UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549
FORM 10-K

☒ **Annual Report Pursuant To Section 13 Or 15(d) of The Securities Exchange Act of 1934**
For The Fiscal Year December 31, 2020.

Or

☐ **Transition Report Pursuant To Section 13 Or 15(d) of The Securities Exchange Act of 1934**
For the Transition Period from _________ to __________
Commission file number 000-27719

Southern First Bancshares, Inc.

(Exact name of registrant as specified in its charter)

South Carolina	**58-2459561**
(State of Incorporation)	(I.R.S. Employer Identification No.)
100 Verdae Boulevard, Greenville, SC	**29607**
(Address of principal executive offices)	(Zip Code)

864-679-9000
(Telephone Number)

Securities registered pursuant to Section 12(b) of the Act:

Title of class	Trading Symbol	Name of each exchange on which registered
Common Stock	**SFST**	**The NASDAQ Global Market**

Securities registered pursuant to Section 12(g) of the Act: None

Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act. Yes ☐ No ☒

Indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or Section 15(d) of the Exchange Act. Yes ☐ No ☒

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

Indicate by check mark whether the registrant has submitted electronically every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§ 232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files).
Yes ☒ No ☐

Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K is not contained herein, and will not be contained, to the best of registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K. ☐

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, a smaller reporting company, or emerging growth company. See definitions of "large accelerated filer," "accelerated filer," "smaller reporting company," and "emerging growth company" in Rule 12b-2 of the Exchange Act.
Large accelerated filer ☐ Accelerated filer ☒ Non-accelerated filer ☐ Smaller reporting company ☒ Emerging growth company ☐

If an emerging growth company, indicate by check mark if the registrant has elected not to use the extended transition period for complying with any new or revised financial accounting standards provided pursuant to Section 13(a) of the Exchange Act. ☐

Indicate by check mark whether the registrant has filed a report on and attestation to its management's assessment of the effectiveness of its internal control over financial reporting under Section 404(b) of the Sarbanes-Oxley Act (15 U.S.C. 7262(b)) by the registered public accounting firm that prepared or issued its audit report. Yes ☒ No ☐

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act). Yes ☐ No ☒

The aggregate market value of the common equity held by non-affiliates of the registrant as of June 30, 2020 (based on the average bid and ask price of the Common Stock as quoted on the NASDAQ Global Market on June 30, 2020), was $200,936,188.

7,797,098 shares of the registrant's common stock were outstanding as of February 22, 2021.

DOCUMENTS INCORPORATED BY REFERENCE

Portions of the registrant's Proxy Statement relating to the Annual Meeting of Shareholders to be held on May 18, 2021 are incorporated by reference into Part III of this Annual Report on Form 10-K where indicated.

Southern First Bancshares, Inc.
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CAUTIONARY NOTE REGARDING FORWARD-LOOKING STATEMENTS

This Annual Report on Form 10-K contains statements which constitute forward-looking statements within the meaning of Section 27A of the Securities Act of 1933 and Section 21E of the Securities Exchange Act of 1934, as amended (the “Exchange Act”). Forward-looking statements may relate to our financial condition, results of operation, plans, business strategy, objectives, or future performance. These statements are based on many assumptions and estimates and are not guarantees of future performance. Our actual results may differ materially from those anticipated in any forward-looking statements, as they will depend on many factors about which we are unsure, including many factors which are beyond our control. The words “may,” “would,” “could,” “should,” “will,” “expect,” “anticipate,” “predict,” “project,” “potential,” “believe,” “continue,” “assume,” “intend,” “plan,” and “estimate,” as well as similar expressions, are meant to identify such forward-looking statements. Potential risks and uncertainties that could cause our actual results to differ from those anticipated in any forward-looking statements include, but are not limited to, those described below under Item 1 A. Risk Factors and the following:

- The impact of the outbreak of the novel coronavirus, or COVID-19, on our business, including the impact of the actions taken by governmental authorities to try and contain the virus or address the impact of the virus on the United States economy (including, without limitation, the Coronavirus Aid, Relief and Economic Security Act, or the CARES Act), and the resulting effect of these items on our operations, liquidity and capital position, and on the financial condition of our borrowers and other customers;
- Restrictions or conditions imposed by our regulators on our operations;
- Increases in competitive pressure in the banking and financial services industries;
- Changes in access to funding or increased regulatory requirements with regard to funding;
- Changes in deposit flows;
- Credit losses as a result of declining real estate values, increasing interest rates, increasing unemployment, changes in payment behavior or other factors;
- Credit losses due to loan concentration;
- Changes in the amount of our loan portfolio collateralized by real estate and weaknesses in the real estate market;
- Our ability to successfully execute our business strategy;
- Our ability to attract and retain key personnel;
- The success and costs of our expansion into the Charlotte, North Carolina, Greensboro, North Carolina and Atlanta, Georgia markets and into potential new markets;
- Changes in the interest rate environment which could reduce anticipated or actual margins;
- Changes in political conditions or the legislative or regulatory environment, including governmental initiatives affecting the financial services industry, including as a result of the new presidential administration and Democratic control of Congress;
- Changes in economic conditions resulting in, among other things, a deterioration in credit quality;
- Changes occurring in business conditions and inflation;
- Increased cybersecurity risk, including potential business disruptions or financial losses;
- Changes in technology;
- The adequacy of the level of our allowance for loan losses and the amount of loan loss provisions required in future periods;
- Examinations by our regulatory authorities, including the possibility that the regulatory authorities may, among other things, require us to increase our allowance for loan losses or write-down assets;
- Changes in monetary and tax policies;
- The rate of delinquencies and amounts of loans charged-off;
- The rate of loan growth in recent years and the lack of seasoning of a portion of our loan portfolio;

- Our ability to maintain appropriate levels of capital and to comply with our capital ratio requirements;
- Adverse changes in asset quality and resulting credit risk-related losses and expenses;
- Changes in accounting policies and practices;
- Risks associated with actual or potential litigation or investigations by customers, regulatory agencies or others;
- Adverse effects of failures by our vendors to provide agreed upon services in the manner and at the cost agreed;
- The potential effects of events beyond our control that may have a destabilizing effect on financial markets and the economy, such as epidemics and pandemics (including COVID-19), war or terrorist activities, disruptions in our customers' supply chains, disruptions in transportation, essential utility outages or trade disputes and related tariffs; and
- Other risks and uncertainties detailed in this Annual Report on Form 10-K and, from time to time, in our other filings with the Securities and Exchange Commission ("SEC").

If any of these risks or uncertainties materialize, or if any of the assumptions underlying such forward-looking statements proves to be incorrect, our results could differ materially from those expressed in, implied or projected by, such forward-looking statements. For information with respect to factors that could cause actual results to differ from the expectations stated in the forward-looking statements, see "Risk Factors" under Part I, Item 1A of this Annual Report on Form 10-K. We urge investors to consider all of these factors carefully in evaluating the forward-looking statements contained in this Annual Report on Form 10-K. We make these forward-looking as of the date of this document and we do not intend, and assume no obligation, to update the forward-looking statements or to update the reasons why actual results could differ from those expressed in, or implied or projected by, the forward-looking statements, except as required by applicable law.

PART I

Item 1. Business

General

Southern First Bancshares, Inc. (the "Company") was incorporated in March 1999 under the laws of South Carolina and is a bank holding company registered under the Bank Holding Company Act of 1956. Our primary business is to serve as the holding company for Southern First Bank (the "Bank"), a South Carolina state bank. The Bank is a commercial bank with eight retail offices located in the Greenville, Columbia, and Charleston markets of South Carolina, two retail offices in the Raleigh and Greensboro markets of North Carolina and one retail office in Atlanta, Georgia. As of February 3, 2021, we have obtained approval to open a retail office in the Charlotte, North Carolina market.

The Bank is primarily engaged in the business of accepting demand deposits and savings deposits insured by the Federal Deposit Insurance Corporation (the "FDIC"), and providing commercial, consumer and mortgage loans to the general public.

The Company's reportable segments represent the distinct product lines the Company offers and are viewed separately for strategic planning purposes by management. The three segments include Commercial and Retail Banking, Mortgage Banking, and Corporate Operations as described below.

Commercial and Retail Banking. The Company's primary business is to provide traditional deposit and lending products and services to its commercial and retail banking clients. The commercial and retail banking segment employs 220 of the Company's full-time equivalent ("FTE") employees.

Mortgage Banking. The mortgage banking segment provides mortgage loan origination services for loans that will be sold in the secondary market to investors and employs 34 FTE employees.

Corporate Operations. Corporate operations is comprised primarily of compensation and benefits for certain members of management and interest on company debt. There are no direct employees of corporate operations, however a portion of the salaries related to executive management and finance are allocated to this segment.

Unless the context requires otherwise, references to the "Company," "we," "us," "our," or similar references mean Southern First Bancshares, Inc. and its subsidiaries.

Our Competitive Strengths
We believe that the following business strengths have been instrumental to the success of our core operations. We believe these attributes will enable us to continue profitable growth, while remaining fundamentally sound and driving value to our shareholders.

Simple and Efficient ClientFIRST Model. We operate our Bank using a simple and efficient style of banking that is focused on providing core banking products and services to our clients through a team of talented and experienced bankers. We refer to this model as “ClientFIRST” and it is structured to deliver superior client service via “relationship teams,” which provide each client with a specific banker contact and a consistent support team responsible for all of the client’s banking needs. We believe this model results in a consistent and superior level of professional service that provides us with a distinct competitive advantage by enabling us to build and maintain long-term relationships with desirable clients, enhancing the quality and stability of our funding and lending operations and positioning us to take advantage of future growth opportunities in our existing markets. We also believe that this client focused culture has led to our successful expansion into new markets in the past, and will enable us to be successful if we seek to expand into new markets in the future.

Our ClientFIRST model focuses on achieving cost efficiencies by diligently managing the growth of our number of employees and banking offices. We believe that the identification of talented bankers will drive our growth strategy, as opposed to a more general desire to enter a specific geography or market. This strategy translates into a smaller number of brick and mortar offices relative to our size and compared to peer banks, but larger overall deposit balances in our offices as compared to peers. As a result, our offices average approximately $192.8 million in total deposits. We believe this style of banking allows us to deliver exceptional client service, while achieving lower efficiency ratios relative to certain of our local competitors, as evidenced by our 50.2% efficiency ratio for the year ended December 31, 2020.

We continue to make significant investments in our IT systems and technology offerings to our clients that we believe will continue to drive low-cost deposit growth. We believe that our current mobile banking, on-line banking and cash management offerings are industry-leading solutions amongst community banks, and we plan to continue to invest in the latest technology solutions to ensure we meet the evolving needs of our clients and maintain this competitive advantage over other community banks.

Attractive South Carolina, North Carolina and Georgia Markets. We have eight banking offices located in Greenville, Columbia and Charleston, South Carolina, which are the three largest markets in South Carolina, two banking offices located in Raleigh and Greensboro, North Carolina, which are the second and third largest markets in North Carolina, respectively, and one banking office located in Atlanta, Georgia, which is the largest market in Georgia. The following table illustrates our market share, by insured deposits as of the dates indicated, in these six markets:

Market[1]	Total Offices	Our Market Deposits at June 30, 2020	Total Market Deposits[2]
		(Dollars in thousands)	
Greenville	4	$ 1,058,852	$ 20,841,299
Charleston	3	520,189	17,469,438
Columbia	1	345,834	24,167,787
Atlanta	1	158,661	193,980,517
Raleigh	1	71,387	34,603,975
Greensboro	1	33,721	15,329,756

(1) Represents the metropolitan statistical area (“MSA”) for each market.
(2) The total market deposits data displayed are as of June 30, 2020 as reported by the FDIC.

Greenville. The city of Greenville is located in Greenville County, South Carolina approximately midway between Atlanta and Charlotte on the heavily traveled I-85 business corridor. The Greenville-Anderson MSA is the most populous market in South Carolina with an estimated 920,477 residents as of 2019. The median household income for the Greenville-Anderson MSA was $55,790 for 2019. A large and diverse metropolitan area, the Greenville-Anderson-Mauldin MSA is one of the southeast region’s premier areas for business, serving as headquarters for Michelin and Hubbell Lighting as well as hosting significant operations for BMW and Lockheed Martin.

Columbia. The city of Columbia is located in Richland County, South Carolina and its surrounding suburban areas expand into adjoining Lexington County. Columbia is the state capital, the largest city in the state and the home of the University of South Carolina and Fort Jackson, the Army’s largest Initial Entry Training Center. The Columbia MSA is the second most populous market in the state with an estimated population of 838,433 residents as of 2019. The median household income for the Columbia MSA was $53,765 for 2019.

Charleston. The city of Charleston is located in Charleston County, South Carolina. The Charleston-North Charleston MSA is the third most populous market in the state with an estimated population of 802,122 residents as of 2019. Charleston is home to the deepest port in the Southeast and boasts top companies in the aerospace, biomedical and technology fields such as Boeing, the Medical University of South Carolina (MUSC) and Blackbaud. The median household income for the Charleston-North Charleston MSA was approximately $64,283 for 2019. One of our retail offices in the Charleston market is located in the city of Mount Pleasant, which is located just north of Charleston in Charleston County and ranks as the fourth largest city in South Carolina.

Raleigh. The city of Raleigh is the second largest city in the state and is located in Wake County, North Carolina. The Raleigh-Cary MSA is one of the most populous markets in the state of North Carolina with an estimated population of 1.39 million residents as of 2019. Raleigh is the state capital and is home to North Carolina State University and is part of the Research Triangle area, together with Durham, North Carolina (home of Duke University) and Chapel Hill, North Carolina (home of the University of North Carolina at Chapel Hill). The median household income for the Raleigh MSA was approximately $75,165 for 2019.

Greensboro. The city of Greensboro is the third largest city in North Carolina and is located in Guilford County. The Greensboro-High Point MSA has an estimated population of 771,851 residents as of 2019. Greensboro has traditionally been a fixture in the textiles, tobacco and furniture industries while also moving towards an increased presence of high-tech, aviation and transportation/logistics sectors. Greensboro, along with Winston-Salem and High Point, is commonly referred to as the Triad region of North Carolina and is home to companies such as Honda Aircraft, Lincoln Financial Group and Volvo Trucks of North America. The median household income for the Greensboro MSA was approximately $50,026 for 2019.

Atlanta. The Atlanta-Sandy Springs-Alpharetta MSA has the ninth largest population in the U.S. with 6.02 million residents as of 2019. Atlanta is the state capital of, and largest city in, Georgia and is the world headquarters of corporations such as Coca-Cola, Home Depot, UPS, Delta Airlines and Turner Broadcasting. The median household income for the Atlanta MSA is $69,464.

We believe that the demographics and growth characteristics of these six markets will provide us with significant opportunities to further develop existing client relationships and expand our client base.

In addition, on February 3, 2021, we obtained regulatory approval to open a retail office in the Charlotte, North Carolina market. The Charlotte-Concord-Gastonia MSA is among the top 25 largest populations in the U.S. with 2.64 million residents as of 2019. Charlotte is the largest manufacturing region in the Carolinas and is the second largest financial hub in the country. Charlotte is also home to many Fortune 500 companies including Duke Energy, Honeywell and Lowe’s. The median household income for the Charlotte MSA was $69,464 in 2019. We believe that our entrance into the Charlotte market will provide us with further opportunity to expand our client base.

Experienced Management Team, Dedicated Board of Directors and Talented Employees. Our senior management team is led by R. Arthur Seaver, Jr., Michael D. Dowling, Calvin C. Hurst and Silvia T. King whose biographies are included below. These executives lead a team of 23 additional senior team members which we believe compares favorably to any community bank management team assembled in South Carolina.

R. Arthur “Art” Seaver, Jr. has served as the Chief Executive Officer of our Company and our Bank since 1999. He has over 30 years of banking experience. From 1986 until 1992, Mr. Seaver held various positions with The Citizens & Southern National Bank of South Carolina. From 1992 until February 1999, he was with Greenville National Bank, which was acquired by Regions Bank in 1998. He was the Senior Vice President in lending and was also responsible for managing Greenville National Bank’s deposit strategies prior to leaving to form the Bank. Mr. Seaver is a 1986 graduate of Clemson University with a bachelor’s degree in Financial Management and a 1999 graduate of the BAI Graduate School of Community Bank Management.

Michael D. Dowling has served as an Executive Vice President and the Chief Financial Officer of our Company and our Bank since 2011 and as Chief Operating Officer since July 2019. He has over 25 years of experience in the banking industry. Mr. Dowling was previously employed with KPMG LLP from 1994 until 2011, including most recently as an Audit Partner (2005-2011) and a member of KPMG’s Financial Services practice. Mr. Dowling has extensive experience working with public companies and financial institutions. He is a 1993 graduate of Clemson University, with a degree in Accounting and is a CPA in South Carolina and North Carolina.

Calvin C. Hurst has served as Chief Banking Officer of our Company and our Bank since March 2019. Mr. Hurst has over 14 years of banking experience. From 2006 to 2008, Mr. Hurst served as a commercial underwriter for RBC Bank, and from 2008 to 2015 he served as commercial relationship manager for PNC Bank. Before joining Southern First, Mr. Hurst served as regional vice president for TD Bank. Mr. Hurst is a 2005 graduate of Furman University, with a Bachelor’s degree in Business Administration and Economics.

Silvia T. King has served as Chief Human Resources Officer of our Company and our Bank since March 2018. Ms. King has over 17 years of Human Resources leadership experience. From 2003 to 2006, Ms. King served in various human resource roles with Monsanto Company and from 2007 to 2009, she served in senior management roles with Select Comfort Corporation. From 2009 to 2016, Ms. King served as senior human resources consultant for FGP International, a professional staffing firm in Greenville, South Carolina, and most recently as a human resources instructor with e-Cornell University. Ms. King holds degrees in Psychology and International Marketing from Clemson University and a Master of Human Resources degree from the University of South Carolina. She has also earned both her Senior Professional in Human Resources through the HR Certification Institute as well as her Senior Certified Professional designations through the Society of Human Resource Management.

In addition to Messrs. Seaver, Dowling, and Hurst and Ms. King, our executive management team consists of nine individuals who bring an average of 29 years of experience in the banking industry.

The management team is complemented by our dedicated board of directors with extensive local market knowledge and a wide range of experience including accounting, business, banking, manufacturing, insurance, management and finance. We believe that our management’s and board’s incentives are closely aligned with our shareholders through the ownership of a substantial amount of our stock. As of December 31, 2020, our executive officers and board of directors owned an aggregate of 580,606 shares of our common stock, including options to purchase shares of our common stock, which represented approximately 7.41% of the fully-diluted amount of our common stock outstanding. We believe that our officers’ and directors’ experience and local market knowledge are valuable assets and will enable them to guide us successfully in the future.

In addition, we believe that we have assembled a group of highly talented employees by being an employer of choice in the markets we serve. We employed a total of 254 FTE employees as of December 31, 2020. Our employees are skilled in the areas of banking, information technology, management, sales, advertising and marketing, among others. We strive to provide an “umbrella for great talent,” characterized by a culture of transparency and collaboration which permeates all levels of the organization. To drive our culture of transparency and collaboration, our employees engage in a series of weekly meetings to understand the goals and plan for each week. These meetings are intended to remind our employees of our vision, strategy and ClientFIRST service, and provide our employees with information regarding monthly and quarterly goals and client or prospect needs. In addition, each week is started with a meeting of all Senior and Executive Vice Presidents to ensure that all team members are informed on the latest developments of our Company. Our employees and their ClientFIRST approach to service have been instrumental to our success.

Our Business Strategy

We are focused on growing business relationships and building core deposits, profitable loans and noninterest income. We believe that we have built a dynamic franchise that meets the financial needs of our clients by providing an array of personalized products and services delivered by seasoned banking professionals with knowledge of our local markets. Our overall strategic goal is to provide the highest level of service to our clients while achieving high-performance metrics within the community banking market that drive franchise and shareholder value. Our specific business strategies include:

Focus on Profitable and Efficient Growth. Our executive management team and board of directors are dedicated to producing profits and returns for our shareholders. We actively manage the mix of assets and liabilities on our balance sheet to optimize our net interest margin while also maintaining expense controls and developing noninterest income streams. By continually striving to build a well-structured balance sheet, we seek to increase profitability and improve our return on average assets, return on average equity and efficiency ratio. We believe that, as the economy continues to improve, our focus on maximizing our net interest margin and minimizing our efficiency ratio while maintaining credit quality controls will translate into continued and improved profitability and shareholder returns. We are committed to enhancing these levels of profitability by focusing on our core competencies of commercial lending and core deposit gathering. We believe that we have the infrastructure currently in place, such as technology, support staff and administration, to support expansion with limited associated noninterest expense increases.

Provide a Distinctive Client Experience. Our markets have been subject to consolidation of local community banks primarily by larger, out-of-state financial institutions. We believe there is a large client base in our markets that prefers doing business with a local institution and may be dissatisfied with the service offered by national and larger regional banks. We believe that the exceptional level of professional service provided to our clients as a result of our ClientFIRST model provides us with a distinct competitive advantage over our local competitors. We also believe that technology innovation will continue to play a critical role in retaining clients and winning new business. We believe that our current mobile banking, on-line banking and cash management offerings are industry-leading solutions amongst community banks. During 2020, 74% of deposits were acquired through our office network, 21% came through the commercial remote deposit capture channel and the remaining 5% came through consumer mobile deposits. We believe that the volume in remote deposit capture and mobile deposit channels will continue to increase over time as more clients become acquainted with the convenience these services provide. By delivering superior professional service through our ClientFIRST model, coupled with our deep understanding of our markets and our commitment to providing the latest technology solutions to meet our clients' banking needs, we believe that we can attract new clients and expand our total loans and deposits.

Maintain a Rigorous Risk Management Infrastructure. As we grow, one of our top priorities is to continue to build a robust enterprise risk management infrastructure. We believe effective risk management requires a culture of risk management and governance throughout the Company. The legislative and regulatory landscape continues to quickly evolve, so we are continually performing risk assessments throughout the organization and re-allocating resources where appropriate. We will continue to add new resources and technology investments to help enhance all of our risk management processes throughout the Bank. Our risk management success is exemplified by our historic credit risk management and disciplined underwriting practices, which have enabled us to successfully grow our balance sheet while maintaining strong credit quality metrics. We do not reduce our credit standards or pricing discipline to generate new loans. In addition, we are heavily focused on compliance risk and cybersecurity risk, as both of these risks have increased since our inception. Our management team continually analyzes emerging fraud and security risks and utilizes tools, strategies and policies to manage risk while delivering an optimal and appropriate client experience. We believe our risk management structure allows our board and senior management to maintain effective oversight of our risks to ensure that our personnel are following prudent and appropriate risk management practices resulting in strong loan quality and minimal loan losses.

Attract Talented Banking Professionals With A "ClientFIRST" Focus. We believe that our ability to attract and retain banking professionals with strong community relationships and significant knowledge of our markets will continue to drive our success and grow our business in an efficient manner. By focusing on experienced, established bankers who deliver exceptional client service through our ClientFIRST model, we believe we can enhance our market position and add profitable growth opportunities. We believe that the strength of our exceptional client service and relationship banking approach will continue to help us attract these established bankers. In recent years, we have invested in our internal infrastructure, including support and back office personnel, and we believe that we can continue to add experienced frontline bankers to our existing markets, which will drive our efficient growth.

We will continue to expand our franchise, but only in a controlled manner. We may choose to open new locations, but only after rigorous due diligence and substantial quantitative analysis regarding the financial and capital impacts of such investments. We may also choose to enter new metropolitan markets contiguous to, or nearby, our current South Carolina footprint, such as our recently opened expansions in Greensboro and Charlotte, North Carolina, but only after careful study and the identification and vetting of a local, senior level banking team with significant experience and reputational strength in that market. We have not yet supplemented our historic strategy of organic deposit and loan growth with traditional mergers or acquisitions. We evaluate potential acquisition opportunities that we believe would be complementary to our business as part of our growth strategy. However, we have not yet identified any specific acquisition opportunity that meets our strict requirements and do not have any immediate plans, arrangements or understandings relating to any acquisition. Furthermore, we do not believe an acquisition is necessary to successfully drive our growth and execute our ClientFIRST model.

Lending Activities

General. We emphasize a range of lending services, including real estate, commercial, and equity-line consumer loans to individuals and small- to medium-sized businesses and professional firms that are located in or conduct a substantial portion of their business in our market area. Our underwriting standards vary for each type of loan, as described below. Because loans typically provide higher interest yields than other types of interest-earning assets, we invest a substantial percentage of our earning assets in our loan portfolio. At December 31, 2020, we had net loans of $2.10 billion, representing 84.5% of our total assets.

We have focused our lending activities primarily on the professional markets in Greenville, Columbia, Charleston, Raleigh, Greensboro and Atlanta including doctors, dentists, and small business owners. By focusing on this client base and by serving each client with a consistent relationship team of bankers, we have generated a loan portfolio with larger average loan amounts than we believe is typical for a community bank. As of December 31, 2020, our average loan size was approximately $275,000. Excluding home equity lines of credit, the average loan size was approximately $336,000. At the same time, we have strived to maintain a diversified loan portfolio and limit the amount of our loans to any single client. As of December 31, 2020, our 10 largest client loan relationships represented approximately $188.5 million, or 8.80%, of our loan portfolio.

Loan Approval. Certain credit risks are inherent in making loans. These include prepayment risks, risks resulting from uncertainties in the future value of collateral, risks resulting from changes in economic and industry conditions, and risks inherent in dealing with individual borrowers. We attempt to mitigate repayment risks by adhering to internal credit policies and procedures. These policies and procedures include officer and client lending limits, a multi-layered approval process for larger loans, documentation examination, and follow-up procedures for any exceptions to credit policies. Our loan approval policies provide for various levels of officer lending authority. When the amount of aggregate loans to a single borrower exceeds an individual officer's lending authority, the loan request will be considered for approval by a team of officers led by a senior lender, or by the voting members of the Credit Approval Support Team ("CAST") committee, based on the loan amount. The CAST committee, which is comprised of a group of our senior commercial lenders, chief banking officer, and chief executive officer, has pre-determined lending limits, and any loans in excess of this lending limit will be submitted for approval by the finance committee of our board or by the full board. We do not make any loans to any director or executive officer of the Bank unless the loan is approved by the board of directors of the Bank and all loans to directors, officers and employees are on terms not more favorable to such person than would be available to a person not affiliated with the Bank, consistent with federal banking regulations.

Management monitors exposure to credit risk from potential concentrations of loans to particular borrowers or groups of borrowers, industries and geographic regions, as well as concentrations of lending products and practices such as loans that subject borrowers to substantial payment increases (e.g. principal deferral periods, loans with initial interest-only periods, etc.), and loans with high loan-to-value ratios. These types of loans are subject to strict underwriting standards and are more closely monitored than a loan with a low loan-to-value ratio. Furthermore, there are industry practices that could subject us to increased credit risk should economic conditions change over the course of a loan's life. For example, we make variable rate loans and fixed rate principal-amortizing loans with maturities prior to the loan being fully paid (i.e. balloon payment loans). The various types of loans are individually underwritten and monitored to manage the associated risks.

Credit Administration and Loan Review. We maintain a continuous loan review system. We also apply a credit grading system to each loan, and we use an independent process to review the loan files on a test basis to assess the grading of each loan. We periodically review performance benchmarks established by management in the areas of nonperforming assets, charge-offs, past dues, and loan documentation. Each loan officer is responsible for each loan he or she makes, regardless of whether other individuals or committees joined in the approval. This responsibility continues until the loan is repaid or until the loan is officially assigned to another officer.

