729	151,115,802
Total deposits	196,549,163	187,157,098
Federal Home Loan Bank advances (Note 7)	3,186,337	7,229,706
Bank line of credit (Note 8)	3,929,073	3,699,073
Federal funds purchased	734,386	2,887,000
Accrued interest payable	67,673	51,492
Accrued and other liabilities	1,936,592	1,949,705
Total liabilities	206,403,224	202,974,074
Stockholders' Equity		
Preferred stock – no par value; authorized 750,000 shares; 0 shares issued and outstanding	-	-
Common stock - $5.00 par value; authorized 750,000 shares; issued and outstanding 660,600 shares	1,101,000	1,101,000
Treasury stock – At cost; 122,981 and 91,292 shares at December 31, 2019 and 2018, respectively	(2,611,654)	(1,396,559)
Additional paid-in capital	1,118,026	1,107,113
Retained earnings	20,484,588	18,928,415
Accumulated other comprehensive income	605,983	(182,465)
Total stockholders' equity	20,697,943	19,557,504
Total liabilities and stockholders' equity	$ 227,101,167	$ 222,531,578

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

Consolidated Statement of Operations

	Year Ended December 31, 2019	Year Ended December 31, 2018
Interest Income		
Loans – including fees	$ 10,384,621	$ 9,530,288
Debt securities:		
Taxable	410,545	361,236
Tax-exempt	216,633	212,222
Other	214,369	160,714
Total interest income	11,226,168	10,264,460
Interest Expense		
Deposits	2,074,867	1,426,806
Borrowings	389,758	301,873
Total interest expense	2,464,625	1,728,679
Net Interest Income	8,761,543	8,535,781
Provision for Loan Losses (Note 4)	141,100	116,000
Net Interest Income After Provision for Loan Losses	8,620,443	8,419,781
Noninterest Income		
Service charges – Deposits	385,856	427,105
Net gain on sale of loans	219,998	219,129
Writedown of other real estate owned	-	-
Rental fees and commissions	26,137	18,950
Gain on sale of investment securities	(510)	-
Visa interchange fees	197,887	204,555
Other	457,513	440,469
Total noninterest income	1,286,881	1,310,208
Noninterest Expenses		
Salaries and employee benefits (Note 11)	4,220,951	4,129,665
Occupancy and equipment	711,135	705,326
Data processing	673,768	578,982
State tax	194,989	147,127
Professional fees	123,582	143,825
FDIC insurance	29,910	77,739
Advertising	51,060	41,404
Director fees	109,400	99,000
Other	907,927	920,320
Total noninterest expenses	7,022,722	6,843,388
Income – Before income taxes	2,884,602	2,886,601
Income Tax Expense (Note 12)	540,008	323,935
Net Income	$ 2,344,594	$ 2,562,666

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

Consolidated Statement of Comprehensive Income

	2019	2018
Net income	$ 2,344,594	$ 2,562,666
Other comprehensive income (loss), net of tax:		
Unrealized net holding gain (loss) on securities available-for-sale, net of income taxes of $209,723 and $(56,994) for the years ended December 31, 2019 and 2018, respectively	788,958	(214,406)
Reclassification adjustment for gains realized, net of income taxes of $(107) and $- for the years ended December 31, 2019 and 2018, respectively	(510)	-
Other comprehensive income (loss)	788,448	(214,406)
Comprehensive income (loss)	$ 3,133,042	$ 2,348,260

Consolidated Statement of Changes in Stockholders' Equity

	Preferred Stock	Common Stock	Treasury Stock	Additional Paid-in Capital	Retained Earnings	Accumulated Other Comprehensive Income	Total
Balance – December 31, 2017	$ -	$ 1,101,000	$(1,395,520)	$ 1,107,431	$ 16,946,460	$ 31,941	$ 17,791,312
Comprehensive income:							
Net income	-	-	-	-	2,562,666	-	2,562,666
Change in net unrealized gain on securities – Net of tax of $(56,994)	-	-	-	-	-	(214,406)	(214,406)
Total comprehensive Income	-	-	-	-	-	-	2,348,260
Purchase of treasury stock	-	-	(1,039)	(318)	-	-	(1,357)
Dividends declared $1.06 per share	-	-	-	-	(580,711)	-	(580,711)
Balance – December 31, 2018	-	$ 1,101,000	$(1,396,559)	$ 1,107,113	$ 18,928,415	$ (182,465)	$ 19,557,504
Comprehensive income:							
Net income	-	-	-	-	2,344,594	-	2,344,594
Change in net unrealized gain on securities – Net of tax of $209,587	-	-	-	-	-	788,448	788,448
Total comprehensive Income	-	-	-	-	-	-	3,133,042
Purchase of treasury stock	-	-	(1,228,920)	-	-	-	(1,228,920)
Sale of treasury stock	-	-	13,825	10,913	-	-	24,738
Dividends declared $1.17 per share	-	-	-	-	(788,421)	-	(788,421)
Balance – December 31, 2019	$ -	$ 1,101,000	$(2,611,654)	$ 1,118,026	$ 20,484,588	$ 605,983	$ 20,697,943

Consolidated Statement of Cash Flows

	Year Ended December 31, 2019	2018
Cash Flows from Operating Activities		
Net Income	$ 2,344,594	$ 2,562,666
Adjustments to reconcile net income to net cash from operating activities:		
Depreciation expense	294,639	302,156
Provision for loan losses	141,100	116,000
Accretion and amortization of securities	173,607	240,711
(Gain) loss on sale of investments	510	-
Deferred income taxes	89,286	(60,759)
Change in cash surrender value of life insurance	(104,951)	(100,740)
Writedown of fixed assets	-	76,122
Impairment of other real estate owned	-	18,448
Net change in:		
Accrued interest receivable and other assets	31,383	(166,120)
Accrued interest payable and other liabilities	3,067	194,775
Net cash provided by operating activities	2,973,235	3,183,259
Cash Flows from Investing Activities		
Activity in available-for-sale securities:		
Proceeds from sale	860,000	-
Maturities, prepayments, and calls	1,511,675	4,069,834
Purchases	(7,953,988)	(4,441,332)
Activity in held-to-maturities securities:		
Payments on held-to-maturity securities	1,628,283	26,513
Purchase of Federal Reserve Bank stock	(77,400)	-
Net change in loans	310,109	(12,896,753)
Proceeds from sale of foreclosed assets	74,997	6,552
Additions to premises and equipment	(2,978,858)	(16,955)
Net cash used in investing activities	(6,625,182)	(13,252,141)
Cash Flows from Financing Activities		
Net change in deposits	9,392,064	7,339,402
Payments on Federal Home Loan Bank advances	(4,043,369)	(4,015,209)
Proceeds from Federal Home Loan Bank advances	-	7,000,000
Change in short-term borrowed funds	(1,922,614)	599,000
Purchase of treasury stock	(1,228,920)	(1,357)
Sale of treasury stock	24,738	
Dividends paid	(788,421)	(580,711)
Net cash provided by financing activities	1,433,478	10,341,125
Net Increase (Decrease) in Cash and Cash Equivalents	(2,218,469)	272,243
Cash and Cash Equivalents – Beginning of year	5,986,783	5,714,540
Cash and Cash Equivalents – End of year	$ 3,768,314	$ 5,986,783
Supplemental Cash Flow Information		
Cash paid for:		
Interest	$ 2,448,444	$ 1,711,043
Income taxes	503,000	575,000
Loans transferred to other real estate	-	-

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

Note 1 – Nature of Business and Significant Accounting Policies

Basis of Presentation and Consolidation – The consolidated financial statements include the accounts of First Bancshares, Inc. (the "Corporation") and its wholly owned subsidiaries, First National Bank (the "Bank") and First Bellevue Properties, Inc. All significant intercompany balances and transactions have been eliminated in consolidation.

Nature of Operations – The Bank provides a full range of financial services to individuals and corporate customers in the Ohio counties of Huron, Sandusky, Erie, Ottawa, and Seneca. First Bellevue Properties, Inc. is used for property management.

Use of Estimates – In preparing consolidated financial statements in conformity with accounting principles generally accepted in the United States of America, management is required to make estimates and assumptions that affect the reported amounts of assets and liabilities as of the date of the balance sheet and reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates. Material estimates that are particularly susceptible to significant change in the near term relate to the determination of the allowance for loan losses, the valuation of investment securities, and deferred tax assets.

Cash and Cash Equivalents – For the purpose of the consolidated statement of cash flows, cash and cash equivalents include cash and balances due from banks, federal funds sold, and interest-bearing deposits in banks which mature within 90 days.

Securities – Debt securities that management has the positive intent and ability to hold to maturity are classified as "held to maturity" and recorded at amortized cost. Securities not classified as held to maturity, including equity securities with readily determinable fair values, are classified as "available for sale" and are recorded at fair value, with unrealized gains and losses excluded from earnings and reported in other comprehensive income.

Purchase premiums and discounts are recognized in interest income using the interest method over the terms of the securities. Declines in the fair value of held-to-maturity and available-for-sale securities below their cost that are deemed to be other than temporary are reflected in earnings as realized losses. In estimating other-than-temporary impairment losses, management considers (1) the length of time and the extent to which the fair value has been less than cost, (2) the financial condition and near-term prospects of the issuer, and (3) the intent and ability of the Corporation to retain its investment in the issuer for a period of time sufficient to allow for any anticipated recovery in fair value. Gains and losses on the sale of securities are recorded on the trade date and are determined using the specific identification method.

Loans and Allowance for Loan Losses
Loans are carried at the amount of unpaid principal, adjusted for deferred loan fees and origination costs. Interest on loans is accrued based on the principal amounts outstanding. Nonrefundable loan fees and related direct costs are deferred and the net amount is amortized to income as a yield adjustment over the life of the loan using the interest method. When principal or interest is delinquent for ninety days or more, the bank evaluates the loan for nonaccrual status. Also any loan that is considered uncollectible, regardless of past due status, will be evaluated for nonaccrual status.

After a loan is placed on nonaccrual status, all interest previously accrued but not collected is reversed against current period interest income. Subsequent collections of interest payments on nonaccrual loans are recognized as interest income unless ultimate collectability of the loan is in doubt. Cash collections on loans where ultimate collectability remains in doubt are applied as reductions of the loan principal balance and no interest income is recognized until the principal balance has been collected.

The allowance for loan losses is established as losses are estimated to have occurred through a provision for loan losses charged to earnings. Loan losses are charged against the allowance when management believes the uncollectability of a loan balance is confirmed. Subsequent recoveries, if any, are credited to the allowance. The allowance is based on two basic principles of accounting (i) FASB ASC 450, *Contingencies,* which requires that losses be accrued when they are probable of occurring and estimable and (ii) FASB ASC 310, *Receivables,* which requires that losses on impaired loans be accrued based on the differences between the loan balance and either the value of collateral, if such loans are considered to be collateral dependent and in the process of collection, or the present value of future cash flows, or the loan's value as observable in the secondary market. A loan is considered impaired when, based on current information and events, the bank has concerns about the ability to collect the scheduled payments of principal or interest when due according to the contractual terms of the loan agreement. Factors considered by mange-

Note 1 – Nature of Business and Significant Accounting Policies (Continued)

ment in determining impairment include payment status, collateral value and the probability of collecting scheduled principal and interest payments when due. Loans that experience insignificant payment delays and payment shortfall generally are not classified as impaired. Management determines the significance of payment delays and payment shortfalls on a case-by-case basis, taking into consideration all of the circumstances surrounding the loan and borrower, including the length of the delay, the reasons for the delay, the borrower's prior payment record, and the amount of the shortfall in relation to the principal and interest owed.

The bank's allowance for loan losses has two basic components: the specific allowance, and the pooled allowance. Each of these components is determined based upon estimates that can and do change when the actual events occur. As a result of the uncertainties inherent in the estimation process, management's estimate of loan losses and the related allowance could change in the near term.

The specific allowance component is used to individually establish an allowance for loans identified for impairment testing. When impairment is identified, a specific reserve may be established based on the bank's calculation of the estimated loss embedded in the individual loan. Impairment testing includes consideration of the borrower's overall financial condition, resources and payment record, support available from financial guarantors and the fair market value of collateral. These factors are combined to estimate the probability and severity of inherent losses.

The pooled formula component is used to estimate the losses inherent in the pools of non-impaired loans.

These loans are then also segregated by loan type and allowance factors are assigned by management based on delinquencies, loss history, trends in volume and terms of loans, effects of changes in lending policy, the experience and depth of management, national and local economic trends, concentrations of credit, results of the loan review system and the effect of external factors (i.e. competition and regulatory requirements).

Allowance factors and overall size of the allowance may change from period to period based on management's assessment of the above-described factors and the relative weights given to each factor, in addition, various regulatory agencies periodically review the allowance for loan losses. These agencies may require the bank to make additions to the allowance for loan losses based on their judgments of collectability based on information available to them at the time of their examination.

Loans are placed into a nonaccruing status and classified as nonperforming when the principal or interest has been in default for a period of 90 days or more.

Loans classified as substandard or worse, 90 days past due, nonaccrual status or troubled debt restructurings are considered for impairment testing. A substandard loan shows signs of continuing negative financial trends and unprofitability and therefore, is inadequately protected by the current sound worth and paying capacity of the obligor or of the collateral pledged, if any. The borrower on such loans typically exhibits one or more of the following characteristics: financial ratios and profitability margins are well below industry average; a negative cash flow position exists; debt service capacity is insufficient to the service debt and an improvement in the cash flow position is unlikely within the next twelve months; secondary and tertiary means of debt repayment are weak. Loans classified as substandard are characterized by the probability that the bank will not collect amounts due according to the contractual terms or sustain some loss if the deficiencies are not corrected.

Loss potential, while existing with respect to the aggregate amount of substandard (or worse) loans, does not have to exist in any individual assets classified as substandard. Such credits are also evaluated for nonaccrual status.

Impaired loans include loans that have been classified as substandard or worse. However, certain loans have been paying as agreed and have remained current, with some financial issues related to cash flow that have caused some concern as to the ability of the borrower to perform in accordance with the current loan terms but not to such an extent as to require the loan be put in a nonaccruing status. Cash receipts on impaired loans are recorded as interest income as received, unless the loan is in a nonaccrual status.