Lending Limits. Our lending activities are subject to a variety of lending limits imposed by federal and state laws and regulations. In general, the Bank is subject to a legal limit on loans to a single borrower equal to 15% of the Bank's capital and unimpaired surplus. Based upon the capitalization of the Bank at December 31, 2020, the maximum amount we could lend to one borrower was $44.7 million. However, to mitigate concentration risk, our internal lending limit at December 31, 2020 was $31.3 million and may vary based on our assessment of the lending relationship. The board of directors will adjust the internal lending limit as deemed necessary to continue to mitigate risk and serve our clients. The Bank's legal lending limit will increase or decrease in response to increases or decreases in the Bank's level of capital. We are able to sell participations in our larger loans to other financial institutions, which allow us to manage the risk involved in these loans and to meet the lending needs of our clients requiring extensions of credit in excess of these limits.

Loan Portfolio Segments. Our loan portfolio is comprised of commercial and consumer loans made to small businesses and individuals for various business and personal purposes. While our loan portfolio is not concentrated in loans to any single borrower or a relatively small number of borrowers, the principal component of our loan portfolio is loans secured by real estate mortgages on either commercial or residential property. These loans will generally fall into one of the following six categories: commercial owner occupied real estate, commercial non-owner occupied real estate, commercial construction, consumer real estate, consumer construction, and home equity loans. We obtain a security interest in real estate whenever possible, in addition to any other available collateral, in order to increase the likelihood of the ultimate repayment of the loan. At December 31, 2020, loans secured by first or second mortgages on commercial and consumer real estate made up approximately 84.6% of our loan portfolio. In addition to loans secured by real estate, our loan portfolio includes commercial business loans and other consumer loans which comprised 14.4% and 1.0%, respectively, of our total loan portfolio at December 31, 2020.

Interest rates for all real estate loan categories may be fixed or adjustable, and will more likely be fixed for shorter-term loans. We generally charge an origination fee for each loan which is taken into income over the life of the loan as an adjustment to the loan yield. Other loan fees consist primarily of late charge fees. Real estate loans are subject to the same general risks as other loans and are particularly sensitive to fluctuations in the value of real estate. Fluctuations in the value of real estate, as well as other factors arising after a loan has been made, could negatively affect a borrower's cash flow, creditworthiness, and ability to repay the loan. Although, the loans are collateralized by real estate, the primary source of repayment may not be the sale of real estate.

The following describes the types of loans in our loan portfolio.

- *Commercial Real Estate Loans (Commercial Owner Occupied and Commercial Non-owner Occupied Real Estate Loans).* At December 31, 2020, commercial owner occupied and non-owner occupied real estate loans (other than construction loans) amounted to $1.02 billion, or 47.5% of our loan portfolio. Of our commercial real estate loan portfolio, $585.3 million in loans were non-owner occupied properties, representing 42.2% of our commercial loan portfolio and 27.3% of our total loan portfolio. The remainder of our commercial real estate loan portfolio, $433.3 million in loans or 31.2% of the commercial loan portfolio, were owner occupied. Owner occupied loans represented 20.2% of our total loan portfolio. At December 31, 2020, our individual commercial real estate loans ranged in size from approximately $10,000 to $23.6 million, with an average loan size of approximately $730,000. These loans generally have terms of five years or less, although payments may be structured on a longer amortization basis. We evaluate each borrower on an individual basis and attempt to determine the business risks and credit profile of each borrower. We attempt to reduce credit risk in the commercial real estate portfolio by emphasizing loans on owner-occupied office and retail buildings where the loan-to-value ratio, established by independent appraisals, does not exceed 85%. We also generally require that a borrower's cash flow exceeds 115% of monthly debt service obligations. In order to ensure secondary sources of payment and liquidity to support a loan request, we typically review all of the personal financial statements of the principal owners and require their personal guarantees.

- *Construction Real Estate Loans.* We offer adjustable and fixed rate construction real estate loans for commercial and consumer projects, typically to builders and developers and to consumers who wish to build their own homes. At December 31, 2020, total commercial and consumer construction loans amounted to $102.0 million, or 4.8% of our loan portfolio. Commercial construction loans represented $61.5 million, or 2.9%, of our total loan portfolio, while consumer construction loans represented $40.5 million, or 1.9% of our total loan portfolio. At December 31, 2020, our commercial construction real estate loans ranged in size from approximately $50,000 to $12.5 million, with an average loan balance of approximately $1.5 million. At December 31, 2020, our consumer or residential construction loans ranged in size from approximately $25,000 to $2.2 million, with an average loan size of approximately $395,000. The duration of our construction loans generally is limited to 18 months, although payments may be structured on a longer amortization basis. Commercial construction loans generally carry a higher degree of risk than long-term financing of existing properties because repayment depends on the ultimate completion of the project and sometimes on the sale of the property. Specific risks include:

  - cost overruns;
  - mismanaged construction;
  - inferior or improper construction techniques;
  - economic changes or downturns during construction;
  - a downturn in the real estate market;
  - rising interest rates which may prevent sale of the property; and
  - failure to sell completed projects in a timely manner.

  We attempt to reduce the risk associated with construction loans by obtaining personal guarantees where possible and by keeping the loan-to-value ratio of the completed project at or below 80%.

- *Commercial Business Loans.* We make loans for commercial purposes in various lines of businesses, including the manufacturing, service industry, and professional service areas. At December 31, 2020, commercial business loans amounted to $307.6 million, or 14.4% of our loan portfolio, and ranged in size from approximately $5,000 to $13.4 million, with an average loan size of approximately $197,000. Commercial loans are generally considered to have greater risk than first or second mortgages on real estate because commercial loans may be unsecured, or if they are secured, the value of the collateral may be difficult to assess and more likely to decrease than real estate.

  We are eligible to offer small business loans utilizing government enhancements such as the Small Business Administration’s (“SBA”) 7(a) program and SBA’s 504 programs. These loans typically are partially guaranteed by the government, which helps to reduce their risk. Government guarantees of SBA loans do not exceed, and are generally less than, 80% of the loan. As of December 31, 2020, we had originated one loan utilizing government enhancements.

- *Consumer Real Estate Loans and Home Equity Loans.* At December 31, 2020 consumer real estate loans (other than construction loans) amounted to $693.3 million, or 32.4% of our loan portfolio. Included in the consumer real estate loans was $536.3 million, or 25.0% of our loan portfolio, in first and second mortgages on individuals’ homes, while home equity loans represented $157.0 million, or 7.3% of our total loan portfolio. At December 31, 2020, our individual residential real estate loans ranged in size from $10,000 to $5.9 million, with an average loan size of approximately $434,000. Generally, we limit the loan-to-value ratio on our consumer real estate loans to 85%. We offer fixed and adjustable rate consumer real estate loans with terms of up to 30 years. We typically offer these long-term fixed rate loans through a third party rather than originating and retaining these loans ourselves. Consumer real estate and home equity loans that we retain on our balance sheet typically have terms of 10 years or less. We also offer home equity lines of credit. At December 31, 2020, our individual home equity lines of credit ranged in size from $5,000 to $2.0 million, with an average of approximately $84,000. Our underwriting criteria and the risks associated with home equity loans and lines of credit are generally the same as those for first mortgage loans. Home equity lines of credit typically have terms of ten years or less. We generally limit the extension of credit to 90% of the market value of each property, although we may extend up to 100% of the market value.

- *Other Consumer Loans.* We make a variety of loans to individuals for personal and household purposes, including secured and unsecured installment loans and revolving lines of credit. These consumer loans are underwritten based on the borrower’s income, current debt level, past credit history, and the availability and value of collateral. Consumer rates are both fixed and variable, with negotiable terms. At December 31, 2020, consumer loans other than real estate amounted to $21.4 million, or 1.0% of our loan portfolio, and ranged in size from $5,000 to $1.8 million, with an average loan size of approximately $14,000. Our installment loans typically amortize over periods up to 60 months. We will offer consumer loans with a single maturity date when a specific source of repayment is available. We typically require monthly payments of interest and a portion of the principal on our revolving loan products. Consumer loans are generally considered to have greater risk than first or second mortgages on real estate because they may be unsecured, or, if they are secured, the value of the collateral may be difficult to assess and more likely to decrease in value than real estate.

Deposit Services

Our principal source of funds is core deposits. We offer a full range of deposit services, including checking accounts, commercial checking accounts, savings accounts, and other time deposits of various types, ranging from daily money market accounts to long-term certificates of deposit. Our out-of-market, or wholesale, certificates of deposits represented $22.0 million, or 0.9%, of total deposits at December 31, 2020. In an effort to obtain lower cost deposits, we have focused on expanding our retail deposit program. We currently have 11 retail offices which assist us in obtaining low cost transaction accounts that are less affected by rising rates. Deposit rates are reviewed regularly by our senior management. We believe that the rates we offer are competitive with those offered by other financial institutions in our area. We focus on client service and our ClientFIRST culture to attract and retain deposits.

Other Banking Services

In addition to deposit and loan services, we offer other bank services such as internet banking, cash management, safe deposit boxes, direct deposit, automatic drafts, bill payment and mobile banking services. We earn fees for most of these services, including debit and credit card transactions, sales of checks, and wire transfers. We also receive ATM transaction fees from transactions performed by our clients. We are associated with the NYCE, Pulse, STAR, and Cirrus networks, which are available to our clients throughout the country. Since we outsource our ATM services, we are charged related transaction fees from our ATM service provider. We have contracted with Fidelity National Information Systems, an outside computer service company, to provide our core data processing services and our ATM processing. By outsourcing these services, we believe we are able to reduce our overhead by matching the expense in each period to the transaction volume that occurs during the period, as a significant portion of the fee charged is directly related to the number of loan and deposit accounts and the related number of transactions we have during the period. We believe that by being associated with a shared network of ATMs, we are better able to serve our clients and are able to attract clients who are accustomed to the convenience of using ATMs, although we do not believe that maintaining this association is critical to our success. We also offer Internet banking services, bill payment services, and cash management and mobile banking services.

Competition

The banking business is highly competitive, and we experience competition in our market from many other financial institutions. Competition among financial institutions is based upon interest rates offered on deposit accounts, interest rates charged on loans, other credit and service charges relating to loans, the quality and scope of the services rendered, the convenience of banking facilities, and, in the case of loans to commercial borrowers, relative lending limits. We compete with commercial banks, credit unions, savings and loan associations, mortgage banking firms, consumer finance companies, securities brokerage firms, insurance companies, money market funds, and other mutual funds, as well as other super-regional, national, and international financial institutions that operate offices in Greenville, Columbia and Charleston, South Carolina; Raleigh and Greensboro, North Carolina; Atlanta, Georgia and elsewhere.

As of June 30, 2020, the most recent date for which market data is available, there were 30 financial institutions in our primary market of Greenville County, 17 financial institutions in the Columbia market, 28 financial institutions in the Charleston market, 33 financial institutions in the Raleigh market, 22 financial institutions in the Greensboro market and 47 financial institutions in the Atlanta market. We compete with other financial institutions in our market areas both in attracting deposits and in making loans. In addition, we have to attract our client base from other existing financial institutions and from new residents. Many of our competitors are well-established, larger financial institutions with substantially greater resources and lending limits, such as, Bank of America, Wells Fargo, and Truist. These institutions offer some services, such as extensive and established branch networks and trust services that we do not provide. In addition, many of our non-bank competitors are not subject to the same extensive federal regulations that govern bank holding companies and federally insured banks. We believe the financial services industry will likely continue to become more competitive as further technological advances enable more financial institutions to provide expanded financial services without having a physical presence in our markets. Because larger competitors have advantages in attracting business from larger corporations, we do not generally compete for that business. Instead, we concentrate our efforts on attracting the business of individuals and small and medium-size businesses. With regard to such accounts, we generally compete on the basis of client service and responsiveness to client needs, the convenience of our offices and hours, and the availability and pricing of our products and services.

We believe our commitment to quality and personalized banking services through our ClientFIRST culture is a factor that contributes to our competitiveness and success.

Employees

At December 31, 2020, we employed a total of 254 FTE employees. We provide our full-time employees and certain part-time employees with a comprehensive program of benefits, including medical benefits, life insurance, long-term disability coverage and a 401(k) plan. Our employees are not represented by a collective bargaining agreement. Management considers its employee relations to be excellent.

Available Information

We file Annual Reports on Form 10-K, Quarterly Reports on Form 10-Q, and Current Reports on Form 8-K with the SEC which are accessible electronically at the SEC's website at **www.sec.gov.** We maintain an Internet website at www.southernfirst.com where these reports can also be accessed free of charge. No information contained on our website is intended to be included as part of, or incorporated by reference into, this Annual Report on Form 10-K.

SUPERVISION AND REGULATION

Both the Company and the Bank are subject to extensive state and federal banking laws and regulations that impose specific requirements or restrictions on and provide for general regulatory oversight of virtually all aspects of our operations. These laws and regulations are generally intended to protect depositors, not shareholders. Changes in applicable laws or regulations may have a material effect on our business and prospects.

The following discussion is not intended to be a complete list of all the activities regulated by the banking laws or of the impact of such laws and regulations on our operations. It is intended only to briefly summarize some material provisions. The following summary is qualified by reference to the statutory and regulatory provisions discussed.

Legislative and Regulatory Developments

Although the 2008 financial crisis has now passed, two legislative and regulatory responses – the Dodd-Frank Wall Street Reform and Consumer Protection Act (the "Dodd-Frank Act") and the Basel III-based capital rules – will continue to have an impact on our operations.

In addition, newer regulatory developments implemented in response to the COVID-19 pandemic, including the CARES Act and the Consolidated Appropriations Act, 2021, which enhanced and expanded certain provisions of the CARES Act, have had and will continue to have an impact on our operations.

The Dodd-Frank Wall Street Reform and Consumer Protection Act

The Dodd-Frank Act was signed into law in July 2010 and impacts financial institutions in numerous ways, including:

- The creation of a Financial Stability Oversight Council responsible for monitoring and managing systemic risk,
- Granting additional authority to the Board of Governors of the Federal Reserve (the "Federal Reserve") to regulate certain types of nonbank financial companies,
- Granting new authority to the FDIC as liquidator and receiver,
- Changing the manner in which deposit insurance assessments are made,
- Requiring regulators to modify capital standards,
- Establishing the Consumer Financial Protection Bureau (the "CFPB"),
- Capping interchange fees that banks charge merchants for debit card transactions,
- Imposing more stringent requirements on mortgage lenders, and
- Limiting banks' proprietary trading activities.

There are many provisions in the Dodd-Frank Act mandating regulators to adopt new regulations and conduct studies upon which future regulation may be based. While some have been issued, many remain to be issued. Governmental intervention and new regulations could materially and adversely affect our business, financial condition and results of operations.

The Economic Growth, Regulatory Relief, and Consumer Protection Act

On May 24, 2018, President Trump signed into law the first major financial services reform bill since the enactment of the Dodd-Frank Act. The Economic Growth, Regulatory Relief, and Consumer Protection Act (the "Reform Law") modifies or eliminates certain requirements on community and regional banks and nonbank financial institutions. For instance, under the Reform Act and related rule making:

- banks that have less than $10 billion in total consolidated assets and total trading assets and trading liabilities of less than five percent of total consolidated assets from Section 619 of the Dodd-Frank Act, known as the "Volcker Rule", which prohibits "proprietary trading" and the ownership or sponsorship of private equity or hedge funds that are referred to as "covered funds";
- the asset threshold for bank holding companies to qualify for treatment under the "Small Bank Holding Company and Savings and Loan Holding Company Policy Statement" was raised from $1 billion to $3 billion, which exempts these institutions (including the Company) from certain regulatory requirements including the Basel III capital rules;
- a new "community bank leverage ratio" was adopted, which is applicable to certain banks and bank holding companies with total assets of less than $10 billion (as described below under "Basel Capital Standards"); and
- banks with up to $3 billion in total consolidated assets may be examined by their federal banking regulator every 18 months (as opposed to every 12 months).

Basel Capital Standards

Regulatory capital rules adopted in July 2013 and fully phased in as of January 1, 2019, which we refer to as Basel III, impose minimum capital requirements for bank holding companies and banks. The Basel III rules apply to all national and state banks and savings and loan associations regardless of size and bank holding companies and savings and loan holding companies other than “small bank holding companies,” generally holding companies with consolidated assets of less than $3 billion. The Company is currently considered a “small bank holding company.” More stringent requirements are imposed on “advanced approaches” banking organizations-those organizations with $250 billion or more in total consolidated assets, $10 billion or more in total foreign exposures, or that have opted in to the Basel II capital regime.

The rules include certain higher risk-based capital and leverage requirements than those previously in place. Specifically, the following minimum capital requirements apply to the Bank:

- a new common equity Tier 1 (“CET1”) risk-based capital ratio of 4.5%;
- a Tier 1 risk-based capital ratio of 6%;
- a total risk-based capital ratio of 8%; and
- a leverage ratio of 4%.

Under Basel III, Tier 1 capital includes two components: CET1 capital and additional Tier 1 capital. The highest form of capital, CET1 capital, consists solely of common stock (plus related surplus), retained earnings, accumulated other comprehensive income, otherwise referred to as AOCI, and limited amounts of minority interests that are in the form of common stock. Additional Tier 1 capital is primarily comprised of noncumulative perpetual preferred stock, Tier 1 minority interests and grandfathered trust preferred securities (as discussed below). Tier 2 capital generally includes the allowance for loan losses up to 1.25% of risk-weighted assets, qualifying preferred stock, subordinated debt and qualifying tier 2 minority interests, less any deductions in Tier 2 instruments of an unconsolidated financial institution. Cumulative perpetual preferred stock is included only in Tier 2 capital, except that the Basel III rules permit bank holding companies with less than $15 billion in total consolidated assets to continue to include trust preferred securities and cumulative perpetual preferred stock issued before May 19, 2010 in Tier 1 Capital (but not in CET1 capital), subject to certain restrictions. AOCI is presumptively included in CET1 capital and often would operate to reduce this category of capital. When implemented, Basel III provided a one-time opportunity at the end of the first quarter of 2015 for covered banking organizations to opt out of much of this treatment of AOCI. We made this opt-out election and, as a result, retained our pre-existing treatment for AOCI.

In addition, in order to avoid restrictions on capital distributions or discretionary bonus payments to executives, under Basel III, a banking organization must maintain a “capital conservation buffer” on top of its minimum risk-based capital requirements. This buffer must consist solely of CET1 capital, but the buffer applies to all three risk-based measurements (CET1, Tier 1 capital and total capital). The 2.5% capital conservation buffer was phased in incrementally over time, and became fully effective for us on January 1, 2019, resulting in the following effective minimum capital plus capital conservation buffer ratios: (i) a CET1 capital ratio of 7.0%, (ii) a Tier 1 risk-based capital ratio of 8.5%, and (iii) a total risk-based capital ratio of 10.5%.

On December 21, 2018, the federal banking agencies issued a joint final rule to revise their regulatory capital rules to (i) address the upcoming implementation of a new credit impairment model, the Current Expected Credit Loss, or CECL model, an accounting standard under GAAP; (ii) provide an optional three-year phase-in period for the day-one adverse regulatory capital effects that banking organizations are expected to experience upon adopting CECL; and (iii) require the use of CECL in stress tests beginning with the 2020 capital planning and stress testing cycle for certain banking organizations that are subject to stress testing. We are currently evaluating the impact the CECL model will have on our accounting and expect to recognize a one-time cumulative-effect adjustment to our allowance for loan losses as of the beginning of the first quarter of 2023, the first reporting period in which the new standard is effective. At this time, we cannot yet reasonably determine the magnitude of such one-time cumulative adjustment, if any, or of the overall impact of the new standard on our business, financial condition or results of operations.

In November 2019, the federal banking regulators published final rules under the Reform Law (discussed above) implementing a simplified measure of capital adequacy for certain banking organizations that have less than $10 billion in total consolidated assets. Under the final rules, which went into effect on January 1, 2020, depository institutions and depository institution holding companies that have less than $10 billion in total consolidated assets and meet other qualifying criteria, including a leverage ratio of greater than 9%, off-balance-sheet exposures of 25% or less of total consolidated assets and trading assets plus trading liabilities of 5% or less of total consolidated assets, are deemed “qualifying community banking organizations” and are eligible to opt into the “community bank leverage ratio framework.” A qualifying community banking organization that elects to use the community bank leverage ratio framework and that maintains a leverage ratio of greater than 9% is considered to have satisfied the generally applicable risk-based and leverage capital requirements under the Basel III rules and, if applicable, is considered to have met the “well capitalized” ratio requirements for purposes of its primary federal regulator’s prompt corrective action rules, discussed below. The final rules include a two-quarter grace period during which a qualifying community banking organization that temporarily fails to meet any of the qualifying criteria, including the greater-than-9% leverage capital ratio requirement, is generally still deemed “well capitalized” so long as the banking organization maintains a leverage capital ratio greater than 8%. A banking organization that fails to maintain a leverage capital ratio greater than 8% is not permitted to use the grace period and must comply with the generally applicable requirements under the Basel III rules and file the appropriate regulatory reports. We do not have any immediate plans to elect to use the community bank leverage ratio framework but may make such an election in the future.

As of December 31, 2020, the Bank was well-capitalized, as defined by FDIC regulations. As of December 31, 2020, the Company had regulatory capital in excess of the Federal Reserve’s requirements and met the Basel III rule requirements to be well-capitalized.

The CARES Act and Initiatives Related to COVID-19

On March 27, 2020, the Coronavirus Aid, Relief, and Economic Security Act, or the CARES Act, was signed into law. The CARES Act provided for approximately $2.2 trillion in direct economic relief in response to the public health and economic impacts of COVID-19. Many of the CARES Act’s programs are, and remain, dependent upon the direct involvement of financial institutions like the Bank. These programs have been implemented through rules and guidance adopted by federal departments and agencies, including the U.S. Department of Treasury, the Federal Reserve and other federal bank regulatory authorities, including those with direct supervisory jurisdiction over the Company and the Bank. Furthermore, as the COVID-19 pandemic evolves, federal regulatory authorities continue to issue additional guidance with respect to the implementation, life cycle, and eligibility requirements for the various CARES Act programs, as well as industry-specific recovery procedures for COVID-19. In addition, it is possible that Congress will enact supplementary COVID-19 response legislation, including amendments to the CARES Act or new bills comparable in scope to the CARES Act. The Company continues to assess the impact of the CARES Act and other statutes, regulations and supervisory guidance related to the COVID-19 pandemic.

Paycheck Protection Program

A principal provision of the CARES Act amended the SBA’s loan program to create a guaranteed, unsecured loan program, the Paycheck Protection Program, or PPP, to fund operational costs of eligible businesses, organizations and self-employed persons impacted by COVID-19. These loans are eligible to be forgiven if certain conditions are satisfied and are fully guaranteed by the SBA. Additionally, loan payments will also be deferred for the first six months of the loan term. The PPP commenced on April 3, 2020 and was available to qualified borrowers through August 8, 2020. No collateral or personal guarantees were required. On December 27, 2020, the President signed into law omnibus federal spending and economic stimulus legislation titled the “Consolidated Appropriations Act, 2021” that included the Economic Aid to Hard-Hit Small Businesses, Nonprofits, and Venues Act (the “HHSB Act”). Among other things, the HHSB Act renewed the PPP, allocating $284.45 billion for both new first time PPP loans under the existing PPP and the expansion of existing PPP loans for certain qualified, existing PPP borrowers. In addition to extending and amending the PPP, the HHSB Act also creates a new grant program for “shuttered venue operators.” While we were a participating lender in the PPP in 2020, we sold our PPP loan portfolio in the second quarter of 2020.

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Troubled Debt Restructurings and Loan Modifications for Affected Borrowers

The CARES Act, as extended by certain provisions of the Consolidated Appropriations Act, 2021, permits banks to suspend requirements under GAAP for loan modifications to borrowers affected by COVID-19 that may otherwise be characterized as troubled debt restructurings and suspend any determination related thereto if (i) the borrower was not more than 30 days past due as of December 31, 2019, (ii) the modifications are related to COVID-19, and (iii) the modification occurs between March 1, 2020 and the earlier of 60 days after the date of termination of the national emergency or January 1, 2022. Federal bank regulatory authorities also issued guidance to encourage banks to make loan modifications for borrowers affected by COVID-19.

Main Street Lending Program

The CARES Act encouraged the Federal Reserve, in coordination with the Secretary of the Treasury, to establish or implement various programs to help mid-size businesses, nonprofit organizations, and municipalities. On April 9, 2020, the Federal Reserve proposed the creation of the Main Street Lending Program (the “MSLP”) to implement certain of these recommendations. The MSLP supported lending to small- and medium-sized businesses that were in sound financial condition before the onset of the COVID-19 pandemic. The MSLP, which expired on January 8, 2021, operated through three facilities: the Main Street New Loan Facility, the Main Street Priority Loan Facility, and the Main Street Expanded Loan Facility. We did not participate as a lender under the MSLP.

Proposed Legislation and Regulatory Action

From time to time, various legislative and regulatory initiatives are introduced in Congress and state legislatures, as well as by regulatory agencies. Such initiatives may include proposals to expand or contract the powers of bank holding companies and depository institutions or proposals to substantially change the financial institution regulatory system. Such legislation could change banking statutes and the operating environment of the Company in substantial and unpredictable ways. If enacted, such legislation could increase or decrease the cost of doing business, limit or expand permissible activities or affect the competitive balance among banks, savings associations, credit unions, and other financial institutions. We cannot predict whether any such legislation will be enacted, and, if enacted, the effect that it, or any implementing regulations, would have on the financial condition or results of operations of the Company. A change in statutes, regulations or regulatory policies applicable to the Company or the Bank could have a material effect on the business of the Company.

Southern First Bancshares, Inc.

We own 100% of the outstanding capital stock of the Bank, and therefore we are considered to be a bank holding company under the federal Bank Holding Company Act of 1956 (the “Bank Holding Company Act”). As a result, we are primarily subject to the supervision, examination and reporting requirements of the Federal Reserve under the Bank Holding Company Act and its regulations promulgated thereunder. Moreover, as a bank holding company of a bank located in South Carolina, we also are subject to the South Carolina Banking and Branching Efficiency Act.

Permitted Activities. Under the Bank Holding Company Act, a bank holding company is generally permitted to engage in, or acquire direct or indirect control of more than 5% of the voting shares of any company engaged in, the following activities:

- banking or managing or controlling banks;
- furnishing services to or performing services for our subsidiaries; and
- any activity that the Federal Reserve determines to be so closely related to banking as to be a proper incident to the business of banking.

Activities that the Federal Reserve has found to be so closely related to banking as to be a proper incident to the business of banking include:

- factoring accounts receivable;
- making, acquiring, brokering or servicing loans and usual related activities;
- leasing personal or real property;
- operating a non-bank depository institution, such as a savings association;
- trust company functions;
- financial and investment advisory activities;
- conducting discount securities brokerage activities;

- underwriting and dealing in government obligations and money market instruments;
- providing specified management consulting and counseling activities;
- performing selected data processing services and support services;
- acting as agent or broker in selling credit life insurance and other types of insurance in connection with credit transactions; and
- performing selected insurance underwriting activities.

As a bank holding company we also can elect to be treated as a “financial holding company,” which would allow us to engage in a broader array of activities. In summary, a financial holding company can engage in activities that are financial in nature or incidental or complimentary to financial activities, including insurance underwriting, sales and brokerage activities, providing financial and investment advisory services, underwriting services and limited merchant banking activities. We have not sought financial holding company status, but may elect such status in the future as our business matures. If we were to elect financial holding company status, each insured depository institution we control would have to be well capitalized, well managed and have at least a satisfactory rating under the Community Reinvestment Act as discussed below.

The Federal Reserve has the authority to order a bank holding company or its subsidiaries to terminate any of these activities or to terminate its ownership or control of any subsidiary when it has reasonable cause to believe that the Bank holding company’s continued ownership, activity or control constitutes a serious risk to the financial safety, soundness or stability of it or any of its bank subsidiaries.