The bank's charge-off policy states after all collection efforts have been exhausted and the loan is deemed to be a loss, it will be charged to the bank's established allowance for loan losses. Consumer loans subject to the Uniform Retail Credit Classification are charged-off as follows: (a) closed end loans are charged-off no later than 120 days after becoming delinquent, (b) consumer loans to borrowers who subsequently declare bankruptcy, where the bank is an

Note 1 – Nature of Business and Significant Accounting Policies (Continued)

unsecured creditor, are charged-off within 60 days of receipt of the notification from the bankruptcy court, (c) fraudulent loans are charged-off within 90 days of discovery and (d) death of a borrower will cause a charge-off to be incurred at such time an actual loss is determined. All other types of loans are generally evaluated for loss potential at the 90th day past due threshold, and any loss is recognized no later than the 120th day past due threshold; each loss is evaluated on its specific facts regarding the appropriate timing to recognize the loss.

Troubled Debt Restructuring (TDRs) – Management classified loans as TDRs when a borrower is experiencing financial difficulties and the Corporation has granted a concession. In order to determine whether a borrower is experiencing financial difficulty, an evaluation is performed of the probability that the borrower will be in payment default on any of its debt in the foreseeable future without the modification. This evaluation is performed under the Corporation internal underwriting policy. TDRs are separately identified for impairment disclosures and are measured at the present value of estimated future cash flows using the loan's effective rate at inception. If a TDR is considered to be a collateral dependent loan, the loan is reported, net, at the fair value of the collateral.

Off-balance-sheet Instruments – In the ordinary course of business, the Corporation has entered into commitments under commercial letters of credit and standby letters of credit. Such financial instruments are recorded when they are funded.

Servicing – Servicing assets are recognized as separate assets when rights are acquired through sale of financial assets. Capitalized servicing rights are reported in other assets and are amortized into noninterest income in proportion to, and over the period of, the estimated future net servicing income of the underlying financial assets. Servicing assets are evaluated for impairment based upon the fair value of the rights as compared to amortized cost. Impairment is determined by stratifying rights by predominant characteristics, such as interest rates and terms. Fair value is determined using prices for similar assets with similar characteristics, when available, or based upon discounted cash flows using market-based assumptions. Impairment is recognized through a valuation allowance for an individual stratum, to the extent that fair value is less than the capitalized amount for the stratum.

Loans serviced for others are not included in the accompanying consolidated balance sheet. The unpaid principal balances of mortgage loans serviced for others were $78.7 million and $73.2 million at December 31, 2019 and 2018, respectively. The related mortgage servicing rights, included in other assets, were $719,709 and $719,933 at December 31, 2019 and 2018, respectively. At December 31, 2019 and 2018, the book value of the servicing rights approximated fair value and no valuation allowances were required.

Foreclosed Assets – Assets acquired through, or in lieu of, loan foreclosure are held for sale and are initially recorded at fair value at the date of the foreclosure, establishing a new cost basis. Subsequent to foreclosure, valuations are periodically performed by management and the assets are carried at the lower of carrying amount or fair value less cost to sell. Revenue and expenses from operations and changes in the valuation allowance are included in net expenses from foreclosed assets.

Premises and Equipment – Land is carried at cost. Buildings and equipment are carried at cost, less accumulated depreciation computed on the straight-line method over the estimated useful lives of the assets.

Bank-owned Life Insurance – The Bank has purchased life insurance policies on certain key officers. Bank-owned life insurance is recorded at its cash surrender value, or the amount that can be realized.

Postretirement Benefits – The Corporation has endorsement split-dollar life insurance policies and agreements with individuals to provide a benefit extending to postretirement periods. The liability in connection with these agreements was recorded effective January 1, 2008 as a decrease in retained earnings of $161,060 when the accounting treatment for such agreements changed. At December 31, 2019 and 2018, the Corporation had a liability of $229,571 and $213,960, respectively, in connection with these benefits.

Stock Based Compensation – Compensation cost is recognized for stock options and stock awards issued to employees based on the fair value of these awards at the date of the grant. Fair value of the stock options is determined by the mean between the lowest bid and highest bid asked prices on the grant date. Compensation cost is recognized over the required service period, generally defined as the vesting period.

Treasury Stock – Treasury stock is stated at cost. Cost is determined by the average cost method.

Note 1 – Nature of Business and Significant Accounting Policies (Continued)

Income Taxes - Income taxes are provided for the tax effects reported in the financial statements and consist of taxes currently due plus deferred taxes related primarily to differences between the basis of available-for-sale securities, allowance for loan losses, accumulated depreciation, and accrued employee benefits. The deferred tax assets and liabilities represent the future tax return consequences of those differences, which will either be taxable or deductible when the assets and liabilities are recovered or settled. Deferred tax assets and liabilities are reflected at income tax rates applicable to the period in which the deferred tax assets and liabilities are expected to be realized or settled. As changes in tax laws or rates are enacted, deferred tax assets and liabilities are adjusted through the provision for income taxes. The Bancorp files consolidated income tax returns with its subsidiaries on a calendar year basis.

Fair Value Measurements - The Bancorp follows the guidance of FASB ASC 825, *Financial Instruments*, and FASB ASC 820, *Fair Value Measurement*. This guidance permits entities to measure many financial instruments and certain other items at fair value. The objective is to improve financial reporting by providing entities with the opportunity to mitigate volatility in reported earnings caused by measuring related assets and liabilities differently without having to apply complex hedge accounting provisions. This guidance clarifies that fair value is an exit price, representing the amount that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants. Under this guidance, fair value measurements are not adjusted for transaction costs. This guidance establishes a fair value hierarchy that prioritizes the inputs to valuation techniques used to measure fair value. The hierarchy gives the highest priority to unadjusted quoted prices in active markets for identical assets or liabilities (Level 1 measurements) and the lowest priority to unobservable inputs (Level 3 measurements).

Comprehensive Income – Accounting principles generally require that recognized revenue, expenses, gains, and losses be included in net income. Certain changes in assets and liabilities, such as unrealized gains and losses on available-for-sale securities, are reported as a separate component of the equity section of the consolidated balance sheet; such items, along with net income, are components of comprehensive income.

The components of other comprehensive income and related tax effects are as follows:

	2018	2018
Net income	$2,346,207	$2,562,666
Other comprehensive income		
Unrealized holding gains (losses) on available-for-sale Securities	789,065	(214,406)
Reclassification adjustment for gains on sale recognized in income	(510)	-
Net unrealized gains (losses)	788,555	(214,406)
Tax effect	(107)	-
Other comprehensive income	$3,134,655	$2,348,260

Reclassification – Certain amounts appearing in the prior year's financial statements have been classified to conform to the current year's financial statements.

Subsequent Events – The consolidated financial statements and related disclosures include evaluation of events up through and including February 17, 2020, which is the date the consolidated financial statements were available to be issued.

Note 2 – Restriction on Cash and Amounts Due from Banks

The Bank is required to maintain average balances on hand or with the Federal Reserve Bank. At December 31, 2019 and 2018, these reserve balances amounted to $250,000 and $250,000, respectively.

Note 3 – Securities

The amortized cost and fair value of securities, with gross unrealized gains and losses, are as follows:

	2019			
	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Estimated Market Value
Available-for-sale securities:				
U.S. government and federal agency	$ 1,473,208	$ 24,625	$ (10,292)	$ 1,487,541
Mortgage backed	13,712,676	83,176	(39,740)	13,756,112
State and municipal	10,409,759	398,997	(23,779)	10,784,977
Preferred stock	448,000	334,080	-	782,080
Total available-for-sale securities	$26,043,643	$ 840,878	$ (73,811)	$26,810,710
Held-to-maturity securities:				
Tax-exempt bonds	$ -	$ -	$ -	$ -
Total held-to-maturity securities	$ -	$ -	$ -	$ -

	2018			
	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Estimated Market Value
Available-for-sale securities:				
U.S. government and federal agency	$ 1,926,544	$ 23,690	$ (37,982)	$ 1,912,252
Mortgage backed	10,724,242	13,210	(326,614)	10,410,838
State and municipal	7,536,658	4,317	(104,127)	7,436,848
Preferred stock	448,000	196,539	-	644,539
Total available-for-sale securities	$20,635,444	$ 237,756	$(468,723)	$20,404,477
Held-to-maturity securities:				
Tax-exempt bonds	$ 1,628,283	$ 77,984	$ (3,336)	$ 1,702,931
Total held-to-maturity securities	$ 1,628,283	$ 77,984	$ (3,336)	$ 1,702,931

At December 31, 2019 and 2018, securities with a carrying value of $16,468,288 and $15,781,434, respectively, were pledged to secure borrowings, public deposits, and for other purposes required or permitted by law.

Note 3 – Securities (Continued)

The amortized cost and fair value of debt securities by contractual maturity at December 31, 2019 are as follows:

	Securities Held to Maturity		Securities Available for Sale	
	Amortized Cost	Market Value	Amortized Cost	Market Value
Due in one year or less	$ -	$ -	$ 456,508	$ 457,484
Due in one through five years	-	-	2,978,769	3,049,319
Due in five years through ten years	-	-	4,692,849	4,795,330
Due after ten years	-	-	3,754,841	3,970,385
	-	-	11,882,967	12,272,518
Mortgage-backed securities	-	-	13,712,676	13,756,112
Preferred stock	-	-	448,000	782,080
Total	$ -	$ -	$26,043,643	$26,810,710

Information pertaining to securities with gross unrealized losses at December 31, 2019 and 2018, aggregated by investment category and length of time that individual securities have been in a continuous loss position, is as follows:

	2019			
	Less Than Twelve Months		Over Twelve Months	
	Gross Unrealized Losses	Fair Value	Gross Unrealized Losses	Fair Value
Available-for-sale securities:				
U.S. government and federal agency	$ -	$ -	$ (10,292)	$ 748,842
State and municipal	(20,528)	1,420,961	(3,251)	170,000
Mortgage backed	(17,405)	4,822,470	(22,335)	4,358,376
Total available-for-sale securities	$ (37,933)	$6,243,431	$ (35,878)	$ 5,277,218

	2018			
	Less Than Twelve Months		Over Twelve Months	
	Gross Unrealized Losses	Fair Value	Gross Unrealized Losses	Fair Value
Available-for-sale securities:				
U.S. government and federal agency	$ -	$ -	$ (37,982)	$ 965,059
State and municipal	(11,168)	1,035,881	(92,959)	3,249,502
Mortgage backed	(11,538)	1,052,363	(315,076)	7,541,249
Total available-for-sale securities	$ (22,706)	$2,088,244	$ (446,017)	$11,755,810

Unrealized losses on securities have not been recognized into income because the issuers' bonds are of high credit quality, the Bank has the intent and ability to hold the securities for the foreseeable future, and the decline in fair value is primarily due to increased market interest rates. The fair value is expected to recover as the bonds approach the maturity date.

Other securities consist of restricted Federal Home Loan Bank stock, Federal Reserve Bank stock and United Bankers' Bank stock. These stocks are carried at cost, which approximates market value.

Note 4 – Loans

A summary of the balances of loans is as follows:

	2019	2018
Mortgage loans on real estate:		
Residential 1-4 family	$ 37,386,080	$ 35,780,341
Commercial	103,932,660	102,169,854
Total mortgage loans on real estate	141,318,740	137,950,195
Commercial and agricultural loans	39,443,272	43,184,694
Consumer loans	3,116,538	3,099,279
Total loans	183,878,550	184,234,168
Less allowances for loan losses	2,111,283	2,015,692
Net loans	$181,767,267	$182,218,476

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

	2019	2018
Balance at beginning of year	$ 2,015,692	$ 1,972,106
Provision for loan losses	141,100	116,000
Loans charged off	(100,093)	(73,184)
Recoveries of loans previously charged off	54,584	770
Balance at end of year	$ 2,111,283	$ 2,015,692

The following is a summary of information pertaining to impaired loans:

	2019	2018
Impaired loans without a valuation allowance	$ 2,155,862	$ 2,587,748
Impaired loans with a valuation allowance	-	77,225
Total impaired	$ 2,155,862	$ 2,664,973
Valuation allowance related to impaired loans	$ -	$ 21,926
Total nonaccrual loans	2,155,862	2,664,973
Average investment in impaired loans during the year	2,410,418	2,421,006

No interest income has been recognized on impaired loans during the years ended December 31, 2019 and 2018. No additional funds are committed to be advanced in connection with impaired loans.

In the ordinary course of business, the Bank has granted loans to principal officers, directors, and their affiliates amounting to $781,273 and $759,277 as of December 31, 2019 and 2018, respectively.

Note 4 – Loans (Continued)

December 31, 2019

	Residential Mortgages	Consumer Loans	Commercial Loans	Agricultural Loans	Commercial Real Estate Mortgages	Agricultural Real Estate Mortgages	Total
Allowance for Loan Loss:							
Beginning Balance	$ 343,726	$ 21,562	$ 405,165	$ 63,808	$ 1,105,772	$ 75,659	$ 2,015,692
Provision	128,023	17,370	(18,817)	4,815	(1,224)	10,933	141,100
Charge-offs	(67,252)	(9,670)	(9,500)	-	(13,672)	-	(100,094)
Recoveries	-	1,882	3,711	-	48,992	-	54,585
Total	$ 404,497	$ 31,144	$ 380,559	$ 68,623	$ 1,139,868	$ 86,592	$ 2,111,283
Specific Reserves-Impaired Loans	$ -	$ -	$ -	$ -	$ -	$ -	$ -
General Reserves	404,497	31,144	380,559	68,623	1,139,868	86,592	2,111,283
Total	$ 404,497	$ 31,144	$ 380,559	$ 68,623	$ 1,139,868	$ 86,592	$ 2,111,283
Loans individually evaluated for impairment	$ 144,459	$ -	$ 517,716	$ -	$ 3,136,951	$ -	$ 3,799,126
Loans collectively evaluated for impairment	37,241,621	3,116,538	35,406,453	3,519,103	96,466,086	4,329,623	180,079,424
Total	$37,386,080	$ 3,116,538	$35,924,169	$ 3,519,103	$99,603,037	$ 4,329,623	$183,878,550

	Impaired Loans With Allowance			Impaired Loans With No Allowance	
	Principal Balance	Recorded Investment	Allocated Allowance for Loan Loss	Principal Balance	Recorded Investment
Impaired Loans and Related Allowance:					
Residential Mortgages	$ -	$ -	$ -	$ 199,671	$ 143,070
Consumer Loans	-	-	-	-	-
Commercial Loans	-	-	-	59,004	50,599
Agricultural Loans	-	-	-	-	-
Commercial Real Estate Mortgages	-	-	-	2,243,894	1,962,193
Agricultural Real Estate Mortgages	-	-	-	-	-
Total	$ 81,708	$ 77,225	$ 21,926	$ 2,502,569	$ 2,155,862