Change in Control. Two statutes, the Bank Holding Company Act and the Change in Bank Control Act, together with regulations promulgated under them, require some form of regulatory review before any company may acquire “control” of a bank or a bank holding company. Under the Bank Holding Company Act, control is deemed to exist if a company acquires 25% or more of any class of voting securities of a bank holding company; controls the election of a majority of the members of the board of directors; or exercises a controlling influence over the management or policies of a bank or bank holding company. On January 30, 2020, the Federal Reserve issued a final rule (which became effective September 30, 2020) that clarified and codified the Federal Reserve’s standards for determining whether one company has control over another. The final rule established four categories of tiered presumptions of noncontrol that are based on the percentage of voting shares held by the investor (less than 5%, 5-9.9%, 10-14.9% and 15-24.9%) and the presence of other indicia of control. As the percentage of ownership increases, fewer indicia of control are permitted without falling outside of the presumption of noncontrol. These indicia of control include nonvoting equity ownership, director representation, management interlocks, business relationship and restrictive contractual covenants. Under the final rule, investors can hold up to 24.9% of the voting securities and up to 33% of the total equity of a company without necessarily having a controlling influence. State laws generally, including South Carolina law, require state approval before an acquirer may become the holding company of a state bank.

Under the Change in Bank Control Act, a person or company is required to file a notice with the Federal Reserve if it will, as a result of the transaction, own or control 10% or more of any class of voting securities or direct the management or policies of a bank or bank holding company and either if the bank or bank holding company has registered securities or if the acquirer would be the largest holder of that class of voting securities after the acquisition. For a change in control at the holding company level, both the Federal Reserve and the subsidiary bank's primary federal regulator must approve the change in control; at the bank level, only the bank's primary federal regulator is involved. Transactions subject to the Bank Holding Company Act are exempt from Change in Control Act requirements. For state banks, state laws, including that of South Carolina, typically require approval by the state bank regulator as well.

Source of Strength. There are a number of obligations and restrictions imposed by law and regulatory policy on bank holding companies with regard to their depository institution subsidiaries that are designed to minimize potential loss to depositors and to the FDIC insurance funds in the event that the depository institution becomes in danger of defaulting under its obligations to repay deposits. Under a policy of the Federal Reserve, a bank holding company is required to serve as a source of financial strength to its subsidiary depository institutions and to commit resources to support such institutions in circumstances where it might not do so absent such policy. Under the Federal Deposit Insurance Corporation Improvement Act of 1991, to avoid receivership of its insured depository institution subsidiary, a bank holding company is required to guarantee the compliance of any insured depository institution subsidiary that may become “undercapitalized” within the terms of any capital restoration plan filed by such subsidiary with its appropriate federal banking agency up to the lesser of (i) an amount equal to 5% of the institution’s total assets at the time the institution became undercapitalized, or (ii) the amount which is necessary (or would have been necessary) to bring the institution into compliance with all applicable capital standards as of the time the institution fails to comply with such capital restoration plan.

The Federal Reserve also has the authority under the Bank Holding Company Act to require a bank holding company to terminate any activity or relinquish control of a nonbank subsidiary (other than a nonbank subsidiary of a bank) upon the Federal Reserve's determination that such activity or control constitutes a serious risk to the financial soundness or stability of any subsidiary depository institution of the bank holding company. Further, federal law grants federal bank regulatory authorities' additional discretion to require a bank holding company to divest itself of any bank or nonbank subsidiary if the agency determines that divestiture may aid the depository institution's financial condition.

In addition, the "cross guarantee" provisions of the Federal Deposit Insurance Act (the "FDIA") require insured depository institutions under common control to reimburse the FDIC for any loss suffered or reasonably anticipated by the FDIC as a result of the default of a commonly controlled insured depository institution or for any assistance provided by the FDIC to a commonly controlled insured depository institution in danger of default. The FDIC's claim for damages is superior to claims of shareholders of the insured depository institution or its holding company, but is subordinate to claims of depositors, secured creditors and holders of subordinated debt (other than affiliates) of the commonly controlled insured depository institutions.

The FDIA also provides that amounts received from the liquidation or other resolution of any insured depository institution by any receiver must be distributed (after payment of secured claims) to pay the deposit liabilities of the institution prior to payment of any other general or unsecured senior liability, subordinated liability, general creditor or shareholder. This provision would give depositors a preference over general and subordinated creditors and shareholders in the event a receiver is appointed to distribute the assets of our Bank.

Any capital loans by a bank holding company to any of its subsidiary banks are subordinate in right of payment to deposits and to certain other indebtedness of such subsidiary bank. In the event of a bank holding company's bankruptcy, any commitment by the bank holding company to a federal bank regulatory agency to maintain the capital of a subsidiary bank will be assumed by the bankruptcy trustee and entitled to a priority of payment.

Capital Requirements. The Federal Reserve imposes certain capital requirements on the bank holding company under the Bank Holding Company Act, including a minimum leverage ratio and a minimum ratio of "qualifying" capital to risk-weighted assets. These requirements are essentially the same as those that apply to the Bank and are described above under "Basel III Capital Standards." However, because the Company currently qualifies as a small bank holding company, these capital requirements do not currently apply to the Company. Subject to certain restrictions, we are able to borrow money to make a capital contribution to the Bank, and these loans may be repaid from dividends paid from the Bank to the Company. Our ability to pay dividends depends on, among other things, the Bank's ability to pay dividends to us, which is subject to regulatory restrictions as described below in "Southern First Bank—Dividends."

We are also able to raise capital for contribution to the Bank by issuing securities without having to receive regulatory approval, subject to compliance with federal and state securities laws.

Dividends. Since the Company is a bank holding company, its ability to declare and pay dividends is dependent on certain federal and state regulatory considerations, including the guidelines of the Federal Reserve. The Federal Reserve has issued a policy statement regarding the payment of dividends by bank holding companies. In general, the Federal Reserve's policies provide that dividends should be paid only out of current earnings and only if the prospective rate of earnings retention by the bank holding company appears consistent with the organization's capital needs, asset quality and overall financial condition. The Federal Reserve's policies also require that a bank holding company serve as a source of financial strength to its subsidiary banks by standing ready to use available resources to provide adequate capital funds to those banks during periods of financial stress or adversity and by maintaining the financial flexibility and capital-raising capacity to obtain additional resources for assisting its subsidiary banks where necessary. Further, under the prompt corrective action regulations, the ability of a bank holding company to pay dividends may be restricted if a subsidiary bank becomes undercapitalized. These regulatory policies could affect the ability of the Company to pay dividends or otherwise engage in capital distributions.

In addition, since the Company is a legal entity separate and distinct from the Bank and does not conduct stand-alone operations, its ability to pay dividends depends on the ability of the Bank to pay dividends to it, which is also subject to regulatory restrictions as described below in "Southern First Bank – Dividends."

South Carolina State Regulation. As a South Carolina bank holding company under the South Carolina Banking and Branching Efficiency Act, we are subject to limitations on sale or merger and to regulation by the South Carolina Board of Financial Institutions (the “S.C. Board”). We are not required to obtain the approval of the S.C. Board prior to acquiring the capital stock of a national bank, but we must notify them at least 15 days prior to doing so. We must receive the S.C. Board’s approval prior to engaging in the acquisition of a South Carolina state chartered bank or another South Carolina bank holding company.

Southern First Bank

As a South Carolina bank, deposits in the Bank are insured by the FDIC up to a maximum amount, which is currently $250,000 per depositor. The S.C. Board and the FDIC regulate or monitor virtually all areas of the Bank’s operations, including;

- security devices and procedures;
- adequacy of capitalization and loss reserves;
- loans;
- investments;
- borrowings;
- deposits;
- mergers;
- issuances of securities;
- payment of dividends;
- interest rates payable on deposits;
- interest rates or fees chargeable on loans;
- establishment of branches;
- corporate reorganizations;
- maintenance of books and records; and
- adequacy of staff training to carry on safe lending and deposit gathering practices.

These agencies, and the federal and state laws applicable to the Bank’s operations, extensively regulate various aspects of our banking business, including, among other things, permissible types and amounts of loans, investments and other activities, capital adequacy, branching, interest rates on loans and on deposits, the maintenance of reserves on demand deposit liabilities, and the safety and soundness of our banking practices.

All insured institutions must undergo regular on-site examinations by their appropriate banking agency. The cost of examinations of insured depository institutions and any affiliates may be assessed by the appropriate federal banking agency against each institution or affiliate as it deems necessary or appropriate. Insured institutions are required to submit annual reports to the FDIC, their federal regulatory agency, and state supervisor when applicable. The FDIC has developed a method for insured depository institutions to provide supplemental disclosure of the estimated fair market value of assets and liabilities, to the extent feasible and practicable, in any balance sheet, financial statement, report of condition or any other report of any insured depository institution. The FDIC and the other federal banking regulatory agencies also have issued standards for all insured depository institutions relating, among other things, to the following:

- internal controls;
- information systems and audit systems;
- loan documentation;
- credit underwriting;
- interest rate risk exposure; and
- asset quality.

Prompt Corrective Action. As an insured depository institution, the Bank is required to comply with the capital requirements promulgated under the FDIA and the prompt corrective action regulations thereunder, which set forth five capital categories, each with specific regulatory consequences. Under these regulations, the categories are:

- Well Capitalized — The institution exceeds the required minimum level for each relevant capital measure. A well-capitalized institution (i) has a total risk-based capital ratio of 10% or greater, (ii) has a Tier 1 risk-based capital ratio of 8% or greater, (iii) has a common equity Tier 1 risk-based capital ratio of 6.5% or greater, (iv) has a leverage capital ratio of 5% or greater, and (v) is not subject to any order or written directive to meet and maintain a specific capital level for any capital measure.

- Adequately Capitalized — The institution meets the required minimum level for each relevant capital measure. No capital distribution may be made that would result in the institution becoming undercapitalized. An adequately capitalized institution (i) has a total risk-based capital ratio of 8% or greater, (ii) has a Tier 1 risk-based capital ratio of 6% or greater, (iii) has a common equity Tier 1 risk-based capital ratio of 4.5% or greater, and (iv) has a leverage capital ratio of 4% or greater.
- Undercapitalized — The institution fails to meet the required minimum level for any relevant capital measure. An undercapitalized institution (i) has a total risk-based capital ratio of less than 8%, (ii) has a Tier 1 risk-based capital ratio of less than 6%, (iii) has a common equity Tier 1 risk-based capital ratio of less than 4.5% or greater, or (iv) has a leverage capital ratio of less than 4%.
- Significantly Undercapitalized — The institution is significantly below the required minimum level for any relevant capital measure. A significantly undercapitalized institution (i) has a total risk-based capital ratio of less than 6%, (ii) has a Tier 1 risk-based capital ratio of less than 4%, (iii) has a common equity Tier 1 risk-based capital ratio of less than 3% or greater, or (iv) has a leverage capital ratio of less than 3%.
- Critically Undercapitalized — The institution fails to meet a critical capital level set by the appropriate federal banking agency. A critically undercapitalized institution has a ratio of tangible equity to total assets that is equal to or less than 2%.

Effective with the March 31, 2020 Call Report, qualifying community banking organizations that elect to use the new community bank leverage ratio framework and that maintain a leverage ratio of greater than 9.0% will be considered to have satisfied the risk-based and leverage capital requirements to be deemed well-capitalized. We do not have any immediate plans to elect to use the community bank leverage ratio framework but may make such an election in the future.

If the FDIC determines, after notice and an opportunity for hearing, that the Bank is in an unsafe or unsound condition, the regulator is authorized to reclassify the Bank to the next lower capital category (other than critically undercapitalized) and require the submission of a plan to correct the unsafe or unsound condition.

If a bank is not well capitalized, it cannot accept brokered deposits without prior regulatory approval. Even if approved, rate restrictions will govern the rate a bank may pay on brokered deposits. In addition, a bank that is not well capitalized cannot offer an effective yield in excess of 75 basis points over interest paid on deposits of comparable size and maturity in such institution’s normal market area for deposits accepted from within its normal market area, or national rate paid on deposits of comparable size and maturity for deposits accepted outside the bank’s normal market area. Moreover, the FDIC generally prohibits a depository institution from making any capital distributions (including payment of a dividend) or paying any management fee to its parent holding company if the depository institution would thereafter be categorized as undercapitalized. Undercapitalized institutions are subject to growth limitations (an undercapitalized institution may not acquire another institution, establish additional branch offices or engage in any new line of business unless determined by the appropriate federal banking agency to be consistent with an accepted capital restoration plan, or unless the FDIC determines that the proposed action will further the purpose of prompt corrective action) and are required to submit a capital restoration plan. The agencies may not accept a capital restoration plan without determining, among other things, that the plan is based on realistic assumptions and is likely to succeed in restoring the depository institution’s capital. In addition, for a capital restoration plan to be acceptable, the depository institution’s parent holding company must guarantee that the institution will comply with the capital restoration plan. The aggregate liability of the parent holding company is limited to the lesser of an amount equal to 5.0% of the depository institution’s total assets at the time it became categorized as undercapitalized or the amount that is necessary (or would have been necessary) to bring the institution into compliance with all capital standards applicable with respect to such institution as of the time it fails to comply with the plan. If a depository institution fails to submit an acceptable plan, it is categorized as significantly undercapitalized.

Significantly undercapitalized categorized depository institutions may be subject to a number of requirements and restrictions, including orders to sell sufficient voting stock to become categorized as adequately capitalized, requirements to reduce total assets, and cessation of receipt of deposits from correspondent banks. The appropriate federal banking agency may take any action authorized for a significantly undercapitalized institution if an undercapitalized institution fails to submit an acceptable capital restoration plan or fails in any material respect to implement a plan accepted by the agency. A critically undercapitalized institution is subject to having a receiver or conservator appointed to manage its affairs and for loss of its charter to conduct banking activities.

An insured depository institution may not pay a management fee to a bank holding company controlling that institution or any other person having control of the institution if, after making the payment, the institution would be undercapitalized. In addition, an institution cannot make a capital distribution, such as a dividend or other distribution, that is in substance a distribution of capital to the owners of the institution if following such a distribution the institution would be undercapitalized. Thus, if payment of such a management fee or the making of such would cause a bank to become undercapitalized, it could not pay a management fee or dividend to the bank holding company.

As of December 31, 2020, the Bank was deemed to be “well capitalized.”

Standards for Safety and Soundness. The FDIA also requires the federal banking regulatory agencies to prescribe, by regulation or guideline, operational and managerial standards for all insured depository institutions relating to: (i) internal controls, information systems and internal audit systems; (ii) loan documentation; (iii) credit underwriting; (iv) interest rate risk exposure; and (v) asset growth. The agencies also must prescribe standards for asset quality, earnings, and stock valuation, as well as standards for compensation, fees and benefits. The federal banking agencies have adopted regulations and Interagency Guidelines Prescribing Standards for Safety and Soundness to implement these required standards. These guidelines set forth the safety and soundness standards that the federal banking agencies use to identify and address problems at insured depository institutions before capital becomes impaired. Under the regulations, if the FDIC determines that the Bank fails to meet any standards prescribed by the guidelines, the agency may require the Bank to submit to the agency an acceptable plan to achieve compliance with the standard, as required by the FDIC. The final regulations establish deadlines for the submission and review of such safety and soundness compliance plans.

Insurance of Accounts and Regulation by the FDIC. The Bank’s deposits are insured up to applicable limits by the Deposit Insurance Fund of the FDIC. The Dodd-Frank Act permanently increased the maximum amount of deposit insurance for banks to $250,000 per account. As insurer, the FDIC imposes deposit insurance premiums and is authorized to conduct examinations of and to require reporting by FDIC insured institutions. It also may prohibit any FDIC insured institution from engaging in any activity the FDIC determines by regulation or order to pose a serious risk to the insurance fund.

As an FDIC-insured bank, the Bank must pay deposit insurance assessments to the FDIC based on its average total assets minus its average tangible equity. The Bank’s assessment rates are currently based on its risk classification (i.e., the level of risk it poses to the FDIC’s deposit insurance fund). Institutions classified as higher risk pay assessments at higher rates than institutions that pose a lower risk. In addition to ordinary assessments described above, the FDIC has the ability to impose special assessments in certain instances.

In addition to the ordinary assessments described above, the FDIC has the ability to impose special assessments in certain instances. For example, under the Dodd-Frank Act, the minimum designated reserve ratio for the deposit insurance fund was increased to 1.35% of the estimated total amount of insured deposits. On September 30, 2018, the deposit insurance fund reached 1.36%, exceeding the statutorily required minimum reserve ratio of 1.35%. On reaching the minimum reserve ratio of 1.35%, FDIC regulations provided for two changes to deposit insurance assessments: (i) surcharges on insured depository institutions with total consolidated assets of $10 billion or more (large institutions) ceased; and (ii) small banks will receive assessment credits for the portion of their assessments that contributed to the growth in the reserve ratio from between 1.15% and 1.35%, to be applied when the reserve ratio is at or above 1.38%. These assessment credits started with the June 30, 2019 assessment invoiced in September 2019 and finished with the September 30, 2019 assessment which was invoiced in December 2019. Assessment rates are expected to decrease if the reserve ratio increases such that it exceeds 2%.

The FDIC may terminate the deposit insurance of any insured depository institution, including the Bank, if it determines after a hearing that the institution has engaged in unsafe or unsound practices, is in an unsafe or unsound condition to continue operations or has violated any applicable law, regulation, rule, order or condition imposed by the FDIC. It also may suspend deposit insurance temporarily during the hearing process for the permanent termination of insurance if the institution has no tangible capital. If insurance of accounts is terminated, the accounts at the institution at the time of the termination, less subsequent withdrawals, shall continue to be insured for a period of six months to two years, as determined by the FDIC. Management is not aware of any practice, condition or violation that might lead to termination of the Bank’s deposit insurance.

Transactions with Affiliates and Insiders. The Company is a legal entity separate and distinct from the Bank and its other subsidiaries. Various legal limitations restrict the Bank from lending or otherwise supplying funds to the Company or its non-bank subsidiaries. The Company and the Bank are subject to Sections 23A and 23B of the Federal Reserve Act and Federal Reserve Regulation W.

Section 23A of the Federal Reserve Act places limits on the amount of loans or extensions of credit by a bank to any affiliate, including its holding company, and on a bank’s investments in, or certain other transactions with, affiliates and on the amount of advances to third parties collateralized by the securities or obligations of any affiliates of the bank. Section 23A also applies to derivative transactions, repurchase agreements and securities lending and borrowing transactions that cause a bank to have credit exposure to an affiliate. The aggregate of all covered transactions is limited in amount, as to any one affiliate, to 10% of the Bank’s capital and surplus and, as to all affiliates combined, to 20% of the Bank’s capital and surplus. Furthermore, within the foregoing limitations as to amount, each covered transaction must meet specified collateral requirements. The Bank is forbidden to purchase low quality assets from an affiliate.

Section 23B of the Federal Reserve Act, among other things, prohibits an institution from engaging in certain transactions with certain affiliates unless the transactions are on terms substantially the same, or at least as favorable to such institution or its subsidiaries, as those prevailing at the time for comparable transactions with nonaffiliated companies. If there are no comparable transactions, a bank's (or one of its subsidiaries') affiliate transaction must be on terms and under circumstances, including credit standards, that in good faith would be offered to, or would apply to, nonaffiliated companies. These requirements apply to all transactions subject to Section 23A as well as to certain other transactions.

The affiliates of a bank include any holding company of the bank, any other company under common control with the bank (including any company controlled by the same shareholders who control the bank), any subsidiary of the bank that is itself a bank, any company in which the majority of the directors or trustees also constitute a majority of the directors or trustees of the bank or holding company of the bank, any company sponsored and advised on a contractual basis by the bank or an affiliate, and any mutual fund advised by a bank or any of the bank's affiliates. Regulation W generally excludes all non-bank and non-savings association subsidiaries of banks from treatment as affiliates, except to the extent that the Federal Reserve decides to treat these subsidiaries as affiliates.

The Bank is also subject to certain restrictions on extensions of credit to executive officers, directors, certain principal shareholders, and their related interests. Extensions of credit include derivative transactions, repurchase and reverse repurchase agreements, and securities borrowing and lending transactions to the extent that such transactions cause a bank to have credit exposure to an insider. Any extension of credit to an insider (i) must be made on substantially the same terms, including interest rates and collateral requirements, as those prevailing at the time for comparable transactions with unrelated third parties and (ii) must not involve more than the normal risk of repayment or present other unfavorable features.

On December 22, 2020, the federal banking agencies issued an interagency statement extending the temporary relief from enforcement action against banks or asset managers, which become principal shareholders of banks, with respect to certain extensions of credit by banks that otherwise would violate Regulation O, provided the asset managers and banks satisfy certain conditions designed to ensure that there is a lack of control by the asset manager over the bank. This temporary relief will apply until January 1, 2022, unless amended or extended, while the Federal Reserve, in consultation with the other federal banking agencies, considers whether to amend Regulation O.

Dividends. The Company's principal source of cash flow, including cash flow to pay dividends to its shareholders, is dividends it receives from the Bank. Statutory and regulatory limitations apply to the Bank's payment of dividends to the Company. As a South Carolina chartered bank, the Bank is subject to limitations on the amount of dividends that it is permitted to pay. Unless otherwise instructed by the S.C. Board, the Bank is generally permitted under South Carolina state banking regulations to pay cash dividends of up to 100% of net income in any calendar year without obtaining the prior approval of the S.C. Board. The FDIC also has the authority under federal law to enjoin a bank from engaging in what in its opinion constitutes an unsafe or unsound practice in conducting its business, including the payment of a dividend under certain circumstances. The Bank must also maintain the CET1 capital conservation buffer of 2.5% to avoid becoming subject to restrictions on capital distributions, including dividends, as described above.

Branching. Under current South Carolina law, the Bank may open branch offices throughout South Carolina with the prior approval of the S.C. Board. In addition, with prior regulatory approval, the Bank is able to acquire existing banking operations in South Carolina. Furthermore, federal legislation permits interstate branching, including out-of-state acquisitions by bank holding companies, interstate branching by banks, and interstate merging by banks. The Dodd-Frank Act removes previous state law restrictions on de novo interstate branching in states such as South Carolina. This change permits out-of-state banks to open de novo branches in states where the laws of the state where the de novo branch to be opened would permit a bank chartered by that state to open a de novo branch.

Community Reinvestment Act. The Community Reinvestment Act ("CRA") requires that the FDIC evaluate the record of the Bank in meeting the credit needs of its local community, including low and moderate income neighborhoods. These factors are also considered in evaluating mergers, acquisitions, and applications to open a branch or facility. Failure to adequately meet these criteria could impose additional requirements and limitations on our Bank. On February 12, 2018, the date of the most recent examination report, the Bank received a satisfactory CRA rating.

The Gramm Leach Bliley Act (the "GLBA") made various changes to the CRA. Among other changes, CRA agreements with private parties must be disclosed and annual CRA reports must be made available to a bank's primary federal regulator. A bank holding company will not be permitted to become a financial holding company and no new activities authorized under the GLBA may be commenced by a holding company or by a bank financial subsidiary if any of its bank subsidiaries received less than a satisfactory CRA rating in its latest CRA examination.

In December 2019, the FDIC and the Office of the Comptroller of the Currency ("OCC") proposed changes to the regulations implementing the CRA, which, if adopted will result in changes to the current CRA framework. On May 20, 2020 the OCC issued a final rule to strengthen and modernize its existing CRA framework. The Federal Reserve did not join the proposal, but instead issued its own proposed rules in September 2020. Neither the FDIC nor the Federal Reserve have finalized their CRA proposals at this time.

Consumer Protection Regulations. Activities of the Bank are subject to a variety of statutes and regulations designed to protect consumers. Interest and other charges collected or contracted for by the Bank are subject to state usury laws and federal laws concerning interest rates. The Bank's loan operations are also subject to federal laws applicable to credit transactions, such as:

- The Dodd-Frank Act that created the CFPB within the Federal Reserve Board, which has broad rulemaking authority over a wide range of consumer laws that apply to all insured depository institutions;
- the Truth-In-Lending Act, governing disclosures of credit terms to consumer borrowers;
- the Home Mortgage Disclosure Act of 1975, requiring financial institutions to provide information to enable the public and public officials to determine whether a financial institution is fulfilling its obligation to help meet the housing needs of the community it serves;
- the Equal Credit Opportunity Act, prohibiting discrimination on the basis of race, creed or other prohibited factors in extending credit;
- the Fair Credit Reporting Act of 1978, as amended by the Fair and Accurate Credit Transactions Act, governing the use and provision of information to credit reporting agencies, certain identity theft protections, and certain credit and other disclosures;
- the Fair Debt Collection Act, governing the manner in which consumer debts may be collected by collection agencies; and
- the rules and regulations of the various federal agencies charged with the responsibility of implementing such federal laws.

The deposit operations of the Bank also are subject to:

- the Federal Deposit Insurance Act, which, among other things, limits the amount of deposit insurance available per account to $250,000 and imposes other limits on deposit-taking;
- the Right to Financial Privacy Act, which imposes a duty to maintain confidentiality of consumer financial records and prescribes procedures for complying with administrative subpoenas of financial records;
- the Electronic Funds Transfer Act and Regulation E, which governs automatic deposits to and withdrawals from deposit accounts and customers' rights and liabilities arising from the use of automated teller machines and other electronic banking services;
- The Check Clearing for the 21st Century Act (also known as "Check 21"), which gives "substitute check," such as digital images and copies made from that image, the same legal standing as the original paper check; and
- the Truth in Savings Act and Regulation DD, which requires depository institutions to provide disclosures so that consumers can make meaningful comparisons about depository institutions and accounts.

Anti-Money Laundering. Financial institutions must maintain anti-money laundering programs that include established internal policies, procedures, and controls; a designated compliance officer; an ongoing employee training program; and testing of the program by an independent audit function. The Company and the Bank are also prohibited from entering into specified financial transactions and account relationships and must meet enhanced standards for due diligence and "knowing your customer" in their dealings with foreign financial institutions and foreign customers. Financial institutions must take reasonable steps to conduct enhanced scrutiny of account relationships to guard against money laundering and to report any suspicious transactions, and recent laws provide law enforcement authorities with increased access to financial information maintained by banks. Anti-money laundering obligations have been substantially strengthened as a result of the Uniting and Strengthening America by Providing Appropriate Tools Required to Intercept and Obstruct Terrorism Act of 2001 (which we refer to as the "USA PATRIOT Act"). Bank regulators routinely examine institutions for compliance with these obligations and are required to consider compliance in connection with the regulatory review of applications. The regulatory authorities have been active in imposing "cease and desist" orders and money penalty sanctions against institutions that have not complied with these requirements.

USA PATRIOT Act. The USA PATRIOT Act became effective on October 26, 2001, amended, in part, the Bank Secrecy Act and provides, in part, for the facilitation of information sharing among governmental entities and financial institutions for the purpose of combating terrorism and money laundering by enhancing anti-money laundering and financial transparency laws, as well as enhanced information collection tools and enforcement mechanics for the U.S. government, including: (i) requiring standards for verifying customer identification at account opening; (ii) rules to promote cooperation among financial institutions, regulators, and law enforcement entities in identifying parties that may be involved in terrorism or money laundering; (iii) reports by nonfinancial trades and businesses filed with the Treasury Department's Financial Crimes Enforcement Network for transactions exceeding $10,000; and (iv) filing suspicious activities reports by brokers and dealers if they believe a customer may be violating U.S. laws and regulations. The Act also requires enhanced due diligence requirements for financial institutions that administer, maintain, or manage private bank accounts or correspondent accounts for non-U.S. persons. Bank regulators routinely examine institutions for compliance with these obligations and are required to consider compliance in connection with the regulatory review of applications.

Under the USA PATRIOT Act, the Financial Crimes Enforcement Network ("FinCEN") can send our banking regulatory agencies lists of the names of persons suspected of involvement in terrorist activities. The Bank can be requested, to search its records for any relationships or transactions with persons on those lists. If the Bank finds any relationships or transactions, it must file a suspicious activity report and contact FinCEN.

The Office of Foreign Assets Control.The Office of Foreign Assets Control ("OFAC"), which is a division of the U.S. Treasury, is responsible for helping to insure that U.S. entities do not engage in transactions with "enemies" of the U.S., as defined by various Executive Orders and Acts of Congress. OFAC has sent, and will send, our banking regulatory agencies lists of names of persons and organizations suspected of aiding, harboring or engaging in terrorist acts. If the Bank finds a name on any transaction, account or wire transfer that is on an OFAC list, it must freeze such account, file a suspicious activity report and notify the FBI. The Bank has appointed an OFAC compliance officer to oversee the inspection of its accounts and the filing of any notifications. The Bank actively checks high-risk OFAC areas such as new accounts, wire transfers and customer files. The Bank performs these checks utilizing software, which is updated each time a modification is made to the lists provided by OFAC and other agencies of Specially Designated Nationals and Blocked Persons.

Privacy, Data Security and Credit Reporting. Financial institutions are required to disclose their policies for collecting and protecting confidential information. Customers generally may prevent financial institutions from sharing nonpublic personal financial information with nonaffiliated third parties except under narrow circumstances, such as the processing of transactions requested by the consumer or if the Bank is jointly sponsoring a product or service with a nonaffiliated third party. Additionally, financial institutions generally may not disclose consumer account numbers to any nonaffiliated third party for use in telemarketing, direct mail marketing or other marketing to consumers. It is the Bank's policy not to disclose any personal information unless required by law.

Recent cyberattacks against banks and other institutions that resulted in unauthorized access to confidential customer information have prompted the Federal banking agencies to issue several warnings and extensive guidance on cyber security. The agencies are likely to devote more resources to this part of their safety and soundness examination than they have in the past.

In addition, pursuant to the Fair and Accurate Credit Transactions Act of 2003 (the "FACT Act") and the implementing regulations of the federal banking agencies and Federal Trade Commission, the Bank is required to have in place an "identity theft red flags" program to detect, prevent and mitigate identity theft. The Bank has implemented an identity theft red flags program designed to meet the requirements of the FACT Act and the joint final rules. Additionally, the FACT Act amends the Fair Credit Reporting Act to generally prohibit a person from using information received from an affiliate to make a solicitation for marketing purposes to a consumer, unless the consumer is given notice and a reasonable opportunity and a reasonable and simple method to opt out of the making of such solicitations.

Federal Home Loan Bank System. The Bank is a member of the Federal Home Loan Bank ("FHLB") of Atlanta, which is one of 12 regional FHLBs that administer home financing credit for depository institutions. Each FHLB serves as a reserve or central bank for its members within its assigned region. It is funded primarily from proceeds derived from the sale of consolidated obligations of the FHLB System. It makes loans or advances to members in accordance with policies and procedures established by the Board of Directors of the FHLB, which are subject to the oversight of the Federal Housing Financing Board. All advances from the FHLB, which are subject to the oversight of the Federal Housing Finance Board. All advances from the FHLB are required to be fully secured by sufficient collateral as determined by the FHLB.

Effect of Governmental Monetary Policies. Our earnings are affected by domestic economic conditions and the monetary and fiscal policies of the U.S. government and its agencies. The Federal Reserve's monetary policies have had, and are likely to continue to have, an important impact on the operating results of commercial banks through its power to implement national monetary policy in order, among other things, to curb inflation or combat a recession. The monetary policies of the Federal Reserve have major effects upon the levels of bank loans, investments and deposits through its open market operations in U.S. government securities and through its regulation of the discount rate on borrowings of member banks and the reserve requirements against member bank deposits. It is not possible to predict the nature or impact of future changes in monetary and fiscal policies. In response to the COVID-19 pandemic, on March 3, 2020, the Federal Open Market Committee ("FOMC") reduced the targeted federal funds interest rate range by 50 basis points to 1.00% to 1.25%. On March 15, 2020, the FOMC again lowered the federal funds rate to a target range of 0.0% to 0.25%.

Incentive Compensation. The Dodd-Frank Act requires the federal bank regulators and the SEC to establish joint regulations or guidelines prohibiting incentive-based payment arrangements at specified regulated entities having at least $1 billion in total assets that encourage inappropriate risks by providing an executive officer, employee, director or principal shareholder with excessive compensation, fees, or benefits or that could lead to material financial loss to the entity. In addition, these regulators must establish regulations or guidelines requiring enhanced disclosure to regulators of incentive-based compensation arrangements. The agencies proposed such regulations in April 2011. However, the 2011 proposal was replaced with a new proposal in May 2016, which makes explicit that the involvement of risk management and control personnel includes not only compliance, risk management and internal audit, but also legal, human resources, accounting, financial reporting and finance roles responsible for identifying, measuring, monitoring or controlling risk-taking. A final rule had not been adopted as of December 31, 2020.

In June 2010, the Federal Reserve, the FDIC and the OCC issued a comprehensive final guidance on incentive compensation policies intended to ensure that the incentive compensation policies of banking organizations do not undermine the safety and soundness of such organizations by encouraging excessive risk-taking. The guidance, which covers all employees that have the ability to materially affect the risk profile of an organization, either individually or as part of a group, is based upon the key principles that a banking organization's incentive compensation arrangements should (i) provide incentives that do not encourage risk-taking beyond the organization's ability to effectively identify and manage risks, (ii) be compatible with effective internal controls and risk management, and (iii) be supported by strong corporate governance, including active and effective oversight by the organization's board of directors.

The Federal Reserve will review, as part of the regular, risk-focused examination process, the incentive compensation arrangements of banking organizations, such as the Company, that are not "large, complex banking organizations." These reviews will be tailored to each organization based on the scope and complexity of the organization's activities and the prevalence of incentive compensation arrangements. The findings of the supervisory initiatives will be included in reports of examination. Deficiencies will be incorporated into the organization's supervisory ratings, which can affect the organization's ability to make acquisitions and take other actions. Enforcement actions may be taken against a banking organization if its incentive compensation arrangements, or related risk-management control or governance processes, pose a risk to the organization's safety and soundness and the organization is not taking prompt and effective measures to correct the deficiencies.

In addition, the Tax Cuts and Jobs Act (the "Tax Act"), which was signed into law in December 2017, contains certain provisions affecting performance-based compensation. Specifically, the pre-existing exception to the $1 million deduction limitation applicable to performance-based compensation was repealed. The deduction limitation is now applied to all compensation exceeding $1.0 million, for our covered employees, regardless of how it is classified, which could have an adverse effect on our income tax expense and net income.

Concentrations in Commercial Real Estate. Concentration risk exists when FDIC-insured institutions deploy too many assets to any one industry or segment. A concentration in commercial real estate is one example of regulatory concern. The interagency Concentrations in Commercial Real Estate Lending, Sound Risk Management Practices guidance ("CRE Guidance") provides supervisory criteria, including the following numerical indicators, to assist bank examiners in identifying banks with potentially significant commercial real estate loan concentrations that may warrant greater supervisory scrutiny: (i) commercial real estate loans exceeding 300% of capital and increasing 50% or more in the preceding three years or (ii) construction and land development loans exceeding 100% of capital. The CRE Guidance does not limit banks' levels of commercial real estate lending activities, but rather guides institutions in developing risk management practices and levels of capital that are commensurate with the level and nature of their commercial real estate concentrations. On December 18, 2015, the federal banking agencies issued a statement to reinforce prudent risk-management practices related to commercial real estate lending, having observed substantial growth in many commercial real estate asset and lending markets, increased competitive pressures, rising commercial real estate concentrations in banks, and an easing of commercial real estate underwriting standards. The federal bank agencies reminded FDIC-insured institutions to maintain underwriting discipline and exercise prudent risk-management practices to identify, measure, monitor and manage the risks arising from commercial real estate lending. In addition, FDIC-insured institutions must maintain capital commensurate with the level and nature of their commercial real estate concentration risk.

Based on the Bank's loan portfolio as of December 31, 2020, it did not exceed the 300% and 100% guidelines for commercial real estate loans. The Bank will continue to monitor its portfolio to manage this increased risk.

Item 1A. Risk Factors.

The following risk factors and other information included in this Annual Report on Form 10-K should be carefully considered. The risks and uncertainties described below are not the only ones we face. Additional risks and uncertainties not presently known to us or that we currently deem immaterial also may adversely impact our business operations. If any of the following risks occur, our business, financial condition, operating results, and cash flows could be materially adversely affected.

Risks Related to Economic Conditions, Including as a Result of the COVID-19 Pandemic

The global COVID-19 pandemic has adversely affected our business, financial condition and results of operations, and the ultimate effect of the pandemic on our business, financial condition and results of operations will depend on future developments and other factors that are highly uncertain.

The global COVID-19 pandemic and related government-imposed and other measures intended to control the spread of the disease, including restrictions on travel and the conduct of business, such as stay-at-home orders, quarantines, travel bans, border closings, business and school closures and other similar measures, have had a significant impact on global economic conditions and have negatively impacted certain aspects of our business, financial condition and results of operations, and may continue to do so in the future. The governmental and social response to the COVID-19 pandemic has resulted in an unprecedented slow-down in economic activity and a related increase in unemployment. The COVID-19 pandemic, and related efforts to contain it, have also caused significant disruptions in the functioning of the financial markets and have increased economic and market uncertainty and volatility.

Given the ongoing, dynamic and unprecedented nature of the COVID-19 pandemic, it is difficult to predict the full impact the pandemic will have on our business. While certain factors point to improving economic conditions, uncertainty remains regarding the path of the economic recovery, the mitigating impacts of government interventions, the success of vaccine distribution and the efficacy of administered vaccines, as well as the effects of the change in leadership resulting from the recent elections. The COVID-19 pandemic may subject us to any of the following risks, any of which could have a material adverse effect on our business, financial condition, liquidity, results of operations, risk-weighted assets and regulatory capital:

- because the incidence of reported COVID-19 cases and related hospitalizations and deaths varies significantly by state and locality, the economic downturn caused by the pandemic may be deeper and more sustained in certain areas, including those in which we do business, relative to other areas of the country;

- our ability to market our products and services may be impaired by a variety of external factors, including a prolonged reduction in economic activity and continued economic and financial market volatility, which could cause demand for our products and services to decline, in turn making it difficult for us to grow assets and income;

- if the economy is unable to substantially reopen and high levels of unemployment continue for an extended period of time, loan delinquencies, problem assets, and foreclosures may increase, resulting in increased charges and reduced income;

- collateral for loans, especially real estate, may decline in value, which may reduce our ability to liquidate such collateral and could cause loan losses to increase and impair our ability over the long run to maintain our targeted loan origination volume;

- our allowance credit losses may have to be increased if borrowers experience financial difficulties beyond forbearance periods, which will adversely affect our net income;

- an increase in non-performing loans due to the COVID-19 pandemic would result in a corresponding increase in the risk-weighting of assets and therefore an increase in required regulatory capital;
- the net worth and liquidity of borrowers and loan guarantors may decline, impairing their ability to honor commitments to us;
- as the result of the reduction of the Federal Reserve's target federal funds rate to near 0%, the yield on our assets may decline to a greater extent than the decline in our cost of interest-bearing liabilities, reducing our net interest margin and spread and reducing net income;
- deposits could decline if customers need to draw on available balances as a result of the economic downturn;
- a material decrease in net income or a net loss over several quarters could result in a decrease in the rate of our quarterly cash dividend;
- the borrowing needs of our clients may increase, especially during this challenging economic environment, which could result in increased borrowing against our contractual obligations to extend credit;
- we face heightened cybersecurity risk in connection with our operation of a remote working environment, which risks include, among others, greater phishing, malware, and other cybersecurity attacks, vulnerability to disruptions of our information technology infrastructure and telecommunications systems, increased risk of unauthorized dissemination of confidential information, limited ability to restore our systems in the event of a systems failure or interruption, greater risk of a security breach resulting in destruction or misuse of valuable information, and potential impairment of our ability to perform critical functions—all of which could expose us to risks of data or financial loss, litigation and liability and could seriously disrupt our operations and the operations of any impacted customers;
- we rely on third party vendors for certain services and the unavailability of a critical service or limitations on the business capacities of our vendors for extended periods of time due to the COVID-19 pandemic could have an adverse effect on our operations; and
- as a result of the COVID-19 pandemic, there may be unexpected developments in financial markets, legislation, regulations and consumer and customer behavior.

Even after the COVID-19 outbreak has subsided, we may continue to experience materially adverse impacts to our business as a result of the virus's global economic impact, including the availability of credit, adverse impacts on our liquidity and any recession that has occurred or may occur in the future. There are no comparable recent events that provide guidance as to the effect the spread of COVID-19 as a global pandemic may have, and, as a result, the ultimate impact of the outbreak is highly uncertain and subject to change. We do not yet know the full extent of the impacts on our business, our operations or the global economy as a whole. However, the effects could have a material impact on our results of operations and heighten many of our known risks described herein.

Our business may be adversely affected by conditions in the financial markets and economic conditions generally.

Our financial performance generally, and in particular the ability of borrowers to pay interest on and repay principal of outstanding loans and the value of collateral securing those loans, as well as demand for loans and other products and services we offer and whose success we rely on to drive our growth, is highly dependent upon the business environment in the primary markets where we operate and in the United States as a whole. Unlike larger banks that are more geographically diversified, we are a regional bank that provides banking and financial services to customers primarily in Greenville, Columbia and Charleston, South Carolina; Raleigh, Greensboro and Charlotte, North Carolina; and Atlanta, Georgia. The economic conditions in these local markets may be different from, and in some instances worse than, the economic conditions in the United States as a whole.

Some elements of the business environment that affect our financial performance include short-term and long-term interest rates, the prevailing yield curve, inflation and price levels, monetary and trade policy, unemployment and the strength of the domestic economy and the local economy in the markets in which we operate. Unfavorable market conditions can result in a deterioration in the credit quality of our borrowers and the demand for our products and services, an increase in the number of loan delinquencies, defaults, charge-offs, foreclosures, additional provisions for loan losses, adverse asset values of the collateral securing our loans and an overall material adverse effect on the quality of our loan portfolio. Unfavorable or uncertain economic and market conditions can be caused by declines in economic growth, business activity or investor or business confidence; limitations on the availability or increases in the cost of credit and capital; increases in inflation or interest rates; high unemployment; natural disasters; epidemics and pandemics (such as COVID-19); or a combination of these or other factors.

The impact of the COVID-19 pandemic is fluid and continues to evolve and there is pervasive uncertainty surrounding the future economic conditions that will emerge in the months and years following the onset of the pandemic. Even after the COVID-19 pandemic subsides, the U.S. economy will likely require some time to recover from its effects, the length of which is unknown, and during which we may experience a recession. In addition, there are continuing concerns related to, among other things, the level of U.S. government debt and fiscal actions that may be taken to address that debt, depressed oil prices and a potential resurgence of economic and political tensions with China that may have a destabilizing effect on financial markets and economic activity. Economic pressure on consumers and overall economic uncertainty may result in changes in consumer and business spending, borrowing and saving habits. These economic conditions and/or other negative developments in the domestic or international credit markets or economies may significantly affect the markets in which we do business, the value of our loans and investments, and our ongoing operations, costs and profitability. Declines in real estate values and sales volumes and high unemployment or underemployment may also result in higher than expected loan delinquencies, increases in our levels of nonperforming and classified assets and a decline in demand for our products and services. These negative events may cause us to incur losses and may adversely affect our capital, liquidity and financial condition.

Our small- to medium-sized business target markets may have fewer financial resources to weather a downturn in the economy.

We target the banking and financial services needs of small- and medium-sized businesses. These businesses generally have fewer financial resources in terms of capital borrowing capacity than larger entities. If general economic conditions negatively affect these businesses in the markets in which we operate, our business, financial condition, and results of operations may be adversely affected.

A significant portion of our loan portfolio is secured by real estate, and events that negatively affect the real estate market could hurt our business.

As of December 31, 2020, approximately 84.6% of our loans had real estate as a primary or secondary component of collateral. The real estate collateral in each case provides an alternate source of repayment in the event of default by the borrower and may deteriorate in value during the time the credit is extended. A weakening of the real estate market in our primary market areas could result in an increase in the number of borrowers who default on their loans and a reduction in the value of the collateral securing their loans, which in turn could have an adverse effect on our profitability and asset quality. Deterioration in the real estate market could cause us to adjust our opinion of the level of credit quality in our loan portfolio. If we are required to liquidate the collateral securing a loan to satisfy the debt during a period of reduced real estate values, our earnings and capital could be adversely affected. Acts of nature, including hurricanes, tornados, earthquakes, fires and floods, which may cause uninsured damage and other loss of value to real estate that secures these loans, may also negatively affect our financial condition.

Risks Related to Lending Activities

Our loan portfolio contains a number of real estate loans with relatively large balances.

Because our loan portfolio contains a number of real estate loans with relatively large balances, the deterioration of one or a few of these loans could cause a significant increase in nonperforming loans, which could result in a net loss of earnings, an increase in the provision for loan losses and an increase in loan charge-offs, all of which could have a material adverse effect on our financial condition and results of operations.

Commercial real estate loans increase our exposure to credit risk.

At December 31, 2020, 50.4% of our loan portfolio was secured by commercial real estate. Loans secured by commercial real estate are generally viewed as having more risk of default than loans secured by residential real estate or consumer loans because repayment of the loans often depends on the successful operation of the property, the income stream of the borrowers, the accuracy of the estimate of the property's value at completion of construction, and the estimated cost of construction. Such loans are generally more risky than loans secured by residential real estate or consumer loans because those loans are typically not secured by real estate collateral. An adverse development with respect to one lending relationship can expose us to a significantly greater risk of loss compared with a single-family residential mortgage loan because we typically have more than one loan with such borrowers. Additionally, these loans typically involve larger loan balances to single borrowers or groups of related borrowers compared with single-family residential mortgage loans. Therefore, the deterioration of one or a few of these loans could cause a significant decline in the related asset quality. A return of recessionary conditions due to the COVID-19 pandemic could result in a sharp increase in loans charged-off and could require us to significantly increase our allowance for loan losses, which could have a material adverse impact on our business, financial condition, results of operations, and cash flows.

Environmental liability associated with commercial lending could result in losses.

In the course of business, the Bank may acquire, through foreclosure, or deed in lieu of foreclosure, properties securing loans it has originated or purchased which are in default. Particularly in commercial real estate lending, there is a risk that hazardous substances could be discovered on these properties. In this event, the Bank may be required to remove these substances from the affected properties at our sole cost and expense. The cost of this removal could substantially exceed the value of affected properties. We may not have adequate remedies against the prior owner or other responsible parties and could find it difficult or impossible to sell the affected properties. These events could have a material adverse effect on our business, results of operations and financial condition.

Imposition of limits by the bank regulators on commercial and multi-family real estate lending activities could curtail our growth and adversely affect our earnings.

In 2006, the FDIC, the Federal Reserve and the Office of the Comptroller of the Currency issued joint guidance entitled "Concentrations in Commercial Real Estate Lending, Sound Risk Management Practices" (the "CRE Guidance"). Although the CRE Guidance did not establish specific lending limits, it provides that a bank's commercial real estate lending exposure could receive increased supervisory scrutiny where total non-owner occupied commercial real estate loans, including loans secured by apartment buildings, investor commercial real estate, and construction and land loans, represent 300% or more of an institution's total risk-based capital, and the outstanding balance of the commercial real estate loan portfolio has increased by 50% or more during the preceding 36 months. Our level of commercial real estate and multi-family loans represents 218.5% of the Bank's total risk-based capital at December 31, 2020.

In December 2015, the regulatory agencies released a new statement on prudent risk management for commercial real estate lending (the "2015 Statement"). In the 2015 Statement, the regulatory agencies, among other things, indicate the intent to continue "to pay special attention" to commercial real estate lending activities and concentrations going forward. If the FDIC, our primary federal regulator, were to impose restrictions on the amount of commercial real estate loans we can hold in our portfolio, for reasons noted above or otherwise, our earnings would be adversely affected.

Repayment of our commercial business loans is often dependent on the cash flows of the borrower, which may be unpredictable, and the collateral securing these loans may fluctuate in value.

At December 31, 2020, commercial business loans comprised 14.4% of our total loan portfolio. Our commercial business loans are originated primarily based on the identified cash flow and general liquidity of the borrower and secondarily on the underlying collateral provided by the borrower and/or repayment capacity of any guarantor. The borrower's cash flow may be unpredictable, and collateral securing these loans may fluctuate in value. Although commercial business loans are often collateralized by equipment, inventory, accounts receivable, or other business assets, the liquidation of collateral in the event of default is often an insufficient source of repayment because accounts receivable may be uncollectible and inventories may be obsolete or of limited use. In addition, business assets may depreciate over time, may be difficult to appraise, and may fluctuate in value based on the success of the business. Accordingly, the repayment of commercial business loans depends primarily on the cash flow and credit worthiness of the borrower and secondarily on the underlying collateral value provided by the borrower and liquidity of the guarantor. If these borrowers do not have sufficient cash flows or resources to pay these loans as they come due or the value of the underlying collateral is insufficient to fully secure these loans, we may suffer losses on these loans that exceed our allowance for loan losses.

We may have higher loan losses than we have allowed for in our allowance for loan losses.

Our actual loans losses could exceed our allowance for loan losses and therefore our historic allowance for loan losses may not be adequate. As of December 31, 2020, 50.4% of our loan portfolio was secured by commercial real estate. Repayment of such loans is generally considered more subject to market risk than residential mortgage loans. Industry experience shows that a portion of loans will become delinquent and a portion of loans will require partial or entire charge-off. Regardless of the underwriting criteria utilized, losses may be experienced as a result of various factors beyond our control, including among other things, changes in market conditions affecting the value of loan collateral, the cash flows of our borrowers and problems affecting borrower credit. If we suffer loan losses that exceed our allowance for loans losses, our financial condition, liquidity or results of operations could be materially and adversely affected.

While the fiscal stimulus and relief programs appear to have delayed any materially adverse financial impact to the Bank, once these stimulus programs have been exhausted, we believe our credit metrics could worsen and loan losses could ultimately materialize. Any potential loan losses will be contingent upon a number of factors beyond our control, such as the resurgence of the virus, including any new strains, offset by the potency of the vaccine along with its extensive distribution, and the ability for customers and businesses to return to their pre-pandemic routines.

Our decisions regarding allowance for loan losses and credit risk may materially and adversely affect our business.

Making loans and other extensions of credit is an essential element of our business. Although we seek to mitigate risks inherent in lending by adhering to specific underwriting practices, our loans and other extensions of credit may not be repaid. The risk of nonpayment is affected by a number of factors, including:

- the duration of the credit;
- credit risks of a particular client;
- changes in economic and industry conditions; and
- in the case of a collateralized loan, risks resulting from uncertainties about the future value of the collateral.

We attempt to maintain an appropriate allowance for loan losses to provide for probable losses in our loan portfolio. We periodically determine the amount of the allowance based on consideration of several factors, including but not limited to:

- an ongoing review of the quality, mix, and size of our overall loan portfolio;
- our historical loan loss experience;
- evaluation of economic conditions;
- regular reviews of loan delinquencies and loan portfolio quality;
- ongoing review of financial information provided by borrowers; and
- the amount and quality of collateral, including guarantees, securing the loans.

The determination of the appropriate level of the allowance for loan losses inherently involves a high degree of subjectivity and requires us to make significant estimates of current credit risks and future trends, all of which may undergo material changes. Continuing deterioration in economic conditions affecting borrowers, new information regarding existing loans, identification of additional problem loans and other factors, both within and outside of our control, may require an increase in the allowance for loan losses. In addition, regulatory agencies periodically review our allowance for loan losses and may require an increase in the provision for loan losses or the recognition of further loan charge-offs, based on judgments different than those of management. In addition, if charge-offs in future periods exceed the allowance for loan losses, we will need additional provisions to increase the allowance for loan losses. Any increases in the allowance for loan losses will result in a decrease in net income and, possibly, capital, and may have a material adverse effect on our financial condition and results of operations.

Lack of seasoning of our loan portfolio may increase the risk of credit defaults in the future.

Due to the growth of the Bank and expansion into new markets over the past several years, a portion of the loans in our loan portfolio and our lending relationships are of relatively recent origin. In general, loans do not begin to show signs of credit deterioration or default until they have been outstanding for some period of time, a process we refer to as “seasoning.” As a result, a portfolio of older loans will usually behave more predictably than a newer portfolio. Because our loan portfolio is relatively new, the current level of delinquencies and defaults may not be representative of the level that will prevail when the portfolio becomes more seasoned, which may be higher than current levels. If delinquencies and defaults increase, we may be required to increase our provision for loan losses, which would adversely affect our results of operations and financial condition.

A percentage of the loans in our portfolio currently include exceptions to our loan policies and supervisory guidelines.

All of the loans that we make are subject to written loan policies adopted by our board of directors and to supervisory guidelines imposed by our regulators. Our loan policies are designed to reduce the risks associated with the loans that we make by requiring our loan officers to take certain steps that vary depending on the type and amount of the loan, prior to closing a loan. These steps include, among other things, making sure the proper liens are documented and perfected on property securing a loan, and requiring proof of adequate insurance coverage on property securing loans. Loans that do not fully comply with our loan policies are known as “exceptions.” We categorize exceptions as policy exceptions, financial statement exceptions and document exceptions. As a result of these exceptions, such loans may have a higher risk of loan loss than the other loans in our portfolio that fully comply with our loan policies. In addition, we may be subject to regulatory action by federal or state banking authorities if they believe the number of exceptions in our loan portfolio represents an unsafe banking practice.

Risks Related to Capital and Liquidity

Liquidity needs could adversely affect our financial condition and results of operations.

Dividends from the Bank provide the primary source of funds for the Company. The primary sources of funds of the Bank are client deposits and loan repayments. While scheduled loan repayments are a relatively stable source of funds, they are subject to the ability of borrowers to repay the loans. The ability of borrowers to repay loans can be adversely affected by a number of factors, including changes in economic conditions, adverse trends or events affecting business industry groups, reductions in real estate values or markets, business closings or lay-offs, inclement weather, natural disasters and international instability.

Additionally, deposit levels may be affected by a number of factors, including rates paid by competitors, general interest rate levels, regulatory capital requirements, returns available to clients on alternative investments and general economic conditions. Accordingly, we may be required from time to time to rely on secondary sources of liquidity to meet withdrawal demands or otherwise fund operations. Such sources include proceeds from FHLB advances, sales of investment securities and loans, and federal funds lines of credit from correspondent banks, as well as out-of-market time deposits. While we believe that these sources are currently adequate, there can be no assurance they will be sufficient to meet future liquidity demands, particularly if we continue to grow and experience increasing loan demand. We may be required to slow or discontinue loan growth, capital expenditures or other investments or liquidate assets should such sources not be adequate.

The Company is a stand-alone entity with its own liquidity needs to service its debt or other obligations. Other than dividends from the Bank, the Company does not have additional means of generating liquidity without obtaining additional debt or equity funding. If we are unable to receive dividends from the Bank or obtain additional funding, we may be unable to pay our debt or other obligations.

We may be subject to more stringent capital requirements in the future.

We are subject to regulatory requirements specifying minimum amounts and types of capital that we must maintain. From time to time, the regulators change these regulatory capital adequacy guidelines. If we fail to meet these minimum capital guidelines and other regulatory requirements, we or our subsidiaries may be restricted in the types of activities we may conduct and we may be prohibited from taking certain capital actions, such as paying dividends and repurchasing or redeeming capital securities.

In particular, the capital requirements applicable to the Bank under the Basel III rules become fully phased-in on January 1, 2019. The Bank is now required to satisfy additional, more stringent, capital adequacy standards than it had in the past. While we expect to meet the requirements of the Basel III rules, we may fail to do so. Failure to meet minimum capital requirements could result in certain mandatory and possible additional discretionary actions by regulators that, if undertaken, could have an adverse material effect on our financial condition and results of operations. In addition, these requirements could have a negative impact on our ability to lend, grow deposit balances, make acquisitions or make capital distributions in the form of dividends or share repurchases. Higher capital levels could also lower our return on equity.

Legal, Accounting, Regulatory and Compliance Risks

We are subject to extensive regulation that could restrict our activities, have an adverse impact on our operations, and impose financial requirements or limitations on the conduct of our business.