Note 4 – Loans (Continued)

December 31, 2018

	Residential Mortgages	Consumer Loans	Commercial Loans	Agricultural Loans	Commercial Real Estate Mortgages	Agricultural Real Estate Mortgages	Total
Allowance for Loan Loss:							
Beginning Balance	$ 349,153	$ 17,489	$ 435,275	$ 59,105	$ 1,057,343	$ 53,741	$ 1,972,106
Provision	17,853	4,985	(30,880)	4,703	97,421	21,918	116,000
Charge-offs	(23,280)	(912)	-	-	(48,992)	-	(73,184)
Recoveries	-	-	770	-	-	-	770
Total	$ 343,726	$ 21,562	$ 405,165	$ 63,808	$ 1,105,772	$ 75,659	$ 2,015,692
Specific Reserves-Impaired Loans	$ -	$ -	$ 21,926	$ -	$ -	$ -	$ 21,926
General Reserves	343,726	21,562	383,239	63,808	1,105,772	75,659	1,993,766
Total	$ 343,726	$ 21,562	$ 405,165	$ 63,808	$ 1,105,772	$ 75,659	$ 2,015,692
Loans individually evaluated for impairment	$ 94,963	$ -	$ 123,801	$ -	$ 3,669,067	$ -	$ 3,887,831
Loans collectively evaluated for impairment	35,685,378	3,099,279	39,181,962	3,878,931	93,901,454	4,599,333	180,346,337
Total	$35,780,341	$ 3,099,279	$39,305,763	$ 3,878,931	$97,570,521	$ 4,599,333	$184,234,168

	Impaired Loans With Allowance			Impaired Loans With No Allowance	
	Principal Balance	Recorded Investment	Allocated Allowance for Loan Loss	Principal Balance	Recorded Investment
Impaired Loans and Related Allowance:					
Residential Mortgages	$ -	$ -	$ -	$ 143,051	$ 94,963
Consumer Loans	-	-	-	-	-
Commercial Loans	81,708	77,225	21,926	49,491	46,576
Agricultural Loans	-	-	-	-	-
Commercial Real Estate Mortgages	-	-	-	2,693,971	2,446,209
Agricultural Real Estate Mortgages	-	-	-	-	-
Total	$ 81,708	$ 77,225	$ 21,926	$ 2,886,513	$ 2,587,748

Note 4 – Loans (Continued)

December 31, 2019

Credit Quality Indicators by Type of Loan:	Residential Mortgages	Consumer Loans	Commercial Loans	Agricultural Loans	Commercial Real Estate Mortgages	Agricultural Real Estate Mortgages	Total	Grade
Grade								
Pass	$37,194,093	$ 3,116,538	$33,411,052	$ 3,032,015	$93,759,051	$ 3,950,010	$174,462,759	1-4
Special Mention	-	-	1,864,608	487,088	2,917,594	349,581	5,618,871	5
Substandard	191,987	-	648,509	-	2,926,392	30,032	3,796,920	6
Doubtful	-	-	-	-	-	-	-	7
Loss	-	-	-	-	-	-	-	8
Total	$37,386,080	$ 3,116,538	$35,924,169	$ 3,519,103	$99,603,037	$ 4,329,623	$183,878,550	

Aging analysis of Past Due Loans and Nonaccrual Loans:	30-59 Days Past Due	60-89 Days Past Due	Greater than 90 Days or Nonaccrual	Total Past Due Loans	Total Current Loans	Total Loans	Recorded Investment Past Due >90 Days and Still Accruing
Residential Mortgages	$ 88,051	$ -	$ 73,181	$ 161,232	$ 37,224,848	$ 37,386,080	$ -
Consumer Loans	2,274	1,094	-	3,368	3,113,170	3,116,538	-
Commercial Loans	50,000	12,588	-	62,588	35,861,581	35,924,169	-
Agricultural Loans	-	-	-	-	3,519,103	3,519,103	-
Commercial Real Estate Mortgages	-	-	1,727,542	1,727,542	97,875,495	99,603,037	-
Agricultural Real Estate Mortgages	-	-	-	-	4,329,623	4,329,623	-
Total	$ 140,325	$ 13,682	$ 1,800,723	$ 1,954,730	$181,923,820	$183,878,550	$ -

Note 4 – Loans (Continued)

December 31, 2018

Credit Quality Indicators by Type of Loan:	Residential Mortgages	Consumer Loans	Commercial Loans	Agricultural Loans	Commercial Real Estate Mortgages	Agricultural Real Estate Mortgages	Total	Grade
Grade								
Pass	$35,633,115	$ 3,099,279	$37,423,407	$ 3,878,931	$93,293,903	$ 4,568,611	$177,897,246	1-4
Special Mention	-	-	926,549	-	1,270,447	30,722	2,227,718	5
Substandard	147,226	-	832,006	-	3,006,171	-	3,985,403	6
Doubtful	-	-	123,801	-	-	-	123,801	7
Loss	-	-	-	-	-	-	-	8
Total	$35,780,341	$ 3,099,279	$39,305,763	$ 3,878,931	$97,570,521	$ 4,599,333	$184,234,168	

Aging analysis of Past Due Loans and Nonaccrual Loans:	30-59 Days Past Due	60-89 Days Past Due	Greater than 90 Days or Nonaccrual	Total Past Due Loans	Total Current Loans	Total Loans	Recorded Investment Past Due >90 Days and Still Accruing
Residential Mortgages	$ 123,830	$ -	$ 5,698	$ 129,528	$ 35,650,813	$ 35,780,341	$ -
Consumer Loans	11,464	1,979	-	13,443	3,085,836	3,099,279	-
Commercial Loans	-	569,003	-	569,003	38,736,760	39,305,763	-
Agricultural Loans	-	-	-	-	3,878,931	3,878,931	-
Commercial Real Estate Mortgages	833,106	905,374	426,874	2,165,354	95,405,167	97,570,521	-
Agricultural Real Estate Mortgages	-	-	-	-	4,599,333	4,599,333	-
Total	$ 968,400	$1,476,356	$ 432,572	$ 2,877,328	$181,356,840	$184,234,168	$ -

Note 4 – Loans (Continued)

The following tables present loans by class modified as troubled debt restructurings that occurred during the years ending December 31, 2019 and 2018:

2019	Number of Loans	Premodification Outstanding Recorded Investment	Post-Modification Balance at December 31, 2019
Troubled Debt Restructurings:			
Commercial:			
Construction		$ -	$ -
Commercial residential	1	1,242,595	1,174,758
Non-farm non-residential	8	1,670,540	1,571,762
Other	-	-	-
Agriculture:			
Agriculture 1-4 family	-	-	-
Other agriculture real estate	-	-	-
Other agriculture	-	-	-
Real Estate Mortgage:			
Construction	-	-	-
1-4 owner occupied	-	-	-
Installment:			
Auto	-	-	-
Other	-	-	-
Total	9	$ 2,913,135	$ 2,746,520

2018	Number of Loans	Premodification Outstanding Recorded Investment	Post-Modification Balance at December 31, 2018
Troubled Debt Restructurings:			
Commercial:			
Construction		$ -	$ -
Commercial residential	1	1,296,294	1,222,859
Non-farm non-residential	7	1,627,639	1,549,688
Other	-	-	-
Agriculture:			
Agriculture 1-4 family	-	-	-
Other agriculture real estate	-	-	-
Other agriculture	-	-	-
Real Estate Mortgage:			
Construction	-	-	-
1-4 owner occupied	-	-	-
Installment:			
Auto	-	-	-
Other	-	-	-
Total	8	$ 2,923,933	$ 2,772,547

Troubled debt restructurings for which there was a payment default within twelve months following the modification during the year ending December 31, 2019 consists of loans totaling $134,147 at December 31, 2019.