We operate in a highly regulated industry and are subject to examination, supervision, and comprehensive regulation by various regulatory agencies. We are subject to regulation by the Federal Reserve. The Bank is subject to extensive regulation, supervision, and examination by our primary federal regulator, the FDIC, the regulating authority that insures client deposits, and by our primary state regulator, the S.C. Board. Also, as a member of the Federal Home Loan Bank, the Bank must comply with applicable regulations of the Federal Housing Finance Board and the Federal Home Loan Bank. Regulation by these agencies is intended primarily for the protection of our depositors and the deposit insurance fund and not for the benefit of our shareholders. The Bank’s activities are also regulated under consumer protection laws applicable to our lending, deposit, and other activities. A sufficient claim against us under these laws could have a material adverse effect on our results of operations.

Failure to comply with laws, regulations or policies could also result in heightened regulatory scrutiny and in sanctions by regulatory agencies (such as a memorandum of understanding, a written supervisory agreement or a cease and desist order), civil money penalties and/or reputation damage. Any of these consequences could restrict our ability to expand our business or could require us to raise additional capital or sell assets on terms that are not advantageous to us or our shareholders and could have a material adverse effect on our business, financial condition and results of operations. While we have policies and procedures designed to prevent any such violations, such violations may occur despite our best efforts.

We face risks related to the adoption of future legislation and potential changes in federal regulatory agency leadership, policies, and priorities.

With a new Congress taking office in January 2021, Democrats have retained control of the U.S. House of Representatives, and have gained control of the U.S. Senate, albeit with a majority found only in the tie-breaking vote of Vice President Harris. However slim the majorities, though, the net result is unified Democratic control of the White House and both chambers of Congress, and consequently Democrats will be able to set the agenda both legislatively and in the Administration. We expect that Democratic-led Congressional committees will pursue greater oversight and will also pay increased attention to the banking sector’s role in providing COVID-19-related assistance. The prospects for the enactment of major banking reform legislation under the new Congress are unclear at this time.

Moreover, the turnover of the presidential administration has produced, and likely will continue to produce, certain changes in the leadership and senior staffs of the federal banking agencies, the CFPB, SEC, and the Treasury Department. These changes could impact the rulemaking, supervision, examination and enforcement priorities and policies of the agencies. Of note, promptly after taking office, President Biden issued an Executive Order instituting a “freeze” of certain recently-finalized and pending regulations to allow for review by incoming Administration officials. As a result of this Executive Order, recently-adopted regulations may be subject to further notice-and-comment rulemaking and, more broadly, agency rulemaking agendas may be disrupted. The potential impact of any changes in agency personnel, policies and priorities on the financial services sector, including the Bank, cannot be predicted at this time. Regulations and laws may be modified at any time, and new legislation may be enacted that will affect us. Any future changes in federal and state laws and regulations, as well as the interpretation and implementation of such laws and regulations, could affect us in substantial and unpredictable ways, including those listed above or other ways that could have a material adverse effect on our business, financial condition or results of operations.

We face a risk of noncompliance and enforcement action with the Bank Secrecy Act and other anti-money laundering statutes and regulations.

The federal Bank Secrecy Act, the USA Patriot Act and other laws and regulations require financial institutions, among other duties, to institute and maintain effective anti-money laundering programs and file suspicious activity and currency transaction reports as appropriate. The federal Financial Crimes Enforcement Network, established by the U.S. Treasury to administer the Bank Secrecy Act, is authorized to impose significant civil money penalties for violations of those requirements and has engaged in coordinated enforcement efforts with the individual federal banking regulators, as well as the U.S. Department of Justice, Drug Enforcement Administration and Internal Revenue Service. There is also increased scrutiny of compliance with the rules enforced by OFAC. Federal and state bank regulators also focus on compliance with Bank Secrecy Act and anti-money laundering regulations. If our policies, procedures and systems are deemed deficient or the policies, procedures and systems of the financial institutions that we have already acquired or may acquire in the future are deficient, we would be subject to liability, including fines and regulatory actions such as restrictions on our ability to pay dividends and the necessity to obtain regulatory approvals to proceed with certain aspects of our business plan, including our acquisition plans, which would negatively affect our business, financial condition and results of operations. Failure to maintain and implement adequate programs to combat money laundering and terrorist financing could also have serious reputational consequences for us.

Federal, state and local consumer lending laws may restrict our ability to originate certain mortgage loans or increase our risk of liability with respect to such loans and could increase our cost of doing business.

Federal, state and local laws have been adopted that are intended to eliminate certain lending practices considered “predatory.” These laws prohibit practices such as steering borrowers away from more affordable products, selling unnecessary insurance to borrowers, repeatedly refinancing loans and making loans without a reasonable expectation that the borrowers will be able to repay the loans irrespective of the value of the underlying property. Loans with certain terms and conditions and that otherwise meet the definition of a “qualified mortgage” may be protected from liability to a borrower for failing to make the necessary determinations. In either case, we may find it necessary to tighten our mortgage loan underwriting standards in response to the CFPB rules, which may constrain our ability to make loans consistent with our business strategies. It is our policy not to make predatory loans and to determine borrowers' ability to repay, but the law and related rules create the potential for increased liability with respect to our lending and loan investment activities. They increase our cost of doing business and, ultimately, may prevent us from making certain loans and cause us to reduce the average percentage rate or the points and fees on loans that we do make.

We are subject to federal and state fair lending laws, and failure to comply with these laws could lead to material penalties.

Federal and state fair lending laws and regulations, such as the Equal Credit Opportunity Act and the Fair Housing Act, impose nondiscriminatory lending requirements on financial institutions. The Department of Justice, CFPB and other federal and state agencies are responsible for enforcing these laws and regulations. Private parties may also have the ability to challenge an institution's performance under fair lending laws in private class action litigation. A successful challenge to our performance under the fair lending laws and regulations could adversely impact our rating under the Community Reinvestment Act and result in a wide variety of sanctions, including the required payment of damages and civil money penalties, injunctive relief, imposition of restrictions on merger and acquisition activity and restrictions on expansion activity, which could negatively affect our reputation, business, financial condition and results of operations.

The Federal Reserve may require us to commit capital resources to support the Bank.

The Federal Reserve requires a bank holding company to act as a source of financial and managerial strength to a subsidiary bank and to commit resources to support such subsidiary bank. Under the “source of strength” doctrine, the Federal Reserve may require a bank holding company to make capital injections into a troubled subsidiary bank and may charge the bank holding company with engaging in unsafe and unsound practices for failure to commit resources to such a subsidiary bank. In addition, the Dodd-Frank Act directs the federal bank regulators to require that all companies that directly or indirectly control an insured depository institution serve as a source of strength for the institution. Under these requirements, in the future, we could be required to provide financial assistance to the Bank if the Bank experiences financial distress.

A capital injection may be required at times when we do not have the resources to provide it, and therefore we may be required to borrow the funds. In the event of a bank holding company's bankruptcy, the bankruptcy trustee will assume any commitment by the holding company to a federal bank regulatory agency to maintain the capital of a subsidiary bank. Moreover, bankruptcy law provides that claims based on any such commitment will be entitled to a priority of payment over the claims of the holding company's general unsecured creditors, including the holders of its note obligations. Thus, any borrowing that must be done by the holding company in order to make the required capital injection becomes more difficult and expensive and will adversely impact the holding company's cash flows, financial condition, results of operations and prospects.

A new accounting standard will result in a significant change in how we recognize credit losses and may have a material impact on our financial condition or results of operations.

In June 2016, the Financial Accounting Standards Board (“FASB”) issued an accounting standard update, “Financial Instruments-Credit Losses (Topic 326), Measurement of Credit Losses on Financial Instruments,” which replaces the current “incurred loss” model for recognizing credit losses with an “expected loss” model referred to as the Current Expected Credit Loss (“CECL”) model. Under the CECL model, we will be required to present certain financial assets carried at amortized cost, such as loans held for investment and held-to-maturity debt securities, at the net amount expected to be collected. The measurement of expected credit losses is to be based on information about past events, including historical experience, current conditions, and reasonable and supportable forecasts that affect the collectability of the reported amount. This measurement will take place at the time the financial asset is first added to the balance sheet and periodically thereafter. This differs significantly from the “incurred loss” model required under current generally accepted accounting principles (“GAAP”), which delays recognition until it is probable a loss has been incurred. Accordingly, we expect that the adoption of the CECL model will materially affect how we determine our allowance for loan losses and could require us to significantly increase our allowance. Moreover, the CECL model may create more volatility in the level of our allowance for loan losses. If we are required to materially increase our level of allowance for loan losses for any reason, such increase could adversely affect our business, financial condition and results of operations.

The new CECL standard will become effective for us on January 1, 2023 and for interim periods within that year. We are currently evaluating the impact the CECL model will have on our accounting, but we expect to recognize a one-time cumulative-effect adjustment to our allowance for loan losses as of the beginning of the first reporting period in which the new standard is effective, consistent with regulatory expectations set forth in interagency guidance issued at the end of 2016. We cannot yet determine the magnitude of any such one-time cumulative adjustment or of the overall impact of the new standard on our business, financial condition and results of operations.

Risks Related to Our Operations

Competition with other financial institutions may have an adverse effect on our ability to retain and grow our client base, which could have a negative effect on our financial condition or results of operations.

The banking and financial services industry is very competitive and includes services offered from other banks, savings and loan associations, credit unions, mortgage companies, other lenders, and institutions offering uninsured investment alternatives. Legal and regulatory developments have made it easier for new and sometimes unregulated competitors to compete with us. The financial services industry has and is experiencing an ongoing trend towards consolidation in which fewer large national and regional banks and other financial institutions are replacing many smaller and more local banks. These larger banks and other financial institutions hold a large accumulation of assets and have significantly greater resources and a wider geographic presence or greater accessibility. In some instances, these larger entities operate without the traditional brick and mortar facilities that restrict geographic presence. Some competitors have more aggressive marketing campaigns and better brand recognition, and are able to offer more services, more favorable pricing or greater customer convenience than the Bank. In addition, competition has increased from new banks and other financial services providers that target our existing or potential clients. As consolidation continues among large banks, we expect other smaller institutions to try to compete in the markets we serve. This competition could reduce our net income by decreasing the number and size of the loans that we originate and the interest rates we charge on these loans. Additionally, these competitors may offer higher interest rates, which could decrease the deposits we attract or require us to increase rates to retain existing deposits or attract new deposits. Increased deposit competition could adversely affect our ability to generate the funds necessary for lending operations which could increase our cost of funds.

The financial services industry could become even more competitive as a result of legislative, regulatory and technological changes and continued consolidation. Banks, securities firms and insurance companies can merge as part of a financial holding company, which can offer virtually any type of financial service, including banking, securities underwriting, insurance (both agency and underwriting) and merchant banking. Technological developments have allowed competitors, including some non-depository institutions, to compete more effectively in local markets and have expanded the range of financial products, services and capital available to our target clients. If we are unable to implement, maintain and use such technologies effectively, we may not be able to offer products or achieve cost-efficiencies necessary to compete in the industry. In addition, some of these competitors have fewer regulatory constraints and lower cost structures.

We rely on other companies to provide key components of our business infrastructure.

Third parties provide key components of our business operations such as data processing, recording and monitoring transactions, online banking interfaces and services, internet connections and network access. While we have selected these third party vendors carefully, we do not control their actions. Any problem caused by these third parties, including poor performance of services, data breaches, failure to provide services, disruptions in communication services provided by a vendor and failure to handle current or higher volumes, could adversely affect our ability to deliver products and services to our clients and otherwise conduct our business, and may harm our reputation. Financial or operational difficulties of a third party vendor could also hurt our operations if those difficulties interfere with the vendor’s ability to serve us. Replacing these third party vendors could also create significant delay and expense. Accordingly, use of such third parties creates an unavoidable inherent risk to our business operations.

We may be adversely affected by the soundness of other financial institutions.

Financial services institutions are interrelated as a result of trading, clearing, counterparty, or other relationships. We have exposure to many different industries and counterparties, and routinely execute transactions with counterparties in the financial services industry, including commercial banks, brokers and dealers, investment banks, and other institutional clients. Many of these transactions expose us to credit risk in the event of a default by a counterparty or client. In addition, our credit risk may be exacerbated when the collateral held by the Bank cannot be realized upon or is liquidated at prices not sufficient to recover the full amount of the credit or derivative exposure due to the Bank. Any such losses could have a material adverse effect on our financial condition and results of operations.

We are subject to losses due to errors, omissions or fraudulent behavior by our employees, clients, counterparties or other third parties.

We are exposed to many types of operational risk, including the risk of fraud by employees and third parties, clerical recordkeeping errors and transactional errors. Our business is dependent on our employees as well as third-party service providers to process a large number of increasingly complex transactions. We could be materially and adversely affected if employees, clients, counterparties or other third parties caused an operational breakdown or failure, either as a result of human error, fraudulent manipulation or purposeful damage to any of our operations or systems.

In deciding whether to extend credit or to enter into other transactions with clients and counterparties, we may rely on information furnished to us by or on behalf of clients and counterparties, including financial statements and other financial information, which we do not independently verify. We also may rely on representations of clients and counterparties as to the accuracy and completeness of that information and, with respect to financial statements, on reports of independent auditors. For example, in deciding whether to extend credit to clients, we may assume that a client’s audited financial statements conform with GAAP and present fairly, in all material respects, the financial condition, results of operations and cash flows of the client. Our financial condition and results of operations could be negatively affected to the extent we rely on financial statements that do not comply with GAAP or are materially misleading, any of which could be caused by errors, omissions, or fraudulent behavior by our employees, clients, counterparties, or other third parties.

Our operational or security systems may experience an interruption or breach in security, including as a result of cyber-attacks.

We rely heavily on communications and information systems to conduct our business. Any failure, interruption or breach in security of these systems, including as a result of cyber-attacks, could result in failures or disruptions in our client relationship management, deposit, loan, and other systems and also the disclosure or misuse of confidential or proprietary information. While we have systems, policies and procedures designed to prevent or limit the effect of the failure, interruption or security breach of our information systems, there can be no assurance that any such failures, interruptions or security breaches will not occur or, if they do occur, that they will be adequately addressed. The occurrence of any failures, interruptions or security breaches of our information systems could damage our reputation, result in a loss of client business, subject us to additional regulatory scrutiny, or expose us to civil litigation and possible financial liability, any of which could have a material adverse effect on our business, financial condition and results of operations.

Furthermore, information security risks for financial institutions have generally increased in recent years in part because of the proliferation of new technologies, the use of the Internet and telecommunications technologies to conduct financial transactions, and the increased sophistication and activities of organized crime, hackers, terrorists, activists, and other external parties. Our technologies, systems, networks, and our customers’ devices may become the target of cyber-attacks or information security breaches that could result in the unauthorized release, gathering, monitoring, misuse, loss or destruction of our or our customers’ confidential, proprietary and other information, or otherwise disrupt our or our customers’ or other third parties’ business operations. As cyber threats continue to evolve, we may also be required to expend significant additional resources to continue to modify or enhance our protective measures or to investigate and remediate any information security vulnerabilities.

While we have not experienced any material losses relating to cyber-attacks or other information security breaches to date, we may suffer such losses in the future and any information security breach could result in significant costs to us, which may include fines and penalties, potential liabilities from governmental or third party investigations, proceedings or litigation, legal, forensic and consulting fees and expenses, costs and diversion of management attention required for investigation and remediation actions, and the negative impact on our reputation and loss of confidence of our customers and others, any of which could have a material adverse impact on our business, financial condition and operating results.

Our controls and procedures may fail or be circumvented.

We regularly review and update our internal controls, disclosure controls and procedures, and corporate governance policies and procedures. Any system of controls, however well designed and operated, is based in part on certain assumptions and can provide only reasonable, not absolute, assurances that the objectives of the system are met. Any failure or circumvention of our controls and procedures or failure to comply with regulations related to controls and procedures could have a material adverse effect on our business, results of operations and financial condition.

Failure to keep pace with technological change could adversely affect our business.

The financial services industry is continually undergoing rapid technological change with frequent introductions of new technology-driven products and services. The effective use of technology increases efficiency and enables financial institutions to better serve customers and to reduce costs. Our future success depends, in part, upon our ability to address the needs of our customers by using technology to provide products and services that will satisfy customer demands, as well as to create additional efficiencies in our operations. Many of our competitors have substantially greater resources to invest in technological improvements. We may not be able to effectively implement new technology-driven products and services or be successful in marketing these products and services to our customers. Failure to successfully keep pace with technological change affecting the financial services industry could have a material adverse impact on our business and, in turn, our financial condition and results of operations.

Our profitability is dependent on our banking activities.

Because we are a bank holding company, our profitability is directly attributable to the success of the Bank. Our banking activities compete with other banking institutions on the basis of products, service, convenience and price, among others. Due in part to both regulatory changes and consumer demands, banks have experienced increased competition from other entities offering similar products and services. We rely on the profitability of the Bank and dividends received from the Bank for payment of our operating expenses and satisfaction of our obligations. As is the case with other similarly situated financial institutions, our profitability will be subject to the fluctuating cost and availability of funds, changes in the prime lending rate and other interest rates, changes in economic conditions in general, and other factors.

Risks Related to Our Industry

We are subject to interest rate risk, which could adversely affect our financial condition and profitability.

A significant portion of our banking assets are subject to changes in interest rates. As of December 31, 2020, approximately 81% of our loan portfolio was in fixed rate loans, while only 19% was in variable rate loans. Like most financial institutions, our earnings significantly depend on our net interest income, the principal component of our earnings, which is the difference between interest earned by us from our interest-earning assets, such as loans and investment securities, and interest paid by us on our interest-bearing liabilities, such as deposits and borrowings. We expect that we will periodically experience “gaps” in the interest rate sensitivities of our assets and liabilities, meaning that either our interest-bearing liabilities will be more sensitive to changes in market interest rates than our interest-earning assets, or vice versa. In either event, if market interest rates should move contrary to our position, this “gap” will negatively impact our earnings. Many factors beyond our control impact interest rates, including economic conditions, governmental monetary policies, inflation, recession, changes in unemployment, the money supply, and disorder and instability in domestic and foreign financial markets. Changes in monetary policies of the various government agencies could influence not only the interest we receive on loans and securities and the interest we pay on deposits and borrowings, but such changes could also affect our ability to originate loans and obtain deposits, the fair value of our financial assets and liabilities, and the average duration of our assets and liabilities.

In a declining interest rate environment, there may be an increase in prepayments on loans as borrowers refinance their loans at lower rates. Interest rate increases often result in larger payment requirements for our floating interest rate borrowers, which increases the potential for default. At the same time, the marketability of the property securing a loan may be adversely affected by any reduced demand resulting from higher interest rates. An increase (or decrease) in interest rates may also require us to increase (or decrease) the interest rates that we pay on our deposits. Changes in interest rates also can affect the value of loans, securities and other assets. An increase in interest rates that adversely affects the ability of borrowers to pay the principal or interest on loans may lead to increases in nonperforming assets, charge-offs and delinquencies, further increases to the allowance for loan losses, and a reduction of income recognized, among others, which could have a material adverse effect on our results of operations and cash flows. Further, when we place a loan on non-accrual status, we reverse any accrued but unpaid interest receivable, which decreases interest income. At the same time, we continue to have a cost to fund the loan, which is reflected as interest expense, without any interest income to offset the associated funding expense. Thus, an increase in the amount of nonperforming assets could have a material adverse impact on our net interest income.

In response to the COVID-19 pandemic, the FOMC cut short-term interest rates to a record low range of 0% to 0.25%, and the Federal Reserve has indicated it expects rates to remain within this range through 2023 and possibly longer. If short-term interest rates continue to remain at their historically low levels for a prolonged period and assuming longer-term interest rates fall further, we could experience net interest margin compression as our interest-earning assets would continue to reprice downward while our interest-bearing liability rates could fail to decline in tandem, which would have an adverse effect on our net interest income.

In addition, our mortgage operations provide a portion of our noninterest income. We generate mortgage revenues primarily from gains on the sale of residential mortgage loans pursuant to programs currently offered by Fannie Mae, Ginnie Mae or Freddie Mac. In a rising or higher interest rate environment, our originations of mortgage loans may decrease, resulting in fewer loans that are available to be sold to investors, which would decrease mortgage revenues in noninterest income. In addition, our results of operations are affected by the amount of noninterest expenses associated with mortgage activities, such as salaries and employee benefits, other loan expense, and other costs. During periods of reduced loan demand, our results of operations may be adversely affected to the extent that we are unable to reduce expenses commensurate with the decline in loan originations.

Higher FDIC deposit insurance premiums and assessments could adversely affect our financial condition.

Our deposits are insured up to applicable limits by the Deposit Insurance Fund of the FDIC and are subject to deposit insurance assessments to maintain deposit insurance. As an FDIC-insured institution, we are required to pay quarterly deposit insurance premium assessments to the FDIC. Although we cannot predict what the insurance assessment rates will be in the future, either deterioration in our risk-based capital ratios or adjustments to the base assessment rates could have a material adverse impact on our business, financial condition, results of operations, and cash flows.

The phase-out of LIBOR could negatively impact our net interest income and require significant operational work.

The United Kingdom’s Financial Conduct Authority, which regulates the London Interbank Offered Rate (“LIBOR”), has announced that it will not compel panel banks to contribute to LIBOR after 2021. The discontinuance of LIBOR has resulted in significant uncertainty regarding the transition to suitable alternative reference rates and could adversely impact our business, operations, and financial results.

The Federal Reserve, in conjunction with the Alternative Reference Rates Committee, a steering committee comprised of large U.S. financial institutions, has endorsed replacing the U.S. dollar LIBOR with a new index calculated by short-term repurchase agreements, backed by Treasury securities (“SOFR”). SOFR is observed and backward looking, which stands in contrast with LIBOR under the current methodology, which is an estimated forward-looking rate and relies, to some degree, on the expert judgment of submitting panel members. Given that SOFR is a secured rate backed by government securities, it will be a rate that does not take into account bank credit risk (as is the case with LIBOR). In November 2020, the federal banking agencies issued a statement that says that banks may use any reference rate for its loans that the bank determines to be appropriate for its funding model and customer needs.

We have exposure to LIBOR-based products, including loans and securities, and we are preparing to transition away from the widespread use of LIBOR to alternative rates. As of December 31, 2020, $82.7 million, or 3.9% of our loan portfolio, was tied to LIBOR. We continue to monitor market developments and regulatory updates, including recent announcements from the ICE Benchmark Administrator to extend the cessation date for several USD LIBOR tenors to June 30, 2023, as well as collaborate with regulators and industry groups on the transition. The manner and impact of this transition, as well as the effect of these developments on our funding costs, loan and investment and trading securities portfolios, asset-liability management, and business, is uncertain.

Negative public opinion surrounding the Company and the financial institutions industry generally could damage our reputation and adversely impact our earnings.

Reputation risk, or the risk to our business, earnings and capital from negative public opinion surrounding the Company and the financial institutions industry generally, is inherent in our business. Negative public opinion can result from our actual or alleged conduct in any number of activities, including lending practices, corporate governance and acquisitions, and from actions taken by government regulators and community organizations in response to those activities. Negative public opinion can adversely affect our ability to keep and attract clients and employees and can expose us to litigation and regulatory action. Although we take steps to minimize reputation risk in dealing with our clients and communities, this risk will always be present given the nature of our business.

Consumers may decide not to use banks to complete their financial transactions.

Technology and other changes are allowing parties to complete financial transactions through alternative methods that historically have involved banks. For example, consumers can now maintain funds that would have historically been held as bank deposits in brokerage accounts, mutual funds or general-purpose reloadable prepaid cards. Consumers can also complete transactions such as paying bills and/or transferring funds directly without the assistance of banks. The process of eliminating banks as intermediaries, known as “disintermediation,” could result in the loss of fee income, as well as the loss of customer deposits and the related income generated from those deposits. The loss of these revenue streams and the lower cost of deposits as a source of funds could have a material adverse effect on our financial condition and results of operations.

Risks Related to Our Strategic Plans

We are dependent on key individuals and the loss of one or more of these key individuals could curtail our growth and adversely affect our prospects.

R. Arthur Seaver, Jr., our chief executive officer and Michael D. Dowling, our chief financial officer and chief operating officer, both have extensive and long-standing ties within our primary market area and substantial experience with our operations, and each has contributed significantly to our growth. If we lose the services of any of these individuals, they would be difficult to replace and our business and development could be materially and adversely affected.

Our success also depends, in part, on our continued ability to attract and retain experienced loan originators, as well as other management personnel, including other executive vice presidents. Competition for personnel is intense, and we may not be successful in attracting or retaining qualified personnel. Our failure to compete for these personnel, or the loss of the services of several of such key personnel, could adversely affect our growth strategy and materially and adversely affect our business, results of operations, and financial condition.

The success of our growth strategy depends on our ability to identify and retain individuals with experience and relationships in the markets in which we intend to expand.

To expand our franchise successfully, we must identify and retain experienced key management members with local expertise and relationships in these markets. We expect that competition for qualified management in the markets in which we may expand will be intense and that there will be a limited number of qualified persons with knowledge of and experience in the community banking industry in these markets. Even if we identify individuals that we believe could assist us in establishing a presence in a new market, we may be unable to recruit these individuals away from more established financial institutions. In addition, the process of identifying and recruiting individuals with the combination of skills and attributes required to carry out our strategy requires both management and financial resources and is often lengthy. Our inability to identify, recruit, and retain talented personnel to manage new offices effectively would limit our growth and could materially adversely affect our business, financial condition, and results of operations.

We will face risks with respect to future expansion.

We routinely evaluate opportunities to expand into new markets, as we did in Columbia, South Carolina in 2007, Charleston, South Carolina in 2012, Raleigh, North Carolina in 2017, Atlanta, Georgia in 2017, Summerville, South Carolina and Greensboro, North Carolina in 2018 and Charlotte, North Carolina in 2021. We may also expand our lines of business or offer new products or services as well as seek to acquire other financial institutions or parts of those institutions. Our merger and acquisition activities could be material and could require us to use a substantial amount of common stock, cash, other liquid assets, and/or incur debt. Moreover, these types of expansions involve various risks, including:

- the time and costs of evaluating new markets, hiring or retaining experienced local management, and opening new offices and the time lags between these activities and the generation of sufficient assets and deposits to support the costs of the expansion;
- the incurrence and possible impairment of goodwill associated with an acquisition and possible adverse effects on our results of operations;
- the potential inaccuracy of the estimates and judgments used to evaluate credit, operations, management, and market risks with respect to a target institution;
- incurring the time and expense associated with identifying and evaluating potential merger or acquisition targets and other expansion opportunities and negotiating potential transactions, resulting in management's attention being diverted from the operation of our existing business;
- the possibility that the expected benefits of a transaction may not materialize in the timeframe expected or at all, or may be costlier to achieve;
- the risk that we may be unsuccessful in attracting and retaining deposits and originating high quality loans in new markets;
- difficulty or unanticipated expense associated with converting the operating systems of an acquired or merged company into ours;
- delay in completing a merger, acquisition or other expansion activities due to litigation, closing conditions or the regulatory approval process; and
- the risk of loss of key employees and clients of the Company or the acquired or merged company.

There is no assurance that existing branches or future branches will maintain or achieve deposit levels, loan balances or other operating results necessary to avoid losses or produce profits. Our growth may entail an increase in overhead expenses as we add new branches and staff. There are considerable costs involved in opening branches, and new branches generally do not generate sufficient revenues to offset their costs until they have been in operation for at least a year or more. Accordingly, any new branches we establish can be expected to negatively impact our earnings for some period of time until they reach certain economies of scale. Our historical results may not be indicative of future results or results that may be achieved, particularly if we continue to expand.

Failure to successfully address these and other issues related to our expansion could have a material adverse effect on our business, financial condition and results of operations, including short-term and long-term liquidity, and could adversely affect our ability to successfully implement our business strategy.

New lines of business or new products and services may subject us to additional risk.

From time to time, we may implement new lines of business or offer new products and services within existing lines of business. There are substantial risks and uncertainties associated with these efforts, particularly in instances where the markets are not fully developed. In developing and marketing new lines of business and/or new products and services, we may invest significant time and resources. Initial timetables for the introduction and development of new lines of business and/or new products or services may not be achieved and price and profitability targets may not prove feasible. External factors, such as compliance with regulations, competitive alternatives, and shifting market preferences, may also impact the successful implementation of a new line of business and/or a new product or service. Furthermore, any new line of business and/or new product or service could have a significant impact on the effectiveness of our system of internal controls. Failure to successfully manage these risks in the development and implementation of new lines of business and/or new products or services could have a material adverse effect on our business and, in turn, our financial condition and results of operations.

Risks Related to Our Common Stock

Our ability to pay cash dividends is limited, and we may be unable to pay future dividends even if we desire to do so.

The Federal Reserve has issued a policy statement regarding the payment of dividends by bank holding companies. In general, the Federal Reserve's policies provide that dividends should be paid only out of current earnings and only if the prospective rate of earnings retention by the bank holding company appears consistent with the organization's capital needs, asset quality and overall financial condition. The Federal Reserve's policies also require that a bank holding company serve as a source of financial strength to its subsidiary banks by standing ready to use available resources to provide adequate capital funds to those banks during periods of financial stress or adversity and by maintaining the financial flexibility and capital-raising capacity to obtain additional resources for assisting its subsidiary banks where necessary. Further, under the prompt corrective action regulations, the ability of a bank holding company to pay dividends may be restricted if a subsidiary bank becomes undercapitalized. These regulatory policies could affect the ability of the Company to pay dividends or otherwise engage in capital distributions.

Statutory and regulatory limitations apply to the Bank's payment of dividends to the Company. As a South Carolina chartered bank, the Bank is subject to limitations on the amount of dividends that it is permitted to pay. Unless otherwise instructed by the S.C. Board, the Bank is generally permitted under South Carolina state banking regulations to pay cash dividends of up to 100% of net income in any calendar year without obtaining the prior approval of the S.C. Board. The FDIC also has the authority under federal law to enjoin a bank from engaging in what in its opinion constitutes an unsafe or unsound practice in conducting its business, including the payment of a dividend under certain circumstances. If the Bank is not permitted to pay cash dividends to the Company, it is unlikely that we would be able to pay cash dividends on our common stock. Moreover, holders of our common stock are entitled to receive dividends only when, and if declared by our board of directors.

Our stock price may be volatile, which could result in losses to our investors and litigation against us.

Our stock price has been volatile in the past and several factors could cause the price to fluctuate substantially in the future. These factors include but are not limited to: actual or anticipated variations in earnings, changes in analysts' recommendations or projections, our announcement of developments related to our businesses, operations and stock performance of other companies deemed to be peers, new technology used or services offered by traditional and non-traditional competitors, news reports of trends, irrational exuberance on the part of investors, new federal banking regulations, and other issues related to the financial services industry. Our stock price may fluctuate significantly in the future, and these fluctuations may be unrelated to our performance. General market declines or market volatility in the future, especially in the financial institutions sector, could adversely affect the price of our common stock, and the current market price may not be indicative of future market prices. Stock price volatility may make it more difficult for you to resell your common stock when you want and at prices you find attractive. Moreover, in the past, securities class action lawsuits have been instituted against some companies following periods of volatility in the market price of its securities. We could in the future be the target of similar litigation. Securities litigation could result in substantial costs and divert management's attention and resources from our normal business.

Future sales of our stock by our shareholders or the perception that those sales could occur may cause our stock price to decline.

Although our common stock is listed for trading on The NASDAQ Global Market, the trading volume in our common stock is lower than that of other larger financial services companies. A public trading market having the desired characteristics of depth, liquidity and orderliness depends on the presence in the marketplace of willing buyers and sellers of our common stock at any given time. This presence depends on the individual decisions of investors and general economic and market conditions over which we have no control. Given the relatively low trading volume of our common stock, significant sales of our common stock in the public market, or the perception that those sales may occur, could cause the trading price of our common stock to decline or to be lower than it otherwise might be in the absence of those sales or perceptions.

Economic and other circumstances may require us to raise capital at times or in amounts that are unfavorable to us. If we have to issue shares of common stock, they will dilute the percentage ownership interest of existing shareholders and may dilute the book value per share of our common stock and adversely affect the terms on which we may obtain additional capital.

We may need to incur additional debt or equity financing in the future to make strategic acquisitions or investments or to strengthen our capital position. Our ability to raise additional capital, if needed, will depend on, among other things, conditions in the capital markets at that time, which are outside of our control and our financial performance. We cannot provide assurance that such financing will be available to us on acceptable terms or at all, or if we do raise additional capital that it will not be dilutive to existing shareholders.

If we determine, for any reason, that we need to raise capital, subject to applicable NASDAQ rules, our board generally has the authority, without action by or vote of the shareholders, to issue all or part of any authorized but unissued shares of stock for any corporate purpose, including issuance of equity-based incentives under or outside of our equity compensation plans. Additionally, we are not restricted from issuing additional common stock or preferred stock, including any securities that are convertible into or exchangeable for, or that represent the right to receive, common stock or preferred stock or any substantially similar securities. The market price of our common stock could decline as a result of sales by us of a large number of shares of common stock or preferred stock or similar securities in the market or from the perception that such sales could occur. If we issue preferred stock that has a preference over the common stock with respect to the payment of dividends or upon liquidation, dissolution or winding-up, or if we issue preferred stock with voting rights that dilute the voting power of the common stock, the rights of holders of the common stock or the market price of our common stock could be adversely affected. Any issuance of additional shares of stock will dilute the percentage ownership interest of our shareholders and may dilute the book value per share of our common stock. Shares we issue in connection with any such offering will increase the total number of shares and may dilute the economic and voting ownership interest of our existing shareholders.

Provisions of our articles of incorporation and bylaws, South Carolina law, and state and federal banking regulations, could delay or prevent a takeover by a third party.

Our articles of incorporation and bylaws could delay, defer, or prevent a third party takeover, despite possible benefit to the shareholders, or otherwise adversely affect the price of our common stock. Our governing documents:

- authorize a class of preferred stock that may be issued in series with terms, including voting rights, established by the board of directors without shareholder approval;
- authorize 10,000,000 shares of common stock and 10,000,000 shares of preferred stock that may be issued by the board of directors without shareholder approval;
- classify our board with staggered three year terms, preventing a change in a majority of the board at any annual meeting;
- require advance notice of proposed nominations for election to the board of directors and business to be conducted at a shareholder meeting;
- grant the board of directors the discretion, when considering whether a proposed merger or similar transaction is in the best interests of the Company and our shareholders, to take into account the effect of the transaction on the employees, clients and suppliers of the Company and upon the communities in which offices of the Company are located, to the extent permitted by South Carolina law;

- provide that the number of directors shall be fixed from time to time by resolution adopted by a majority of the directors then in office, but may not consist of fewer than five nor more than 25 members; and
- provide that no individual who is or becomes a "business competitor" or who is or becomes affiliated with, employed by, or a representative of any individual, corporation, or other entity which the board of directors, after having such matter formally brought to its attention, determines to be in competition with us or any of our subsidiaries (any such individual, corporation, or other entity being a "business competitor") shall be eligible to serve as a director if the board of directors determines that it would not be in our best interests for such individual to serve as a director (any financial institution having branches or affiliates within Greenville County, South Carolina is presumed to be a business competitor unless the board of directors determines otherwise).

In addition, the South Carolina business combinations statute provides that a 10% or greater shareholder of a resident domestic corporation cannot engage in a "business combination" (as defined in the statute) with such corporation for a period of two years following the date on which the 10% shareholder became such, unless the business combination or the acquisition of shares is approved by a majority of the disinterested members of such corporation's board of directors before the 10% shareholder's share acquisition date. This statute further provides that at no time (even after the two-year period subsequent to such share acquisition date) may the 10% shareholder engage in a business combination with the relevant corporation unless certain approvals of the board of directors or disinterested shareholders are obtained or unless the consideration given in the combination meets certain minimum standards set forth in the statute. The law is very broad in its scope and is designed to inhibit unfriendly acquisitions but it does not apply to corporations whose articles of incorporation contain a provision electing not to be covered by the law. Our articles of incorporation do not contain such a provision. An amendment of our articles of incorporation to that effect would, however, permit a business combination with an interested shareholder even though that status was obtained prior to the amendment.

Finally, the Change in Bank Control Act and the Bank Holding Company Act generally require filings and approvals prior to certain transactions that would result in a party acquiring control of the Company or the Bank.

Our common stock is not an insured deposit and is not guaranteed by the FDIC.

Shares of our common stock are not a bank deposit and, therefore, losses in value are not insured by the FDIC, any other deposit insurance fund or by any other public or private entity. Investment in shares of our common stock is inherently risky for the reasons described herein and our shareholders will bear the risk of loss if the value or market price of our common stock is adversely affected.

General Risk Factors

We may be subject to claims and litigation asserting lender liability.

From time to time, clients and others make claims and take legal action pertaining to our performance of fiduciary responsibilities. These claims are often referred to as “lender liability” claims and are sometimes brought in an effort to produce or increase leverage against us in workout negotiations or debt collection proceedings. Lender liability claims frequently assert one or more of the following allegations: breach of fiduciary duties, fraud, economic duress, breach of contract, breach of the implied covenant of good faith and fair dealing, and similar claims. Whether customer claims and legal action related to the performance of our responsibilities are founded or unfounded, if such claims and legal actions are not resolved in a favorable manner, they may result in significant financial liability and/or adversely affect our market reputation, products and services, as well as potentially affecting customer demand for those products and services. Any financial liability or reputation damage could have a material adverse effect on our business, which, in turn, could have a material adverse effect on our financial condition, results of operations and liquidity.

From time to time we are, or may become, involved in suits, legal proceedings, information-gatherings, investigations and proceedings by governmental and self-regulatory agencies that may lead to adverse consequences.

Many aspects of the banking business involve a substantial risk of legal liability. From time to time, we are, or may become, the subject of information-gathering requests, reviews, investigations and proceedings, and other forms of regulatory inquiry, including by bank regulatory agencies, self-regulatory agencies, the SEC and law enforcement authorities. The results of such proceedings could lead to significant civil or criminal penalties, including monetary penalties, damages, adverse judgements, settlements, fines, injunctions, restrictions on the way we conduct our business or reputational harm.

Item 1B. Unresolved Staff Comments.

None.

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Item 2. Properties.

Our principal executive offices and the Bank's main office is located at 100 Verdae Boulevard, Suite 100, Greenville, South Carolina 29607. In addition, we currently operate seven additional offices located in Greenville, Columbia and Charleston, South Carolina, one office in Raleigh, North Carolina, one office in Greensboro, North Carolina, and one office in Atlanta, Georgia. We recently received regulatory approval to open a retail office in Charlotte, North Carolina, as well. We lease six of our offices and own the remaining five locations. During the fourth quarter of 2020, we consolidated our three Columbia, South Carolina locations into one and subsequently sold the two remaining offices. In addition, the Company owns a piece of property in Greenville, South Carolina on which it is currently constructing a new bank headquarters. Management believes the terms of the various leases are consistent with market standards and were arrived at through arm's-length bargaining.

Item 3. Legal Proceedings.

In the ordinary course of operations, we may be a party to various legal proceedings from time to time. We do not believe that there is any pending or threatened proceeding against us, which, if determined adversely, would have a material effect on our business, results of operations, or financial condition.

Item 4. Mine Safety Disclosures.

None.

PART II

Item 5. Market for Common Equity, Related Shareholder Matters and Issuer Purchases of Equity Securities.

Market Information and Holders of Record

Our common stock is currently traded on the NASDAQ Global Market under the symbol “SFST.” We had approximately 2,600 shareholders of record on February 10, 2021.

Dividends

We have not declared or paid any cash dividends on our common stock since our inception. For the foreseeable future, we do not intend to declare cash dividends. We intend to retain earnings to grow our business and strengthen our capital base. Our ability to pay cash dividends depends primarily on the ability of our subsidiary, the Bank to pay dividends to us. As a South Carolina chartered bank, the Bank is subject to limitations on the amount of dividends that it is permitted to pay. Unless otherwise instructed by the S.C. Board, the Bank is generally permitted under South Carolina state banking regulations to pay cash dividends of up to 100% of net income in any calendar year without obtaining the prior approval of the S.C. Board. The FDIC also has the authority under federal law to enjoin a bank from engaging in what in its opinion constitutes an unsafe or unsound practice in conducting its business, including the payment of a dividend under certain circumstances.

Equity Compensation Plan Information

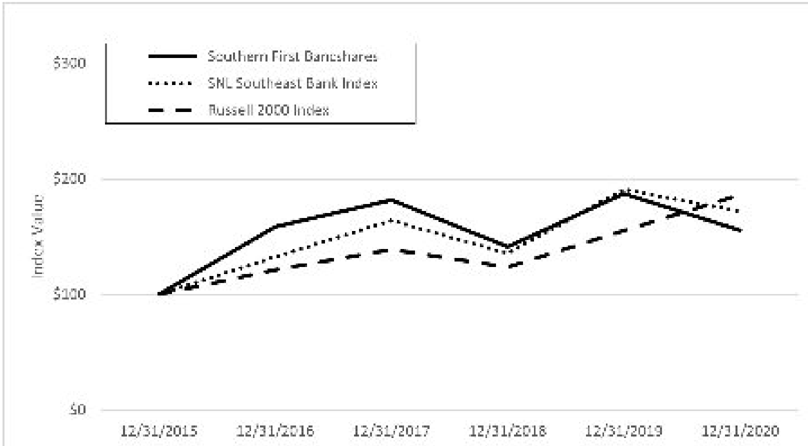
The following table sets forth equity compensation plan information at December 31, 2020. The number of shares and the exercise prices for options have been adjusted for the 10% stock dividends in 2006, 2011, 2012, and 2013.

Plan Category	Number of securities to be issued upon exercise of outstanding options, warrants and rights (a)	Weighted-average exercise price of outstanding options, warrants and rights (b)	Number of securities remaining available for future issuance under equity compensation plans (c) (excluding securities reflected in column(a))
Equity compensation plans approved by security holders			
2010 Stock Incentive Plan – options	226,585	$ 21.49	-
2016 Equity Incentive Plan – options	268,610	37.05	123,827
2016 Equity Incentive Plan – restricted stock	-	-	25,524
2020 Equity Incentive Plan	-	-	450,000
Total	495,195	$ 29.93	599,351

(1) Under the terms of the 2010 Plan no further incentive stock option awards may be granted, effective March 16, 2020; however, the Plan will remain in effect until all awards have been exercised or forfeited and we determine to terminate the Plan.

Stock Performance Graph

The performance graph below compares the Company's cumulative total return over the most recent five-year period with the SNL Southeast Bank Index, a banking industry performance index for the southeastern United States, and the Russell 2000 Index, a small-cap stock market index which the Company was added to in June 201z6. Returns are shown on a total return basis, assuming the reinvestment of dividends and a beginning stock index value of $100 per share.



	Period Ending					
	12/31/2015	12/31/2016	12/31/2017	12/31/2018	12/31/2019	12/31/2020
Southern First Bancshares	100.00	158.59	181.72	141.28	187.18	155.73
SNL Southeast Bank Index	100.00	132.75	164.21	135.67	191.06	172.07
Russell 2000 Index	100.00	121.31	139.08	123.76	155.35	186.36

On March 11, 2020, the Company announced a share repurchase plan allowing us to repurchase up to 383,650 shares of our common stock (the "Repurchase Plan"). As of December 31, 2020, we have not repurchased any of the shares authorized for repurchase under the Repurchase Plan. The Company is not obligated to purchase any such shares under the Repurchase Plan, and the Repurchase Plan may be discontinued, suspended or restarted at any time; however, repurchases under the Repurchase Plan after December 31, 2020 would require additional approval of our Board of Directors and the Federal Reserve.

The following table reflects share repurchase activity during the fourth quarter of 2020:

Period	(a) Total Number of Shares (or Units) Purchased	(b) Average Price Paid per Share (or Unit)	(c) Total Number of Shares (or Units) Purchased as Part of Publicly Announced Plans or Programs	(d) Maximum Number (or Approximate Dollar Value) of Shares (or Units) that May Yet Be Purchased Under the Plans or Programs
October 1 – October 31	-	$ -	-	383,650
November 1 – November 30	-	-	-	383,650
December 1 – December 31	-	-	-	383,650
Total	-		-	383,650

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Item 6. Selected Financial Data

The following table sets forth our selected historical consolidated financial information for the periods and as of the dates indicated. We derived our balance sheet and income statement data for the years ended December 31, 2020, 2019, 2018, 2017 and 2016 from our audited consolidated financial statements. You should read this information together with "Management's Discussion and Analysis of Financial Condition and Results of Operations" and our audited consolidated financial statements and the related notes thereto, which are included elsewhere in this Annual Report on Form 10-K.

					Years Ended December 31,
(dollars in thousands, except per share data)	2020	2019	2018	2017	2016
BALANCE SHEET DATA					
Total assets	$ 2,482,587	$ 2,267,195	$ 1,900,614	$ 1,624,625	$ 1,340,908
Investment securities	98,364	74,642	79,026	72,065	70,222
Loans (1)	2,142,867	1,943,525	1,677,332	1,387,070	1,163,644
Allowance for loan losses	44,149	16,642	15,762	15,523	14,855
Deposits	2,142,758	1,876,124	1,648,136	1,381,123	1,091,151
FHLB advances and other borrowings	25,000	110,000	50,000	67,200	115,200
Subordinated debentures	35,998	35,890	13,403	13,403	13,403
Common equity	228,294	205,860	173,916	149,686	109,872
Preferred stock	-	-	-	-	-
Shareholders' equity	228,294	205,860	173,916	149,686	109,872
SELECTED RESULTS OF OPERATIONS DATA					
Interest income	$ 94,818	$ 92,652	$ 76,657	$ 61,209	$ 51,191
Interest expense	15,008	25,383	16,505	10,333	8,192
Net interest income	79,810	67,269	60,152	50,876	42,999
Provision for loan losses	29,600	2,300	1,900	2,000	2,300
Net interest income after provision for loan losses	50,210	64,969	58,252	48,876	40,699
Noninterest income	27,353	14,983	10,201	9,337	10,846
Noninterest expenses	53,744	44,473	39,763	34,552	31,176
Income before income tax expense	23,819	35,479	28,690	23,661	20,369
Income tax expense	5,491	7,621	6,401	10,616	7,333
Net income	18,328	27,858	22,289	13,045	13,036
Preferred stock dividends	-	-	-	-	-
Net income available to common shareholders	$ 18,328	$ 27,858	$ 22,289	$ 13,045	$ 13,036
PER COMMON SHARE DATA					
Basic	$ 2.37	$ 3.70	$ 3.02	$ 1.86	$ 2.06
Diluted	2.34	3.58	2.88	1.76	1.94
Book value	29.37	26.83	23.29	20.37	17.00
Weighted average number of common shares outstanding:					
Basic, in thousands	7,719	7,528	7,384	7,006	6,318
Diluted, in thousands	7,824	7,773	7,737	7,393	6,721
SELECTED FINANCIAL RATIOS					
Performance Ratios:					
Return on average assets	0.76%	1.35%	1.27%	0.87%	1.04%
Return on average equity	8.49%	14.72%	13.83%	9.66%	12.73%
Return on average common equity	8.49%	14.72%	13.83%	9.66%	12.73%
Net interest margin, tax equivalent(2)	3.55%	3.43%	3.58%	3.57%	3.63%
Efficiency ratio (3)	50.15%	54.07%	56.52%	57.38%	57.90%
Asset Quality Ratios:					
Nonperforming assets to total loans (1)	0.43%	0.35%	0.35%	0.54%	0.53%
Nonperforming assets to total assets	0.37%	0.30%	0.31%	0.46%	0.46%
Net charge-offs to average total loans	0.10%	0.08%	0.11%	0.10%	0.10%
Allowance for loan losses to nonperforming loans	547.14%	244.95%	270.36%	212.60%	270.95%
Allowance for loan losses to total loans	2.06%	0.86%	0.94%	1.12%	1.28%
Holding Company Capital Ratios:					
Total risk-based capital ratio	14.38%	13.73%	12.49%	13.27%	12.11%
Tier 1 risk-based capital ratio	11.97%	11.63%	11.53%	12.11%	10.86%
Leverage ratio	9.70%	10.10%	10.14%	10.26%	9.42%
Common equity tier 1 ratio(4)	11.32%	10.94%	10.73%	11.15%	9.71%
Tangible common equity(5)	9.20%	9.08%	9.15%	9.21%	8.19%
Growth Ratios:					
Change in assets	9.50%	19.29%	16.99%	21.16%	10.15%
Change in loans	10.26%	15.87%	20.93%	19.20%	15.79%
Change in deposits	14.21%	13.83%	19.33%	26.57%	10.69%
Change in net income to common shareholders	-34.21%	24.99%	70.86%	0.07%	28.22%
Change in earnings per common share - diluted	-34.64%	24.31%	63.64%	-9.28%	25.16%

Footnotes to table:
(1) Excludes loans held for sale.
(2) The tax-equivalent adjustment to net interest income adjusts the yield for assets earning tax-exempt income to a comparable yield on a taxable basis.
(3) Noninterest expense divided by the sum of net interest income and noninterest income.
(4) The common equity tier 1 ratio is calculated as the sum of common equity divided by risk-weighted assets.
(5) The common equity ratio is calculated as total equity less preferred stock divided by total assets.

Item 7. Management’s Discussion and Analysis of Financial Condition and Results of Operations

The following discussion and analysis identifies significant factors that have affected our financial position and operating results during the periods included in the accompanying financial statements. We encourage you to read this discussion and analysis in conjunction with the financial statements and the related notes and the other statistical information also included in this Annual Report on Form 10-K.

OVERVIEW

Our business model continues to be client-focused, utilizing relationship teams to provide our clients with a specific banker contact and support team responsible for all of their banking needs. The purpose of this structure is to provide a consistent and superior level of professional service, and we believe it provides us with a distinct competitive advantage. We consider exceptional client service to be a critical part of our culture, which we refer to as "ClientFIRST."

At December 31, 2020, we had total assets of $2.48 billion, a 9.5% increase from total assets of $2.27 billion at December 31, 2019. The largest components of our total assets are loans which were $2.14 billion and $1.94 billion at December 31, 2020 and 2019, respectively. Our liabilities and shareholders’ equity at December 31, 2020 totaled $2.25 billion and $228.3 million, respectively, compared to liabilities of $2.06 billion and shareholders’ equity of $205.9 million at December 31, 2019. The principal component of our liabilities is deposits which were $2.14 billion and $1.88 billion at December 31, 2020 and 2019, respectively.

Like most community banks, we derive the majority of our income from interest received on our loans and investments. Our primary source of funds for making these loans and investments is our deposits, on which we pay interest. Consequently, one of the key measures of our success is our amount of net interest income, or the difference between the income on our interest-earning assets, such as loans and investments, and the expense on our interest-bearing liabilities, such as deposits and borrowings. Another key measure is the difference between the yield we earn on these interest-earning assets and the rate we pay on our interest-bearing liabilities, which is called our net interest spread. In addition to earning interest on our loans and investments, we earn income through fees and other charges to our clients.

Our net income available to common shareholders for the years ended December 31, 2020 and 2019 was $18.3 million and $27.9 million, or diluted earnings per share (“EPS”) of $2.34 and $3.58 for the years ended December 31, 2020 and 2019, respectively. The decrease in net income resulted primarily from increases in our provision for loan loss and noninterest expense, partially offset by an increase in net interest income and noninterest income. In addition, our net income available to shareholders was $22.3 million, or EPS of $2.88 for the year ended December 31, 2018.

COVID-19 PANDEMIC

The COVID-19 pandemic continues to create extensive disruptions to the global economy and financial markets and to businesses and the lives of individuals throughout the world. In particular, the COVID-19 pandemic has severely restricted the level of economic activity in our markets. Federal and state governments have taken, and may continue to take, unprecedented actions to contain the spread of the disease, including quarantines, travel bans, shelter-in-place orders, closures of businesses and schools, fiscal stimulus, and legislation designed to deliver monetary aid and other relief to businesses and individuals impacted by the pandemic. Although in various locations certain activity restrictions have been relaxed and businesses and schools have reopened with some level of success, in many states and localities the number of individuals diagnosed with COVID-19 has increased significantly, which may cause a freezing or, in certain cases, a reversal of previously announced relaxation of activity restrictions and may prompt the need for additional aid and other forms of relief.

The impact of the COVID-19 pandemic is fluid and continues to evolve, adversely affecting many of the Bank's clients. The unprecedented and rapid spread of COVID-19 and its associated impacts on trade (including supply chains and export levels), travel, employee productivity, unemployment, consumer spending, and other economic activities has resulted in less economic activity, lower equity market valuations and significant volatility and disruption in financial markets. In addition, due to the COVID-19 pandemic, market interest rates have declined significantly, with the 10-year Treasury bond falling below 1.00% on March 3, 2020, for the first time, although bond yields have recently begun to rise, nearing where they were before the pandemic in February 2020. In March 2020, the Federal Open Market Committee reduced the targeted federal funds interest rate range to 0% to 0.25%. These reductions in interest rates and the other effects of the COVID-19 pandemic have had, and are expected to continue to have, possibly materially, an adverse effect on our business, financial condition and results of operations. For instance, the pandemic has had negative effects on the Bank's interest income, provision for loan losses, and certain transaction-based line items of noninterest income. The ultimate extent of the impact of the COVID-19 pandemic on our business, financial condition and results of operations is currently uncertain and will depend on various developments and other factors, including, the effect of governmental and private sector initiatives, the effect of the recent rollout of vaccinations for the virus, whether such vaccinations will be effective against any resurgence of the virus, including any new strains, and the ability for customers and businesses to return to their pre-pandemic routine.

Our business, financial condition and results of operations generally rely upon the ability of our borrowers to repay their loans, the value of collateral underlying our secured loans, and demand for loans and other products and services we offer, which are highly dependent on the business environment in our primary markets where we operate and in the United States as a whole.

As we progress through the pandemic, the majority of our team has returned to working in the office at this time; however, we maintain the ability to shift to working remotely as needed. Our offices continue to operate in a drive-thru only mode with "in-person" client meetings available by appointment to maintain the safety of our team and our clients. We believe this strategy, combined with our digital technology, has been extremely effective in serving our clients, and allowed us to consolidate our three Columbia, South Carolina offices into one location. The sale of our two Columbia office buildings was completed on October 9, 2020.

We are focused on servicing the financial needs of our commercial and consumer clients and have offered flexible loan payment arrangements, including short-term loan modifications or forbearance payments, and reduced or waived certain fees on deposit accounts. We continue to assist clients with these accommodations on a case by case basis. Future governmental actions may require these and other types of client-related responses. In response to the Paycheck Protection Program ("PPP"), established under the Coronavirus Aid, Relief, and Economic Security Act, or CARES Act, we became a small business administration approved lender in an effort to assist our clients through this challenging time. In 2020, we processed 853 loans under the PPP for a total of $97.5 million, receiving lender fee income of $3.9 million. As the regulations and guidance for PPP loans and the forgiveness process continued to change and evolve, management recognized the operational risk and complexity associated with this portfolio and decided to pursue the sale of the PPP loan portfolio to a third party better suited to support and serve our PPP clients through the loan forgiveness process. We believe this loan sale allowed our team to focus on serving our clients and proactively monitoring and addressing credit risk brought on by the pandemic. On June 26, 2020, we completed the sale of our PPP loan portfolio to The Loan Source Inc., together with its servicing partner, ACAP SME LLC, and immediately recognized SBA lender fee income of $2.2 million, net of sale and processing costs, which is included in other noninterest income in the consolidated financial statements.