Troubled debt restructurings for which there was a payment default within twelve months following the modification during the year ending December 31, 2018 consists of loans totaling $0 at December 31, 2018.

Note 5 – Bank Premises and Equipment

A summary of the cost and accumulated depreciation of premises and equipment is as follows:

	2019	2018
Land	$ 1,642,302	$ 1,635,010
Buildings and building improvements	7,207,056	4,983,538
Furniture, fixtures, and equipment	2,732,900	2,072,775
Vehicles	47,073	47,073
Construction in progress	87,923	-
Total	11,717,254	8,738,396
Accumulated depreciation	(4,878,692)	(4,584,053)
Net premises and equipment	$ 6,838,562	$ 4,154,343

Depreciation expense for the years ended December 31, 2019 and 2018 amounted to $274,438 and $302,156, respectively.

Note 6 – Deposits

The following is a summary of the distribution of deposits at December 31:

	2019	2018
Demand deposits	$ 38,941,434	$ 36,041,296
NOW accounts	39,356,753	35,463,272
Savings and money market accounts	71,483,345	77,641,392
Time:		
Under $100,000	25,377,000	19,308,518
$100,000 and over	21,390,631	18,702,620
Total	$196,549,163	$187,157,098

At December 31, 2019, the scheduled maturities of time deposits are as follows:

2020	$ 27,148,075
2021	16,743,049
2022	1,715,383
2023	645,809
2024	515,315
Total	$ 46,767,631

Note 7 – Federal Home Loan Bank Advances

The Bank has a borrowing arrangement with the Federal Home Loan Bank of Cincinnati. Advances under the borrowing arrangement are supported by individual agreements. At December 31, 2019, the Bank has advances outstanding with an interest rate ranging from 2.41 percent to 3.07 percent.

The advances are collateralized by investment securities with a carrying value of $49,055,000 at December 31, 2019.

At December 31, 2019, the advances mature as follows:

2020	$ 3,000,000
2021	186,337
2022	-
2023	-
2024	-
2025 and thereafter	-
Total	$ 3,186,337

Note 8 – Bank Line of Credit

During 2008, the Corporation entered into a $5,000,000 line of credit arrangement with a bank. The line of credit is collateralized by First National Bank stock owned by the Corporation. The Corporation makes quarterly interest-only payments and the principal balance is due on demand and subject to an annual review. The balance outstanding as of December 31, 2019 and 2018 was $3,929,073 and $3,699,073, respectively. The interest rate was 4.75 percent and 5.50 percent as of December 31, 2019 and 2018, respectively.

Note 9 – Minimum Regulatory Capital Requirements

The Bank is subject to various regulatory capital requirements administered by the federal banking agencies. Failure to meet minimum capital requirements can initiate certain mandatory and possibly additional discretionary actions by regulators that, if undertaken, could have a direct material effect on the 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 I capital (as defined in the regulations) to risk-weighted assets (as defined) and Tier I capital (as defined) to average assets (as defined).

As of December 31, 2019, the Bank was categorized as well capitalized under regulatory frame work for prompt corrective action. To be categorized as well capitalized, an institution must maintain minimum total risk-based, Tier I risk-based, and Tier I leverage ratios as set forth in the following table. There are no conditions or events since December 31, 2019 that management believes have changed the Bank's category. The Bank's actual capital amounts and ratios as of December 31, 2019 and 2018 are also presented in the table.

	Actual		For Capital Adequacy Purposes		To be Well Capitalized Under Prompt Corrective Action Provisions	
(000's omitted)	Amount	Ratio	Amount	Ratio	Amount	Ratio
As of December 31, 2019						
Total capital to risk-weighted assets	$26,296	12.4%	$16,951	8.0%	$21,189	10.0%
Tier I capital to risk-weighted assets	24,034	11.3%	12,713	6.0%	16,951	8.0%
Common equity Tier I capital to risk-weighted assets	24,034	11.3%	9,535	4.5%	13,773	6.5%
Tier I capital to average assets	24,034	10.2%	9,432	4.0%	11,790	5.0%
As of December 31, 2018						
Total capital to risk-weighted assets	$24,707	11.8%	$16,711	8.0%	$20,694	10.0%
Tier I capital to risk-weighted assets	22,602	10.8%	12,578	6.0%	16,711	8.0%
Common equity Tier I capital to risk-weighted assets	22,602	10.8%	9,434	4.5%	13,626	6.5%
Tier I capital to average assets	22,602	10.3%	8,789	4.0%	10,987	5.0%

Note 10 – Restrictions on Dividends

Banking regulations place certain restrictions on dividends paid and loans or advances made by the Bank to the Corporation. Prior approval of the Bank's federal regulator is required if the total dividends declared by the Bank exceed the sum of the net profits of the Bank for the current year-to-date and the net profits of the Bank for the preceding two years, less any required transfers to surplus. In addition, dividends paid by the Bank would be prohibited if the effect thereof would cause the Bank's capital to be reduced below applicable minimum standards. At December 31, 2019, retained earnings of approximately $5,910,000 was available for the payment of dividends without regulatory approval.

Note 11 – Employee Benefit Plan

The Bank sponsors a defined contribution benefit plan for substantially all employees. Bank contributions are based on matching one-half of participant contributions up to 6 percent of the participant's salary. Additional contributions may be made at the discretion of the board of directors. Discretionary contributions of $108,513 and $179,636 were made for the years ended December 31, 2019 and 2018, respectively. Bank contributions to the plan totaled $185,657 and $255,657 for the years ended December 31, 2019 and 2018, respectively.

Note 12 – Income Taxes

The components of the net deferred tax assets, included in other assets are as follows:

	2019	2018
Deferred tax assets:		
Other real estate owned writedowns	$ -	$ 3,780
Allowance for loan losses	296,935	276,861
Net deferred loan fees	7,774	13,730
Accrued employee benefits	141,398	128,455
Impairment on investment securities	273,420	273,420
Net unrealized loss on securities available for sale	-	48,503
Other	-	-
Total deferred tax assets	$ 719,527	$ 744,749
Deferred tax liabilities:		
Depreciation	$ 237,228	$ 122,840
Mortgage servicing rights	151,139	151,186
Federal Home Loan Bank stock dividends	58,065	58,065
Net unrealized gain on securities available for sale	161,084	-
Other	10,584	12,358
Total deferred tax liabilities	618,100	344,449
Net deferred tax assets	$ 101,427	$ 400,300

The components of deferred taxes are valued using the 21% federal income tax rate.