Through December 31, 2020, we had granted deferrals on loan payments for 864 loans, with aggregate outstanding loan principal balances of approximately $599.6 million as of December 31, 2020, of which 91% were commercial loans. As of December 31, 2020, 98% of these loans have reached the end of their deferral period and have begun to resume normal payments.

The table below provides a breakdown of loan modification requests due to the COVID-19 pandemic by type of concession. At December 31, 2020, there were two modified loan totaling $13.5 million with a remaining deferral period.

				December 31, 2020
(dollars in thousands)	**# Loans**		**Amount**	**% of Total Portfolio**
Payment deferrals	590	$	452,897	21.1%
Interest only	265		143,596	6.7%
Financial difficulty (TDR)	9		3,154	0.1%
	864	$	599,647	27.9%

In accordance with the CARES Act, the Company implemented loan modification programs in response to the COVID-19 pandemic and the Company elected the accounting policy in the CARES Act to not apply TDR accounting to loans modified for borrowers impacted by the COVID-19 pandemic. The Company granted short-term loan deferrals to six client relationships, with loans totaling $3.2 million at December 31, 2020, which were considered TDRs due to the client experiencing financial difficulty before the pandemic. In certain cases, we have made a second three-month deferral to our clients based on individual circumstances for the borrower.

As we closely monitor credit risk and our exposure to increased loan losses resulting from the impact of COVID-19 on our commercial clients, we have identified two industries considered to be at higher risk for credit loss. The table below identifies the outstanding and committed loan balances for each of these industries. Of the $61.5 million of loans modified in these industries as of December 31, 2020, 78% have begun to resume normal payments.

	December 31, 2020								
(dollars in thousands)	# Loans	Balance Outstanding	% of Total Loans Outstanding	Total Modified Balance	% Modified	Deferral Complete	% Deferral Complete	% Past Due 30 Days or More	% on Nonaccrual
Hotels	23	$ 110,138	5.1%	$ 56,161	51.0%	$ 42,679	76.0%	-%	-%
Restaurants	57	13,315	0.6%	5,291	39.7%	5,291	100.0%	-%	-%
Total	80	$ 123,453	5.7%	$ 61,452	49.8%	$ 47,969	78.1%	-%	-%

We continue to monitor unfunded commitments through the pandemic, including home equity lines of credit, for evidence of increased credit exposure as borrowers utilize these lines for liquidity purposes.

We are also monitoring the impact of the COVID-19 pandemic on the operations and value of our investments. We mark to market our publicly traded investments and review our investment portfolio for impairment at each period end. Because of changing economic and market conditions affecting issuers, we may be required to recognize further impairments on the securities we hold as well as reductions in other comprehensive income. We cannot currently determine the ultimate impact of the pandemic on the long-term value of our investment portfolio.

We believe there could be potential stresses on liquidity management as a result of the COVID-19 pandemic. For instance, as clients manage their own liquidity stress, we could experience an increase in the utilization of existing lines of credit.

As of December 31, 2020, all of our capital ratios, and the Bank's capital ratios, were in excess of all regulatory requirements. While we believe that we have sufficient capital to withstand an extended economic recession brought about by the COVID-19 pandemic, our reported and regulatory capital ratios could be adversely impacted by further credit losses. We maintain access to multiple sources of liquidity, including a $15.0 million holding company line of credit with another bank which could be used to support capital ratios at the Bank.

CRITICAL ACCOUNTING POLICIES AND ESTIMATES

We have adopted various accounting policies that govern the application of accounting principles generally accepted in the U.S. and with general practices within the banking industry in the preparation of our financial statements. Our significant accounting policies are described in Note 1 to our Consolidated Financial Statements as of December 31, 2020.

Certain accounting policies inherently involve a greater reliance on the use of estimates, assumptions and judgments and, as such, have a greater possibility of producing results that could be materially different than originally reported, which could have a material impact on the carrying values of our assets and liabilities and our results of operations. We consider these accounting policies and estimates to be critical accounting policies. We have identified the determination of the allowance for loan losses, the fair valuation of financial instruments and income taxes to be the accounting areas that require the most subjective or complex judgments and, as such, could be most subject to revision as new or additional information becomes available or circumstances change, including overall changes in the economic climate and/or market interest rates. Therefore, management has reviewed and approved these critical accounting policies and estimates and has discussed these policies with the Company's Audit Committee.

Allowance for Loan Losses

The allowance for loan loss is management's estimate of credit losses inherent in the loan portfolio. 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 uncollectibility of a loan balance is confirmed. Subsequent recoveries, if any, are credited to the allowance. The allowance for loan losses is evaluated on a regular basis by management and is based upon management's periodic review of the collectability of the loans in light of historical experience, the nature and volume of the loan portfolio, adverse situations that may affect the borrower's ability to repay, estimated value of any underlying collateral and prevailing economic conditions. This evaluation is inherently subjective as it requires estimates that are susceptible to significant revision as more information becomes available.

We have an established process to determine the adequacy of the allowance for loan losses that assesses the losses inherent in our portfolio. While we attribute portions of the allowance to specific portfolio segments, the entire allowance is available to absorb credit losses inherent in the total loan portfolio. Our process involves procedures to appropriately consider the unique risk characteristics of our commercial and consumer loan portfolio segments. For each portfolio segment, impairment is measured individually for each impaired loan. Our allowance levels are influenced by loan volume, loan grade or delinquency status, historic loss experience and other economic conditions.

The allowance consists of general and specific components.

Commercial loans are assessed for estimated losses by grading each loan using various risk factors identified through periodic reviews. We apply historic grade-specific loss factors to each loan class. In the development of our statistically derived loan grade loss factors, we observe historical losses over 20 quarters for each loan grade. These loss estimates are adjusted as appropriate based on additional analysis of external loss data or other risks identified from current economic conditions and credit quality trends. For consumer loans, we determine the allowance on a collective basis utilizing historical losses over 20 quarters to represent our best estimate of inherent loss. We pool loans, generally by loan class with similar risk characteristics.

Included in the general component of the allowance for loan losses for both portfolio segments is a margin of imprecision inherent in the underlying assumptions used in the methodologies for estimating general losses in the portfolio. Uncertainties and subjective issues such as changes in the lending policies and procedures, changes in the local/national economy, changes in volume or type of credits, changes in volume/severity or problem loans, quality of loan review and board of director oversight, concentrations of credit, and peer group comparisons are qualitative and environmental factors considered.

The specific component relates to loans that are classified as impaired. For loans that are classified as impaired, an allowance is established when the value of the impaired loan is lower than the carrying value of that loan. A loan is considered impaired when, based on current information and events, it is probable that the Company will be unable to collect the scheduled payments of principal or interest when due according to the contractual terms of the loan agreement. Factors considered by management in determining impairment include payment status, collateral value, and the probability of collecting scheduled principal and interest payments when due. Impairment is measured on a loan by loan basis for commercial and consumer loans by either the present value of expected future cash flows discounted at the loan’s effective interest rate, the loan’s obtainable market price, or the fair value of the collateral if the loan is collateral dependent. The specific component also includes an amount for the estimated impairment on commercial and consumer loans modified in a troubled debt restructuring (“TDR”), whether on accrual or nonaccrual status.

While management uses available information to recognize losses on loans, future additions to the allowance may be necessary based on changes in local economic conditions. In addition, regulatory agencies, as an integral part of their examination process, periodically review our allowance for loan losses. Such agencies may require us to recognize additions to the allowances based on their judgments about information available to them at the time of their examination.

Fair Valuation of Financial Instruments

We use fair value measurements to record fair value adjustments to certain financial instruments and to determine fair value disclosures. Additionally, we may be required to record other assets at fair value on a nonrecurring basis. These nonrecurring fair value adjustments typically involve application of lower-of-cost-or-market accounting or write-downs of individual assets. Further, we include in the Notes to the Consolidated Financial Statements information about the extent to which fair value is used to measure assets and liabilities, the valuation methodologies used, and the related impact to income. Additionally, for financial instruments not recorded at fair value, we disclose the estimate of their fair value.

Fair value is defined as the exchange price that would be received to sell an asset or paid to transfer the liability in an orderly transaction between market participants at the measurement date. Accounting standards establish a three-level hierarchy for disclosure of assets and liabilities recorded at fair value. The classification of assets and liabilities within the hierarchy is based on whether the inputs to the valuation methodology used for measurement are observable or unobservable. Observable inputs reflect market-derived or market-based information obtained from independent sources, while unobservable inputs reflect our estimates about market data. The three levels of inputs that are used to classify fair value measurements are as follows:

- Level 1 — Valuation is based upon quoted prices for identical instruments traded in active markets. Level 1 instruments generally include securities traded on active exchange markets, such as the New York Stock Exchange, as well as securities that are traded by dealers or brokers in active over-the-counter markets. Instruments we classify as Level 1 are instruments that have been priced directly from dealer trading desks and represent actual prices at which such securities have traded within active markets.
- Level 2 — Valuation is based upon quoted prices for similar instruments in active markets, quoted prices for identical or similar instruments in markets that are not active, and model-based valuation techniques, such as matrix pricing, for which all significant assumptions are observable in the market. Instruments we classify as Level 2 include securities that are valued based on pricing models that use relevant observable information generated by transactions that have occurred in the market place that involve similar securities.
- Level 3 — Valuation is generated from model-based techniques that use significant assumptions not observable in the market. These unobservable assumptions reflect the Company’s estimates of assumptions market participants would use in pricing the asset or liability. Valuation techniques include use of option pricing models, discounted cash flow models, and similar techniques.

We attempt to maximize the use of observable inputs and minimize the use of unobservable inputs when developing fair value measurements. When available, we use quoted market prices to measure fair value. Specifically, we use independent pricing services to obtain fair values based on quoted prices. Quoted prices are subject to our internal price verification procedures. If market prices are not available, fair value measurement is based upon models that use primarily market-based or independently-sourced market parameters. Most of our financial instruments use either of the foregoing methodologies, collectively Level 1 and Level 2 measurements, to determine fair value adjustments recorded to our financial statements. However, in certain cases, when market observable inputs for model-based valuation techniques may not be readily available, we are required to make judgments about assumptions market participants would use in estimating the fair value of the financial instrument.

The degree of management judgment involved in determining the fair value of an instrument is dependent upon the availability of quoted market prices or observable market parameters. For instruments that trade actively and have quoted market prices or observable market parameters, there is minimal subjectivity involved in measuring fair value. When observable market prices and parameters are not fully available, management’s judgment is necessary to estimate fair value. In addition, changes in market conditions may reduce the availability of quoted prices or observable data. For example, reduced liquidity in the capital markets or changes in secondary market activities could result in observable market inputs becoming unavailable. When significant adjustments are required to available observable inputs, it may be appropriate to utilize an estimate based primarily on unobservable inputs. When an active market for a security does not exist, the use of management estimates that incorporate current market participant expectations of future cash flows, and include appropriate risk premiums, is acceptable.

Significant judgment may be required to determine whether certain assets measured at fair value are included in Level 2 or Level 3. If fair value measurement is based upon recent observable market activity of such assets or comparable assets (other than forced or distressed transactions) that occur in sufficient volume and do not require significant adjustment using unobservable inputs, those assets are classified as Level 2. If not, they are classified as Level 3. Making this assessment requires significant judgment.

Income Taxes

The financial statements have been prepared on the accrual basis. When income and expenses are recognized in different periods for financial reporting purposes versus for the purposes of computing income taxes currently payable, deferred taxes are provided on such temporary differences. Deferred tax assets and liabilities are recognized for the expected future tax consequences of events that have been recognized in the consolidated financial statements or tax returns. Deferred tax assets and liabilities are measured using the enacted tax rates expected to apply to taxable income in the years in which those temporary differences are expected to be realized or settled. The Company believes that its income tax filing positions taken or expected to be taken on its tax returns will more likely than not be sustained upon audit by the taxing authorities and does not anticipate any adjustments that will result in a material adverse impact on the Company's financial condition, results of operations, or cash flow. Therefore, no reserves for uncertain income tax positions have been recorded.

RESULTS OF OPERATIONS

Net Interest Income and Margin

Our level of net interest income is determined by the level of earning assets and the management of our net interest margin. For the years ended December 31, 2020, 2019, and 2018, our net interest income was $79.8 million, $67.3 million, and $60.2 million, respectively. The $12.5 million, or 18.6%, increase in net interest income during 2020, compared to 2019, was driven by a $328.1 million increase in average earning assets, partially offset by a $152.2 million increase in our average interest-bearing liabilities. The increase in average earning assets was primarily related to an increase in average loans, while the increase in average interest-bearing liabilities was primarily driven by an increase in interest-bearing deposits. During 2019, our net interest income increased $7.1 million, or 11.8%, compared to 2018, while average interest-earning assets increased $281.1 million and average interest-bearing liabilities increased $190.4 million.

Interest income for the years ended December 31, 2020, 2019, and 2018 was $94.8 million, $92.7 million, and $76.7 million, respectively. A significant portion of our interest income relates to our strategy to maintain a large portion of our assets in higher earning loans compared to lower yielding investments and federal funds sold. As such, 98.2% of our interest income related to interest on loans during 2020, compared to 96.0% during 2019 and 96.2% during 2018. Also, included in interest income on loans was $1.4 million, $1.2 million and $1.1 million related to the net amortization of loan fees and capitalized loan origination costs for the years ended December 31, 2020, 2019 and 2018, respectively.

Interest expense was $15.0 million, $25.4 million, and $16.5 million for the years ended December 31, 2020, 2019, and 2018, respectively. Interest expense on deposits for 2020 represented 87.0% of total interest expense, compared to 93.5% for 2019, and 89.9% for 2018, while interest expense on borrowings represented 13.0% of total interest expense for 2020, compared to 6.5% for 2019, and 10.1% for 2018. The decrease in interest expense on deposits during 2020 resulted from a decrease in deposit rates.

We have included a number of tables to assist in our description of various measures of our financial performance. For example, the “Average Balances, Income and Expenses, Yields and Rates” table shows the average balance of each category of our assets and liabilities as well as the yield we earned or the rate we paid with respect to each category during 2020, 2019, and 2018. Similarly, the “Rate/Volume Analysis” table demonstrates the effect of changing interest rates and changing volume of assets and liabilities on our financial condition during the periods shown. We also track the sensitivity of our various categories of assets and liabilities to changes in interest rates, and we have included tables to illustrate our interest rate sensitivity with respect to interest-earning and interest-bearing accounts.

The following table sets forth information related to our average balance sheet, average yields on assets, and average costs of liabilities at December 31, 2020, 2019 and 2018. We derived these yields or costs by dividing income or expense by the average balance of the corresponding assets or liabilities. We derived average balances from the daily balances throughout the periods indicated. During the same periods, we had no securities purchased with agreements to resell. All investments were owned at an original maturity of over one year. Nonaccrual loans are included in earning assets in the following tables. Loan yields have been reduced to reflect the negative impact on our earnings of loans on nonaccrual status. The net of capitalized loan costs and fees are amortized into interest income on loans.

Average Balances, Income and Expenses, Yields and Rates

	For the Year Ended December 31,								
			2020			2019			2018
(dollars in thousands)	Average Balance	Income/ Expense	Yield/ Rate	Average Balance	Income/ Expense	Yield/ Rate	Average Balance	Income/ Expense	Yield/ Rate
Interest-earning assets									
Federal funds sold and interest-bearing deposits with banks	$ 105,344	$ 270	0.26%	$ 71,797	$ 1,622	2.26%	$ 61,811	$ 1,138	1.84%
Investment securities, taxable	74,517	1,253	1.68%	72,137	1,961	2.72%	64,426	1,623	2.52%
Investment securities, nontaxable (1)	6,262	210	3.36%	7,376	182	2.46%	5,886	231	3.93%
Loans (2)	2,106,569	93,133	4.42%	1,813,259	88,929	4.90%	1,551,354	73,718	4.75%
Total earning assets	2,292,692	94,866	4.14%	1,964,569	92,694	4.72%	1,683,477	76,710	4.56%
Nonearning assets	103,212			101,647			77,127		
Total assets	$2,395,904			$2,066,216			$1,760,604		
Interest-bearing liabilities									
NOW accounts	$ 255,514	352	0.14%	$ 205,513	555	0.27%	$ 235,623	401	0.17%
Savings & money market	1,003,339	7,513	0.75%	864,708	15,086	1.74%	669,306	8,766	1.31%
Time deposits	301,078	5,190	1.72%	363,431	8,089	2.23%	332,201	5,669	1.71%
Total interest-bearing deposits	1,559,931	13,055	0.84%	1,433,652	23,730	1.66%	1,237,130	14,836	1.20%
FHLB advances and other borrowings	30,990	338	1.09%	21,914	736	3.36%	33,781	1,089	3.22%
Subordinated debt	35,940	1,615	4.49%	19,133	917	4.79%	13,403	580	4.33%
Total interest-bearing liabilities	1,626,861	15,008	0.92%	1,474,699	25,383	1.72%	1,284,314	16,505	1.29%
Noninterest-bearing liabilities	553,098			402,216			315,118		
Shareholders' equity	215,945			189,301			161,172		
Total liabilities and shareholders' equity	$2,395,904			$2,066,216			$1,760,604		
Net interest spread			3.22%			3.00%			3.27%
Net interest income(tax equivalent)/margin		$ 79,858	3.48%		$ 67,311	3.43%		$ 60,205	3.58%
Less: tax-equivalent adjustment (1)		(48)			(42)			(53)	
Net interest income		$ 79,810			$ 67,269			$ 60,152	

(1) The tax-equivalent adjustment to net interest income adjusts the yield for assets earning tax-exempt income to a comparable yield on a taxable basis.
(2) Includes loans held for sale.

Our net interest margin, on a tax-equivalent basis (TE), was 3.48%, 3.43% and 3.58% for the years ended December 31, 2020, 2019 and 2018, respectively. Our net interest margin (TE) increased five basis points in 2020, compared to 2019, as the cost of our interest-bearing liabilities decreased quicker than the yield on our interest-earning assets due to our deposits repricing more frequently to market prices than our loan yields. During 2019, our net interest margin decreased 15 basis points, compared to 2018, as the cost of our interest-bearing liabilities increased by 43 basis points, while the yield on our interest-earning assets increased by 16 basis points.

Our average interest-earning assets increased by $328.1 million during the year ended December 31, 2020, compared to 2019, while the related yield on our interest-earning assets decreased by 58 basis points. The increase in average interest-earning assets was driven primarily by a $293.3 million increase in average loan balances combined with a $33.5 million increase in federal funds sold and interest-bearing deposits with banks. In addition, the reduction in yield on our interest earning assets was driven by a 48 basis point decrease in loan yield as the Federal Reserve reduced interest rates by 225 basis points since August 2019. During the year ended December 31, 2019, our average interest-earning assets increased by $281.1 million, compared to 2018, while the yield on our interest-earning assets increased by 16 basis points. The increase in average interest-earning assets was driven primarily by a $261.9 million increase in average loan balances during 2019, compared to 2018. In addition, our loan yield increased 15 basis points during 2019.

Our average interest-bearing liabilities increased by $152.2 million during 2020 while the cost of our interest-bearing liabilities decreased by 80 basis points. The increase in average interest-bearing liabilities was driven primarily by a $126.3 million increase in average interest-bearing deposits at an average rate of 0.84%, an 82 basis point decrease when compared to 2019. During 2019, our average interest-bearing liabilities increased by $190.4 million, compared to 2018, while the cost of our interest-bearing liabilities increased by 43 basis points.

Our net interest spread was 3.22% for the year ended December 31, 2020, compared to 3.00% for the same period in 2019 and 3.27% for 2018. The net interest spread is the difference between the yield we earn on our interest-earning assets and the rate we pay on our interest-bearing liabilities. The 80 basis point decrease in the cost of our interest-bearing liabilities partially offset by a 58 basis point decrease in yield on our interest-earning assets resulted in a 22 basis point increase in our net interest spread for the 2020 period. We anticipate pressure on our net interest spread and net interest margin in future periods as our loan yield continues to decline due to new and renewed loans pricing at rates lower than our current portfolio rate.

Rate/Volume Analysis

Net interest income can be analyzed in terms of the impact of changing interest rates and changing volume. The following tables set forth the effect which the varying levels of interest-earning assets and interest-bearing liabilities and the applicable rates have had on changes in net interest income for the periods presented.

								Years Ended
	December 31, 2020 vs. 2019 Increase (Decrease) Due to Change in				December 31, 2019 vs. 2018 Increase (Decrease) Due to Change in			
(dollars in thousands)	Volume	Rate	Rate/ Volume	Total	Volume	Rate	Rate/ Volume	Total
Interest income								
Loans	$ 14,385	(8,763)	(1,418)	4,204	12,445	2,366	400	15,211
Investment securities	33	(708)	(11)	(686)	236	57	7	300
Federal funds sold	758	(1,438)	(672)	(1,352)	184	258	42	484
Total interest income	15,176	(10,909)	(2,101)	2,166	12,865	2,681	449	15,995
Interest expense								
Deposits	2,088	(11,731)	(1,032)	(10,675)	2,355	5,643	896	8,894
FHLB advances and other borrowings	305	(497)	(206)	(398)	(383)	46	(16)	(353)
Subordinated debt	805	(57)	(50)	698	248	62	27	337
Total interest expense	3,198	(12,285)	(1,288)	(10,375)	2,220	5,751	907	8,878
Net interest income	$ 11,978	1,376	(813)	12,541	10,645	(3,070)	(458)	7,117

Net interest income, the largest component of our income, was $79.8 million for the year ended December 31, 2020, a $12.5 million increase from net interest income of $67.3 million for the year ended December 31, 2019. The increase in net interest income was driven by a $10.4 million decrease in interest expense and a $2.2 million increase in interest income. Reduced rates on our interest-bearing liabilities was the primary driver of the decrease in interest expense which was partially offset by a $152.2 million increase in the average balance of those liabilities. Interest income increased $2.2 million driven by an increase in average loan balances that was partially offset by a decrease in yield across all interest earning assets.

During 2019, our average interest-earning assets increased $281.1 million as compared to 2018, resulting in $12.9 million of additional interest income while higher rates on our interest-earning assets also increased interest income by $2.7 million from the prior year. In addition, our average interest-bearing liabilities increased by $190.4 million during 2019 resulting in $2.2 million of additional interest expense. In addition, higher rates on our interest-bearing deposits, subordinated debt, and FHLB advances and other borrowings resulted in an increase of $5.8 million of additional interest expense from the prior year.

Provision for Loan Losses

We have established an allowance for loan losses through a provision for loan losses charged as an expense on our statements of income. We review our loan portfolio periodically to evaluate our outstanding loans and to measure both the performance of the portfolio and the adequacy of the allowance for loan losses. Please see the discussion below under “Results of Operations – Allowance for Loan Losses” for a description of the factors we consider in determining the amount of the provision we expense each period to maintain this allowance.

Following is a summary of the activity in the allowance for loan losses.

			December 31,
(dollars in thousands)	2020	2019	2018
Balance, beginning of period	$ 16,642	15,762	15,523
Provision	29,600	2,300	1,900
Loan charge-offs	(3,414)	(1,515)	(2,146)
Loan recoveries	1,321	95	485
Net loan charge-offs	(2,093)	(1,420)	(1,661)
Balance, end of period	$ 44,149	16,642	15,762

For the year ended December 31, 2020, we incurred a noncash expense related to the provision for loan losses of $29.6 million, bringing the allowance for loan losses to $44.1 million, or 2.06% of gross loans. In comparison, we added $2.3 million and $1.9 million to the provision for loan losses during the years ended December 31, 2019 and 2018, respectively, resulting in an allowance for loan losses of $16.6 million, or 0.86% of gross loans, as of December 31, 2019, and an allowance for loan losses of $15.8 million, or 0.94% of gross loans, as of December 31, 2018. The increased provision during 2020 was driven by an increase to our qualitative environmental factors related to the uncertain economic and business conditions at both the national and regional levels at December 31, 2020. Factors such as the continued impact on the tourism and hospitality industries due to the pandemic, an increase in permanent job losses and unemployment rates as well as uncertainty in the political realm have driven this increase. We expect economic uncertainty to continue for at least the next few quarters which may result in a continued increase to the allowance for loan losses during 2021, however, should economic conditions improve, we could determine that the qualitative environmental factors indicate that a release of our provision is appropriate, similar to recent determinations made by a number of other insured depository institutions.

During the year ended December 31, 2020, our net charge-offs were $2.1 million, representing 0.10% of average loans, and consisted of $3.4 million in loans charged-off, partially offset by $1.3 million of recoveries on loans previously charged-off. In addition, nonperforming assets increased to 0.37% of total assets while our level of classified assets increased to 8.3% at December 31, 2020.

We reported net charge-offs of $1.4 million and $1.7 million for the years ended December 31, 2019 and 2018, respectively, including recoveries of $95,000 and $485,000 in 2019 and 2018, respectively. The net charge-offs of $1.4 million and $1.7 million during 2019 and 2018, respectively, represented 0.08% and 0.11% of the average outstanding loan portfolios for 2019 and 2018, respectively.

Noninterest Income

The following table sets forth information related to our noninterest income.

		Year ended December 31,	
(dollars in thousands)	2020	2019	2018
Mortgage banking income	$ 19,785	9,923	5,544
Service fees on deposit accounts	860	1,061	1,040
ATM and debit card income	1,741	1,728	1,490
Income from bank owned life insurance	1,091	1,001	878
Gain on sale of investment securities	3	727	7
Loss on extinguishment of debt	(37)	(1,496)	-
Net lender fees on PPP loan sale	2,247	-	-
Other income	1,663	2,039	1,242
Total noninterest income	$ 27,353	14,983	10,201

Noninterest income was $27.4 million for the year ended December 31, 2020, a $12.4 million, or 82.6%, increase compared to noninterest income of $15.0 million for the year ended December 31, 2019. The increase in noninterest income during 2020, compared to 2019, resulted primarily from the following:

- Mortgage banking income increased $9.9 million, or 99.4%, driven by higher mortgage origination volume during 2020 due to the favorable interest rate environment for mortgage loans.
- Loss on extinguishment of debt decreased as a result of fewer prepayment penalties related to the paydown of FHLB Advances. More detail on these transactions is included in the 2019 discussion below.
- Net lender fees on PPP loan sale totaled $2.2 million and related to the net fee income on the PPP loans we originated and then sold to a third party during the second quarter of 2020.

Offsetting these increases were decreases in service fees on deposit accounts and other income. The decrease in service fees on deposit accounts is directly related to the impact of COVID-19 as we have waived certain fees in an effort to assist our clients during this time.

Noninterest income was $15.0 million for the year ended December 31, 2019, a $4.8 million, or 46.9%, increase compared to noninterest income of $10.2 million for the year ended December 31, 2018. The increase in noninterest income during 2019, compared to 2018 resulted primarily from the following:

- Mortgage banking income increased $4.4 million, or 79.0%, driven by higher mortgage origination volume during 2019 due in part to the favorable interest rate environment for mortgage loans.
- ATM and debit card income increased $238,000, or 16.0%, driven by higher transaction volume when compared to 2018.
- Gain on sale of investment securities increased $720,000 primarily due to the sale of investments during the fourth quarter. See paragraph immediately below.
- Loss on extinguishment of debt resulted from the prepayment penalty related to the paydown of FHLB advances. See paragraph immediately below.
- Other income increased by $797,000, or 64.2%, due primarily to the sale of our Health Savings Account ("HSA") deposit accounts during the fourth quarter. See paragraph immediately below.

During the fourth quarter of 2019, the Company sold its Health Savings Account ("HSA") deposit accounts, which totaled $6.2 million, to a nationwide HSA servicer and recognized a gain of approximately $745,000 from the sale. Also during the fourth quarter, the Company sold $29.5 million of investment securities from its existing investment portfolio, recognizing a gain of approximately $720,000 and paid off $25.0 million of FHLB advances that resulted in a prepayment penalty of $1.5 million.

Noninterest Expenses

The following table sets forth information related to our noninterest expenses.