Allocation of income tax recovery between current and deferred portions is as follows:

	2019	2018
Current	$ 450,722	$ 522,659
Deferred	89,286	(198,724)
Total	$ 540,008	$ 323,935

The reasons for the difference between the income tax (recovery) expense at the federal statutory income tax rate and the recorded income tax (recovery) expense are summarized as follows:

	2019	2018
Income tax expense at federal statutory rate of 21%	$ 605,766	$ 606,186
Increases resulting from nondeductible expenses	6,348	4,505
Decreases resulting from nontaxable investment income	(45,305)	(49,678)
Decreases resulting from life insurance contract income	(22,040)	(21,155)
Other	(4,751)	57,880
Effect of tax rate change on deferred taxes	-	(273,803)
Total	$ 540,008	$ 323,935

Note 13 – Commitments and Credit Risk

Credit-related Financial Instruments – The Corporation is a party to credit-related financial instruments with off-balance-sheet risk in the normal course of business to meet the financing needs of its customers. These financial

Note 13 – Commitments and Credit Risk (Continued)

instruments include commitments to extend credit, standby letters of credit, and commercial letters of credit. Such commitments involve, to varying degrees, elements of credit and interest rate risk in excess of the amount recognized in the consolidated balance sheet.

The Corporation's exposure to credit loss is represented by the contractual amount of these commitments. The Corporation follows the same credit policies in making commitments as it does for on-balance-sheet instruments.

At December 31, 2019 and 2018, the following financial instruments were outstanding whose contract amounts represent credit risk:

	Contract Amount	
	2019	2018
Commitments to grant loans and unused lines of credit	$35,653,000	$36,761,000
Commercial and standby letters of credit	121,000	42,000

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. The commitments for equity lines of credit may expire without being drawn upon. Therefore, the total commitment amounts do not necessarily represent future cash requirements. The amount of collateral obtained, if it is deemed necessary by the Corporation, is based on management's credit evaluation of the customer.

Unfunded commitments under commercial lines of credit, revolving credit lines, and overdraft protection agreements are commitments for possible future extensions of credit to existing customers. These lines of credit are generally collateralized and may not be drawn upon to the total extent to which the Corporation is committed.

Commercial and standby letters of credit are conditional commitments issued by the Corporation to guarantee the performance of a customer to a third party. Those letters of credit are used primarily to support public and private borrowing arrangements. The credit risk involved is extending loan facilities to customers. The Corporation generally holds collateral supporting those commitments if deemed necessary.

Collateral Requirements – To reduce credit risk related to the use of credit-related financial instruments, the Corporation might deem it necessary to obtain collateral. The amount and nature of the collateral obtained are based on the Corporation's credit evaluation of the customer. Collateral held varies but may include cash, securities, accounts receivable, inventory, property, plant, and equipment, and real estate.

If the counterparty does not have the right and ability to redeem the collateral or the Corporation is permitted to sell or repledge the collateral on short notice, the Corporation records the collateral in its balance sheet at fair value with a corresponding obligation to return it.

Legal Contingencies – Various legal claims arise from time to time in the normal course of business. In the opinion of management, any outstanding claims will not have a material effect on the Corporation's consolidated financial statements.

Note 14 – Condensed Financial Statements of Parent Company

Presented below is condensed financial information as to financial position, results of operations, and cash flows of the Corporation as of and for the years ended December 31:

Balance Sheet

	2019	2018
Cash	$ 75,156	$ 5,987
Investment in common stock of subsidiaries	24,642,312	22,696,976
Premises and equipment – Net	-	415,000
Other assets	120,393	144,744
Total assets	$ 24,837,861	$ 23,262,707
Liabilities – Borrowings	$ 3,929,073	$ 3,699,073
Other liabilities	210,845	6,131
Stockholders' equity	20,697,943	19,557,503
Total liabilities and stockholders' equity	$ 24,837,861	$ 23,262,707

Note 14 – Condensed Financial Statements of Parent Company (Continued)

Statement of Operations

	2019	2018
Total income – Dividends from subsidiaries	$ -	$ 1,125,000
Operating expenses	316,453	395,775
Income (loss) before equity in undistributed net income of subsidiaries and income tax benefit	(316,453)	729,225
Equity in undistributed net income of subsidiaries	2,591,324	1,750,328
Income tax benefit	69,723	83,113
Net income	$ 2,344,594	$ 2,562,666

Statement of Cash Flows

	2019	2018
Cash flows from operating activities:		
Net income	$ 2,344,594	$ 2,562,666
Adjustments to reconcile net income to net cash from operating activities:		
Distributions from subsidiaries in excess of net income equity in undistributed net income of subsidiaries	136,840	(2,092,002)
Net change in other assets	25,964	73,614
Net change in other liabilities	(434,713)	40,952
Net cash provided by operating activities	2,072,685	585,230
Cash flows from financing activities:		
Cash dividends paid on common stock	(788,421)	(580,711)
Purchase of treasury stock	(1,228,920)	(1,039)
Sale of treasury stock	13,825	-
Net cash used in financing activities	(2,003,516)	(581,750)
Net increase (decrease) in cash	69,169	3,480
Cash – Beginning of year	5,987	2,507
Cash – End of year	$ 75,156	$ 5,987

Note 15 – Fair Value of Financial Instruments

The fair value of a financial instrument is the current amount that would be exchanged between willing parties, other than in a forced liquidation. Fair value is best determined based upon quoted market prices. However, in many instances, there are no quoted market prices for the Corporation's various financial instruments. 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. Accordingly, the fair value estimates may not be realized in an immediate settlement of the instruments. FAS ASC 825 excludes certain financial instruments and all nonfinancial instruments from its disclosure requirements. Accordingly, the aggregate fair value amounts presented may not necessarily represent the underlying fair value of the Corporation.

Note 15 – Fair Value of Financial Instruments (Continued)

The following methods and assumptions were used by the Corporation in estimating fair value disclosures for financial instruments:

Cash and Cash Equivalents – The carrying amounts of cash and cash equivalents approximate fair value.

Securities – Fair values of securities are based on quoted market prices. If a quoted market price is not available, fair value is estimated using quoted market prices for similar securities. The carrying value of Federal Home Loan Bank and Federal Reserve Bank stock approximates fair value based on the redemption provisions of the issuers.

Loan Receivable – For variable-rate loans that reprice frequently and with no significant change in credit risk, fair values are based on carrying values. Fair values for other loans are estimated using discounted cash flow analyses, using interest rates currently being offered for loans with similar terms to borrowers of similar credit quality. Fair values of nonperforming loans are estimated using discounted cash flow analyses or underlying collateral values, where applicable.

Deposit Liabilities – The fair values disclosed for demand deposits are, by definition, equal to the amount payable on demand at the reporting date (i.e., their carrying amounts). The carrying amounts of variable-rate, fixed term money market accounts and certificates of deposit approximate their fair values at the reporting date. 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.

Federal Home Loan Bank Advances and Bank Line of Credit – The fair values of the Corporation's borrowings are estimated using discounted cash flow analyses based on the Corporation's current incremental borrowing rates for similar types of borrowing arrangements.

Accrued Interest – The carrying amounts of accrued interest approximate fair value.

Other Financial Instruments – The fair value of other financial instruments, including loan commitments and unfunded letters of credit, based on discounted cash flow analyses, is not material.

The estimated fair values and related carrying or notional amounts of the Corporation's financial instruments are as follows (000s omitted):

			(Dollars in thousands) Fair Value Measurements		
	Carrying Amount	Fair Value	Quoted Prices (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
December 31, 2019					
FINANCIAL ASSETS					
Cash and cash equivalents	$ 3,768	$ 3,768	$ 3,768	$ -	$ -
Investment securities					
Available-for-sale	26,811	26,811	-	24,006	2,805
Held-to-maturity	-	-	-	-	-
Net loans	181,767	182,329	-	-	182,329
FINANCIAL LIABILITIES					
Deposits	$196,549	$186,308	$ -	$ -	$186,308
FHLB borrowings	3,186	3,186	-	-	3,186
Federal funds purchased	734	734	734	-	-
Bank line of credit	3,929	3,929	-	-	3,929

Note 15 – Fair Value of Financial Instruments (Continued)

			(Dollars in thousands) Fair Value Measurements		
	Carrying Amount	Fair Value	Quoted Prices (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
December 31, 2018					
FINANCIAL ASSETS					
Cash and cash equivalents	$ 5,987	$ 5,987	$ 5,987	$ -	$ -
Investment securities					
Available-for-sale	20,404	20,404	-	18,170	2,234
Held-to-maturity	1,628	1,703	-	1,533	170
Net loans	182,218	184,622	-	-	184,622
FINANCIAL LIABILITIES					
Deposits	$187,157	$171,393	$ -	$ -	$171,393
FHLB borrowings	7,230	7,190	-	-	7,190
Federal funds purchased	2,887	2,887	2,887	-	-
Bank line of credit	3,699	3,699	-	-	3,699

Note 16 – Fair Value Measurements

Accounting standards require certain assets and liabilities be reported at fair value in on the financial statements and provides a framework for establishing other fair value. The framework for determining fair value is based on a hierarchy that prioritizes the inputs and valuation techniques used to measure fair value.

The following table presents information about the Corporation's assets and liabilities measured at fair value on a recurring basis at December 31, 2019, and the valuation techniques used by the Corporation to determine those fair values.

In general, fair values determined by Level 1 inputs use quoted prices in active markets for identical assets or liabilities that the Corporation has the ability to access.

Fair values determined by Level 2 inputs use other inputs that are observable, either directly or indirectly. These Level 2 inputs include quoted prices for similar assets and liabilities in active markets, and other inputs such as interest rates and yield curves that are observable at commonly quoted intervals.

Level 3 inputs are unobservable inputs, including inputs that are available in situations where there is little, if any, market activity for the related asset. These Level 3 fair value measurements are based primarily on management's own estimates using pricing models, discounted cash flow methodologies, similar techniques taking into account the characteristics of the asset.

In instances where inputs used to measure fair value fall into different levels in the above fair value hierarchy, fair value measurements in their entirety are categorized based on the lowest level input that is significant to the valuation. The Corporation's assessment of the significance of particular inputs to these fair value measurements requires judgment and considers factors specific to each asset or liability.

Note 16 – Fair Value Measurements (Continued)

Assets Measured at Fair Value on a Recurring Basis at December 31, 2019 and 2018

	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)	Balance at December 31
2019 – Investment securities available for sale	$ -	$ 24,006,478	$ 2,804,232	$ 26,810,710
2018 – Investment securities available for sale	$ -	$ 18,170,617	$ 2,233,860	$ 20,404,477
2019 – Investment securities held to maturity	$ -	$ -	$ -	$ -
2018 – Investment securities held to maturity	$ -	$ 1,532,931	$ 170,000	$ 1,702,931

The Corporation also has certain assets that are measured at fair value on a nonrecurring basis. These assets are not measured at fair value on an ongoing basis, but are subject to fair value adjustments in certain circumstances (for example, when there is evidence of impairment).

Held-to-maturity investment securities categorized as Level 3 assets consist of tax-exempt bonds issued by local municipalities and trust preferred securities. The balance of these Level 3 securities was $0 and $170,000 at December 31, 2019 and 2018, respectively. The Corporation estimates the fair value of these investments based on the present value of expected future cash flows using management's best estimate of key assumptions, including forecasted interest yield and payment rates, credit quality, and a discount rate commensurate with the current market and other risks involved. Both observable and unobservable inputs may be used to determine the fair value of Level 3 assets

The fair value of impaired loans is estimated using either discounted cash flows or collateral value. Those impaired loans not requiring an allowance represent loans for which the fair value of the expected repayments or collateral exceed the recorded investments in such loans. At December 31, 2019, substantially all of the total impaired loans were evaluated based on the fair value of the collateral. Impaired loans are categorized as Level 3 assets because the values are based on available collateral (typically based on outside appraisals) and customized discounting criteria, if deemed necessary. At December 31, 2019 and 2018, impaired loans total $2,155,862 and $2,664,973, respectively. The change in fair value of impaired loans is accounted for in the allowance for loan losses (see Note 4).

First Bancshares, Inc.
First National Bank and First Bellevue Properties, Inc.

DIRECTORS

Sharon L. Barnes
Vice President
Barnes Nursery, Inc.

John A. Coppeler
Attorney at Law
Flynn, Py & Kruse

Adam L. Crockett
Sec/Treas. – Co-Owner
Green Hills Golf Course & Inn, Inc.

Steven L. Mays, DVM
Doctor of Veterinary Medicine

Duffield E. Milkie
Vice President/General Counsel
Cedar Fair L.P.

Dean J. Miller
President/CEO
First Bancshares, Inc.

Melvin H. Miller
Retired: President/Chairman
Janotta & Herner, Inc.

James V. Stouffer, Jr.
President/CEO
Catawba Island Club

Michael K. Winthrop
President/CEO
The Bellevue Hospital

Gordon A. Gibbs, *Director Emeritus*

First National Bank

OFFICERS

Senior Management Team
Dean Miller, President & CEO
Brian Harr, Executive Vice President/CLO
Edmund Schafer, Senior Vice President/CFO
Deborah Hawkins, Senior Vice President
David Jarvis, Senior Vice President/CTO
Melanie Mischler, Vice President/Retail Manager

Customer Service/Branch Support Team
Hollie Reinhart, Assistant Vice President
Brenda Provenzale, Assistant Vice President
Brenda Clark, Branch Manager
Tracy Fawcett, Branch Manager
Kyann Hay, Branch Manager
Christina Jesberger, Branch Manager
Tonda Zelms, Branch Manager

Lending Team
Frederick Bouyack, Vice President
Craig Buskirk, Vice President
Jeffrey Geary, Vice President
Anthony Luedy, Vice President
Gary Macko, Vice President
Vickie Smith, Assistant Vice President
Melinda Stacy, Assistant Vice President
James Journay, Mortgage Services Officer

Lending Support Team
Sheryl Diehr, Assistant Vice President
Brandon Barr, Assistant Vice President
Darlene Fullen, Loan Operations Officer
Karalee Siesel, Loan Operations Officer

Compliance and Regulation Support	Lisa Ramey, Assistant Vice President
Human Resources Management	Joelle Fritz, Assistant Vice President
Administration Support	Andrea Taylor, Administrative Services Officer
Marketing Department	Laura Schlachter, Marketing Officer
FNB Wealth Management Services	James Deer, Investment Executive

STAFF

Diane Ackerman
Rebecca Andrews
Rachael Baughn
Miranda Bentley
Veronica Blevins
Megan Border
Kelly Bullerwell
Brittany Christiansen
Adam Clark
Antoinette Corrado
Jamie Duke
David Gard
Marie Greene
Emma Hackenburg
Laurie Hale
Stephanie Madison
Tina Miller
Mari Newell
Samantha Norman
Pamela Orman
Savannah Packman
Bruce Roth
Brittany Ruhlman
Doreen Ryan
Sarah Shade
Megan Thomas
Joy Treat
Kerry Tuttle