		Years ended December 31,	
(dollars in thousands)	**2020**	**2019**	**2018**
Compensation and benefits	$ 26,287	23,826	22,328
Mortgage production costs	9,898	6,436	4,152
Occupancy	6,226	5,513	5,035
Other real estate owned (income) expenses, net	1,223	(26)	116
Outside service and data processing costs	4,223	3,782	3,022
Insurance	1,380	813	1,284
Professional fees	1,771	1,327	1,345
Marketing	628	791	758
Other	2,108	2,011	1,723
Total noninterest expenses	$ 53,744	44,473	39,763

Noninterest expenses were $53.7 million for the year ended December 31, 2020, a $9.3 million, or 20.8%, increase from noninterest expense of $44.5 million for 2019.

The increase in total noninterest expenses during 2020, compared to 2019, resulted primarily from the following:

- Compensation and benefits expense increased $2.5 million, or 10.3%, during 2020 relating primarily to a $1.3 million increase in benefits expense, which includes insurance, 401k expenses and executive retirement plans. Base and incentive compensation also increased by $1.1 million as we continue to grow our existing markets.
- Mortgage production costs, which primarily includes compensation and benefits, professional fees, software licensing costs and credit bureau fees, increased $3.5 million, or 53.8%, driven by higher mortgage commissions as a result of the increased origination volume during 2020.
- Occupancy expenses increased $713,000, or 12.9%, driven by increased rent expense primarily due to office expansion in Atlanta, Georgia as well as additional depreciation, insurance, property taxes and maintenance expenses related to all of our owned properties.
- Other real estate owned expenses increased $1.2 million due to a valuation adjustment on one commercial property.
- Outside service and data processing costs increased $441,000, or 11.7%, primarily due to increased electronic banking, software licensing costs and ATM card related expenses.
- Insurance expenses increased $567,000, or 69.7%, resulting primarily from higher FDIC assessments during the year.
- Professional fees increased $444,000, or 33.5%, driven by increased audit, legal and various consulting fees.

Noninterest expenses were $44.5 million for the year ended December 31, 2019, a $4.7 million, or 11.8%, increase from noninterest expense of $39.8 million for 2018.

The increase in total noninterest expenses during 2019, compared to 2018, resulted primarily from the following:

- Compensation and benefits expense increased $3.5 million, or 13.6%, during 2019 relating primarily to an increase in base compensation, partially offset by a decrease in benefits expense. Base compensation expense increased by $4.1 million driven by the addition of 14 new employees - of which 12 were hired to support our new offices in Georgia, North Carolina, and South Carolina. Benefits expense, which includes insurance and 401k expenses, decreased by $485,000 primarily due to lower group insurance costs related to lower claims expense in 2019.
- Occupancy expenses increased $478,000, or 9.5%, driven by increased rent expense primarily due to two new offices in Summerville, South Carolina and Greensboro, North Carolina as well as additional depreciation, insurance, property taxes and maintenance expenses related to all of our owned properties.
- Outside service and data processing costs increased $885,000, or 26.8%, primarily due to increased electronic banking and software licensing costs.

Partially offsetting these increases in noninterest expenses during 2019 was a $471,000 decrease in insurance expenses which was driven by a reduction in FDIC premiums in the fourth quarter.

Our efficiency ratio was 50.2% for 2020 compared to 54.1% for 2019. The efficiency ratio represents the percentage of one dollar of expense required to be incurred to earn a full dollar of revenue and is computed by dividing noninterest expense by the sum of net interest income and noninterest income. The improvement during the 2020 period relates primarily to the increase in interest income and noninterest income, partially offset by the increase in noninterest expense compared to the prior year.

Income Taxes

Income tax expense was $5.5 million, $7.6 million and $6.4 million for the years ended December 31, 2020, 2019 and 2018, respectively. Our effective tax rate was 23.1% for the year ended December 31, 2020, compared to 21.5% for 2019, and 22.3% for 2018. The increase in the effective rate for the 2020 period is related to the greater impact of various employee stock option transactions that occurred during the 2019 period.

Investment Securities

At December 31, 2020 and 2019, our investment securities portfolio was $98.4 million and $74.6 million, respectively, and represented approximately 4.0% and 3.3% of our total assets, respectively. Our available for sale investment portfolio included U.S. agency securities, SBA securities, state and political subdivisions, mortgage-backed securities, and asset-backed securities with a fair value of $94.7 million and amortized cost of $93.4 million for an unrealized gain of $1.3 million at December 31, 2020 compared to a fair value of $67.7 million and amortized cost of $68.1 million for an unrealized loss of $377,000 at December 31, 2019.

The amortized costs and the fair value of our investments are as follows.

						December 31,
		2020		2019		2018
(dollars in thousands)	Amortized Cost	Fair Value	Amortized Cost	Fair Value	Amortized Cost	Fair Value
Available for Sale						
US government agencies	$ 6,500	6,493	$ 500	499	$ 8,975	8,782
SBA securities	504	485	550	531	3,628	3,525
State and political subdivisions	18,614	19,388	4,205	4,184	8,371	8,356
Asset-backed securities	11,587	11,529	13,351	13,167	9,595	9,558
Mortgage-backed securities	56,229	56,834	49,465	49,313	45,496	44,684
Total	$ 93,434	94,729	$ 68,071	67,694	$ 76,065	74,905

Contractual maturities and yields on our investments are shown in the following table. Expected maturities may differ from contractual maturities because issuers may have the right to call or prepay obligations with or without call or prepayment penalties.

	Less Than One Year		One to Five Years		Five to Ten Years		Over Ten Years		December 31, 2020 Total	
(dollars in thousands)	Amount	Yield	Amount	Yield	Amount	Yield	Amount	Yield	Amount	Yield
Available for Sale										
US government agencies	$ -	-	$ 2,501	0.37%	$ 2,995	1.07%	$ 997	1.48%	$ 6,493	0.86%
SBA securities	-	-	-	-	-	-	485	0.98%	485	0.98%
State and political subdivisions	-	-	470	2.13%	3,053	1.98%	15,865	2.23%	19,388	2.18%
Asset-backed securities	-	-	-	-	1,983	1.17%	9,546	1.00%	11,529	1.03%
Mortgage-backed securities	-	-	2,044	1.77%	9,544	1.74%	45,246	1.36%	56,834	1.44%
Total	$ -	-	$ 5,015	1.10%	$ 17,575	1.60%	$ 72,139	1.50%	$ 94,729	1.50%

Other investments are comprised of the following and are recorded at cost which approximates fair value.

	December 31,	
(dollars in thousands)	2020	2019
Federal Home Loan Bank stock	$ 3,103	6,386
Other investments	129	159
Investment in Trust Preferred subsidiaries	403	403
Total	$ 3,635	6,948

Loans

Since loans typically provide higher interest yields than other types of interest-earning assets, a substantial percentage of our earning assets are invested in our loan portfolio. Average loans for the years ended December 31, 2020 and 2019 were $2.11 billion and $1.81 billion, respectively. Before allowance for loan losses, total loans outstanding at December 31, 2020 and 2019 were $2.14 billion and $1.94 billion, respectively.

The principal component of our loan portfolio is loans secured by real estate mortgages. As of December 31, 2020, our loan portfolio included $1.81 billion, or 84.6%, of real estate loans, compared to $1.61 billion, or 82.8%, as of December 31, 2019. Most of our real estate loans are secured by residential or commercial property. We obtain a security interest in real estate, in addition to any other available collateral, in order to increase the likelihood of the ultimate repayment of the loan. Generally, we limit the loan-to-value ratio on loans to coincide with the appropriate regulatory guidelines. We attempt to maintain a relatively diversified loan portfolio to help reduce the risk inherent in concentration in certain types of collateral and business types. In addition to traditional residential mortgage loans, we issue second mortgage residential real estate loans and home equity lines of credit. Home equity lines of credit totaled $157.0 million as of December 31, 2020, of which approximately 45% were in a first lien position, while the remaining balance was second liens, compared to $179.7 million as of December 31, 2019, of which approximately 44% were in first lien positions and the remaining balance was in second liens. The average home equity loan had a balance of approximately $83,000 and a loan to value of approximately 62% as of December 31, 2020, compared to an average loan balance of $90,000 and a loan to value of approximately 68% as of December 31, 2019. Further, 0.2% and 0.4% of our total home equity lines of credit were over 30 days past due as of December 31, 2020 and 2019, respectively.

Following is a summary of our loan composition for each of the five years ended December 31, 2020. Of the $199.3 million in loan growth in 2020, $89.3 million of growth was in commercial related loans, while $110.0 million of growth was in consumer related loans, specifically consumer real estate mortgages which grew by $138.1 million during 2020. The increase in consumer real estate loans is related to our focus to continue to originate high quality 1-4 family consumer real estate loans. Our average consumer real estate loan currently has a principal balance of $429,000, a term of nineteen years, and an average rate of 3.82%.

(dollars in thousands)	2020 Amount	2020 % of Total	2019 Amount	2019 % of Total	2018 Amount	2018 % of Total	2017 Amount	2017 % of Total	December 31, 2016 Amount	2016 % of Total
Commercial										
Owner occupied RE	$ 433,320	20.2%	$ 407,851	21.0%	$ 367,018	21.9%	$ 316,818	22.8%	$ 285,938	24.6%
Non-owner occupied RE	585,269	27.3%	501,878	25.8%	404,296	24.1%	312,798	22.6%	239,574	20.6%
Construction	61,467	2.9%	80,486	4.1%	84,411	5.0%	51,179	3.7%	33,393	2.9%
Business	307,599	14.4%	308,123	15.9%	272,980	16.3%	226,158	16.3%	202,552	17.4%
Total commercial loans	1,387,655	64.8%	1,298,338	66.8%	1,128,705	67.3%	906,953	65.4%	761,457	65.5%
Consumer										
Real estate	536,311	25.0%	398,245	20.5%	320,943	19.1%	273,050	19.7%	215,588	18.5%
Home equity	156,957	7.3%	179,738	9.3%	165,937	9.9%	156,141	11.3%	137,105	11.8%
Construction	40,525	1.9%	41,471	2.1%	37,925	2.3%	28,351	2.0%	31,922	2.7%
Other	21,419	1.0%	25,733	1.3%	23,822	1.4%	22,575	1.6%	17,572	1.5%
Total consumer loans	755,212	35.2%	645,187	33.2%	548,627	32.7%	480,117	34.6%	402,187	34.5%
Total gross loans, net of deferred fees	2,142,867	100.0%	1,943,525	100.0%	1,677,332	100.0%	1,387,070	100.0%	1,163,644	100.0%
Less – allowance for loan losses	(44,149)		(16,642)		(15,762)		(15,523)		(14,855)	
Total loans, net	$2,098,718		$1,926,883		$1,661,570		$1,371,547		$1,148,789	

Maturities and Sensitivity of Loans to Changes in Interest Rates

The information in the following table is based on the contractual maturities of individual loans, including loans which may be subject to renewal at their contractual maturity. Renewal of such loans is subject to review and credit approval, as well as modification of terms upon maturity. Actual repayments of loans may differ from the maturities reflected below because borrowers have the right to prepay obligations with or without prepayment penalties.

The following table summarizes the loan maturity distribution by type and related interest rate characteristics.

(dollars in thousands)	December 31, 2020 One year or less	After one but within five years	After five years	Total
Commercial				
Owner occupied RE	$ 22,232	136,031	275,057	433,320
Non-owner occupied RE	39,359	335,249	210,661	585,269
Construction	21,824	15,785	23,858	61,467
Business	76,662	140,959	89,978	307,599
Total commercial loans	160,077	628,024	599,554	1,387,655
Consumer				
Real estate	14,205	54,863	467,243	536,311
Home equity	4,824	23,835	128,298	156,957
Construction	1,629	1,234	37,662	40,525
Other	6,438	11,413	3,568	21,419
Total consumer loans	27,096	91,345	636,771	755,212
Total gross loan, net of deferred fees	$ 187,173	719,369	1,236,325	2,142,867
Loans maturing – after one year with				
Fixed interest rates				$ 1,590,171
Floating interest rates				365,523

Nonperforming Assets

Nonperforming assets include real estate acquired through foreclosure or deed taken in lieu of foreclosure and loans on nonaccrual status. The following table shows the nonperforming assets and the related percentage of nonperforming assets to total assets and gross loans for the five years ended December 31, 2020. Generally, a loan is placed on nonaccrual status when it becomes 90 days past due as to principal or interest, or when we believe, after considering economic and business conditions and collection efforts, that the borrower's financial condition is such that collection of the loan is doubtful. A payment of interest on a loan that is classified as nonaccrual is recognized as a reduction in principal when received. Our policy with respect to nonperforming loans requires the borrower to make a minimum of six consecutive payments in accordance with the loan terms before that loan can be placed back on accrual status. Further, the borrower must show capacity to continue performing into the future prior to restoration of accrual status. As of December 31, 2020 and 2019, we had no loans 90 days past due and still accruing.

						December 31,
dollars in thousands)		2020	2019	2018	2017	2016
Commercial						
Owner occupied RE	$	-	-	-	-	276
Non-owner occupied RE		1,143	188	210	1,581	2,711
Construction		139	-	-	-	-
Business		195	235	81	910	686
Consumer						
Real estate		2,536	1,829	1,980	992	550
Home equity		547	431	1,006	1,144	256
Construction		-	-	-	-	-
Other		-	-	12	1	13
Nonaccruing troubled debt restructurings (TDRs)		3,509	4,111	2,541	2,673	990
Total nonaccrual loans, including nonaccruing TDRs		8,069	6,794	5,830	7,301	5,482
Other real estate owned		1,169	-	-	242	639
Total nonperforming assets	$	9,238	6,794	5,830	7,543	6,121
Nonperforming assets as a percentage of:						
Total assets		0.37%	0.30%	0.31%	0.46%	0.46%
Gross loans		0.43%	0.35%	0.35%	0.54%	0.53%
Total loans over 90 days past due [1]	$	2,296	2,038	458	2,027	1,984
Loans over 90 days past due and still accruing		-	-	-	-	-
Accruing troubled debt restructurings		4,893	5,219	6,742	5,145	5,675

[1] Loans over 90 days are included in nonaccrual loans

At December 31, 2020, nonperforming assets were $9.2 million, or 0.37% of total assets and 0.43% of gross loans, compared to $6.8 million, or 0.30% of total assets and 0.35% of gross loans at December 31, 2019. Nonaccrual loans increased $1.3 million to $8.1 million at December 31, 2020 from $6.8 million at December 31, 2019. During 2020, we added $10.0 million (consisting of 27 new loans) to nonaccrual, removed eight loans totaling $4.8 million that were paid off, transferred 1 loan totaling $2.2 million to other real estate owned and charged off $1.3 million of nonaccrual loans. The amount of foregone interest income on the nonaccrual loans for the years ended December 31, 2020 and 2019 was approximately $61,000 and $23,000, respectively.

At December 31, 2020, our allowance for loan losses represented 547.08% of nonaccrual loans, compared to 245.0% at year-end 2019 and 270.4% at year-end 2018. A significant portion, or 97.6%, of nonaccrual loans at December 31, 2020 were secured by real estate. We have evaluated the underlying collateral on these loans and believe that the collateral on these loans is sufficient to minimize future losses. As a result of this level of coverage on nonaccrual loans, we believe the allowance for loan losses of $44.1 million for the year ended December 31, 2020 is adequate.

As a general practice, most of our commercial loans and a portion of our consumer loans are originated with relatively short maturities of less than ten years. As a result, when a loan reaches its maturity we frequently renew the loan and thus extend its maturity using similar credit standards as those used when the loan was first originated. Due to these loan practices, we may, at times, renew loans which are classified as nonaccrual after evaluating the loan's collateral value and financial strength of its guarantors. Nonaccrual loans are renewed at terms generally consistent with the ultimate source of repayment and rarely at reduced rates. In these cases, we will generally seek additional credit enhancements, such as additional collateral or additional guarantees to further protect the loan. When a loan is no longer performing in accordance with its stated terms, we will typically seek performance under the guarantee.

In addition, approximately 85% of our loans are collateralized by real estate and approximately 89% of our impaired loans are secured by real estate. We use third party appraisers to determine the fair value of collateral dependent loans. Our current loan and appraisal policies require us to review impaired loans at least annually and determine whether it is necessary to obtain an updated appraisal, either through a new external appraisal or an internal appraisal evaluation. We individually review our impaired loans on a quarterly basis to determine the level of impairment. As of December 31, 2020, we do not have any impaired loans carried at a value in excess of the appraised value. We typically charge-off a portion or create a specific reserve for impaired loans when we do not expect repayment to occur as agreed upon under the original terms of the loan agreement.

At December 31, 2020, impaired loans totaled approximately $13.0 million for which $5.1 million of these loans have a reserve of approximately $1.7 million allocated in the allowance. During 2020, the average recorded investment in impaired loans was approximately $14.6 million. At December 31, 2019, impaired loans totaled approximately $12.0 million for which $4.7 million of these loans had a reserve of approximately $1.4 million allocated in the allowance. During 2019, the average recorded investment in impaired loans was approximately $12.3 million.

We consider a loan to be a TDR when the debtor experiences financial difficulties and we provide concessions such that we will not collect all principal and interest in accordance with the original terms of the loan agreement. Concessions can relate to the contractual interest rate, maturity date, or payment structure of the note. As part of our workout plan for individual loan relationships, we may restructure loan terms to assist borrowers facing challenges in the current economic environment. As of December 31, 2020 and 2019, we had $8.4 million and $9.3 million, respectively, in loans that we considered TDRs. As permitted by the CARES Act, we do not consider loan modifications to borrowers affected by COVID-19 to be TDRs unless the borrower was 30 days or more past due before December 31, 2019. See Notes 1 and 5 to the Consolidated Financial Statements for additional information on TDRs.

In addition, potential problem loans, which are loans rated substandard and not included in nonperforming loans or TDRs, amounted to approximately $19.6 million, or 0.92% of gross loans at December 31, 2020, compared to $9.0 million, or 0.46% of gross loans at December 31, 2019. Potential problem loans represent those loans with a well-defined weakness and where information about possible credit problems of borrowers has caused management to have serious doubts about the borrower's ability to comply with present repayment terms. The increase in potential problem loans since December 31, 2019 is primarily the result of two loans that increased total potential problem loans by approximately $13.5 million, partially offset by one loan partially charged-off and transferred to other real estate owned ("OREO").

Allowance for Loan Losses

At December 31, 2020 and December 31, 2019, the allowance for loan losses was $44.1 million and $16.6 million, respectively, or 2.06% and 0.86% of outstanding loans, respectively. The allowance for loan losses as a percentage of our outstanding loan portfolio increased from the prior year primarily due to an increase to our qualitative environmental factors related to the uncertain economic and business conditions at the national, regional and local levels at December 31, 2020. Factors such as the continued impact on the tourism and hospitality industries due to the pandemic, an increase in permanent job losses and unemployment rates as well as uncertainty in the political realm have driven this increase. We expect economic uncertainty to continue for at least the next few quarters which may result in a continued increase to the allowance for loan losses during 2021. Our nonperforming assets as a percentage of total assets increased to 0.37% at December 31, 2020 compared to 0.30% at December 31, 2019 and our classified assets increased to 8.2% of capital as of December 31, 2020, compared to 7.9% of capital as of December 31, 2019. See Note 4 to the Consolidated Financial Statements for more information on our allowance for loan losses.

The following table summarizes the activity related to our allowance for loan losses for the five years ended December 31, 2020.

(dollars in thousands)				Year ended December 31,	
	2020	2019	2018	2017	2016
Balance, beginning of period	$ 16,642	15,762	15,523	14,855	13,629
Provision for loan losses	29,600	2,300	1,900	2,000	2,300
Loan charge-offs:					
Commercial					
Owner occupied RE	(94)	(110)	-	-	(5)
Non-owner occupied RE	(1,508)	(239)	(432)	(589)	(100)
Construction	-	-	-	-	(42)
Business	(1,309)	(910)	(695)	(638)	(1,031)
Total commercial	(2,911)	(1,259)	(1,127)	(1,227)	(1,178)
Consumer					
Real estate	(134)	-	(826)	-	(194)
Home equity	(299)	(174)	(140)	(400)	(66)
Construction	-	-	-	-	-
Other	(70)	(82)	(53)	(11)	(210)
Total consumer	(503)	(256)	(1,019)	(411)	(470)
Total loan charge-offs	(3,414)	(1,515)	(2,146)	(1,638)	(1,648)
Loan recoveries:					
Commercial					
Owner occupied RE	65	-	-	-	-
Non-owner occupied RE	670	2	132	119	155
Construction	-	-	-	-	-
Business	470	43	229	86	403
Total commercial	1,205	45	361	205	558
Consumer					
Real estate	18	37	5	86	10
Home equity	69	2	115	13	1
Construction	-	-	-	-	-
Other	29	11	4	2	5
Total consumer	116	50	124	101	16
Total recoveries	1,321	95	485	306	574
Net loan charge-offs	(2,093)	(1,420)	(1,661)	(1,332)	(1,074)
Balance, end of period	$ 44,149	16,642	15,762	15,523	14,855
Allowance for loan losses to gross loans	2.06%	0.86%	0.94%	1.12%	1.28%
Net charge-offs to average loans	0.10%	0.08%	0.11%	0.10%	0.10%

Deposits and Other Interest-Bearing Liabilities

Our primary source of funds for loans and investments is our deposits and advances from the FHLB. In the past, we have chosen to obtain a portion of our certificates of deposits from areas outside of our market in order to obtain longer term deposits than are readily available in our local market. Our internal guidelines regarding the use of brokered CDs limit our brokered CDs to 20% of total deposits. In addition, we do not obtain time deposits of $100,000 or more through the Internet. These guidelines allow us to take advantage of the attractive terms that wholesale funding can offer while mitigating the related inherent risk.

Our retail deposits represented $2.12 billion, or 99.0% of total deposits at December 31, 2020, while our out-of-market, or brokered deposits, represented $22.0 million, or 1.0% of our total deposits at December 31, 2020. At December 31, 2019, retail deposits represented $1.81 billion, or 96.4% of our total deposits, and brokered deposits were $67.4 million, representing 3.6% of our total deposits, at December 31, 2019. Our loan-to-deposit ratio was 100%, 104%, and 102% at December 31, 2020, 2019, and 2018, respectively.

The following table shows the average balance amounts and the average rates paid on deposits held by us.

						December 31,
		2020		2019		2018
(dollars in thousands)	Amount	Rate	Amount	Rate	Amount	Rate
Noninterest bearing demand deposits	$ 513,576	-%	$ 367,674	-%	$ 298,709	-%
Interest bearing demand deposits	255,514	0.14%	205,513	0.27%	235,623	0.17%
Money market accounts	981,226	0.76%	849,225	1.78%	653,436	1.34%
Savings accounts	22,113	0.05%	15,483	0.06%	15,870	0.05%
Time deposits less than $100,000	41,406	1.40%	58,043	1.88%	60,032	1.43%
Time deposits greater than $100,000	259,672	1.27%	305,388	1.72%	272,169	1.77%
Total deposits	$ 2,073,507	0.57%	$ 1,801,326	1.22%	$ 1,535,839	0.97%

During the 12 months ended December 31, 2020, our average transaction account balances increased by $334.5 million, or 23.3%, while our average time deposit balances decreased by $62.4 million, or 17.2%. Core deposits exclude out-of-market deposits and time deposits of $250,000 or more and provide a relatively stable funding source for our loan portfolio and other earning assets. Our core deposits were $2.01 billion, $1.66 billion, and $1.43 billion at December 31, 2020, 2019 and 2018, respectively.

All of our time deposits are certificates of deposits. The maturity distribution of our time deposits of $100,000 or more is as follows:

		December 31,
(dollars in thousands)	2020	2019
Three months or less	$ 83,606	85,130
Over three through six months	35,565	58,721
Over six through twelve months	48,083	91,867
Over twelve months	23,702	51,273
Total	$ 190,956	286,991

Included in time deposits of $100,000 or more at December 31, 2020 is $22.0 million of wholesale CDs scheduled to mature within the next 12 months at a weighted average rate of 2.10%. Time deposits that meet or exceed the FDIC insurance limit of $250,000 at December 31, 2020 and December 31, 2019 were $130.9 million and $220.1 million, respectively.

Liquidity and Capital Resources

Liquidity represents the ability of a company to convert assets into cash or cash equivalents without significant loss, and the ability to raise additional funds by increasing liabilities. Liquidity management involves monitoring our sources and uses of funds in order to meet our day-to-day cash flow requirements while maximizing profits. Liquidity management is made more complicated because different balance sheet components are subject to varying degrees of management control. For example, the timing of maturities of our investment portfolio is fairly predictable and subject to a high degree of control at the time investment decisions are made. However, net deposit inflows and outflows are far less predictable and are not subject to the same degree of control.

At December 31, 2020 and 2019, our cash and cash equivalents amounted to $100.7 million and $127.8 million, or 4.1% and 5.6% of total assets, respectively. Our investment securities at December 31, 2020 and 2019 amounted to $98.4 million and $74.6 million, or 4.0% and 3.3% of total assets, respectively. Investment securities traditionally provide a secondary source of liquidity since they can be converted into cash in a timely manner.

Our ability to maintain and expand our deposit base and borrowing capabilities serves as our primary source of liquidity. We plan to meet our future cash needs through the liquidation of temporary investments, the generation of deposits, and from additional borrowings. In addition, we will receive cash upon the maturity and sale of loans and the maturity of investment securities. We maintain five federal funds purchased lines of credit with correspondent banks totaling $118.5 million for which there were no borrowings against the lines at December 31, 2020.

We are also a member of the FHLB of Atlanta, from which applications for borrowings can be made. The FHLB requires that securities, qualifying mortgage loans, and stock of the FHLB owned by the Bank be pledged to secure any advances from the FHLB. The unused borrowing capacity currently available from the FHLB at December 31, 2020 was $512.5 million, based on the Bank's $3.1 million investment in FHLB stock, as well as qualifying mortgages available to secure any future borrowings. However, we are able to pledge additional securities to the FHLB in order to increase our available borrowing capacity. In addition, at December 31, 2020 we had $206.2 million of letters of credit outstanding with the FHLB to secure client deposits.

We also have a line of credit with another financial institution for $15.0 million, which was unused at December 31, 2020. The line of credit bears interest at LIBOR plus 3.50% and matures on December 31, 2021.

We believe that our existing stable base of core deposits, federal funds purchased lines of credit with correspondent banks, and borrowings from the FHLB will enable us to successfully meet our long-term liquidity needs. However, as short-term liquidity needs arise, we have the ability to sell a portion of our investment securities portfolio to meet those needs.

Total shareholders' equity was $228.3 million at December 31, 2020 and $205.9 million at December 31, 2019. The $22.4 million increase during 2020 is due primarily to net income to common shareholders of $18.3 million, stock option exercises and expenses of $2.8 million and $1.3 million in other comprehensive income.

The following table shows the return on average assets (net income divided by average total assets), return on average equity (net income divided by average equity), equity to assets ratio (average equity divided by average assets), and tangible common equity ratio (total equity less preferred stock divided by total assets) for the three years ended December 31, 2020. Since our inception, we have not paid cash dividends.

			December 31,
(dollars in thousands)	**2020**	**2019**	**2018**
Return on average assets	0.76%	1.35%	1.27%
Return on average equity	8.49%	14.72%	13.83%
Return on average common equity	8.49%	14.72%	13.83%
Average equity to average assets ratio	9.01%	9.16%	9.15%
Tangible common equity to assets ratio	9.20%	9.08%	9.15%

Under the capital adequacy guidelines, regulatory capital is classified into two tiers. These guidelines require an institution to maintain a certain level of Tier 1 and Tier 2 capital to risk-weighted assets. Tier 1 capital consists of common shareholders' equity, excluding the unrealized gain or loss on securities available for sale, minus certain intangible assets. In determining the amount of risk-weighted assets, all assets, including certain off-balance sheet assets, are multiplied by a risk-weight factor of 0% to 100% based on the risks believed to be inherent in the type of asset. Tier 2 capital consists of Tier 1 capital plus the general reserve for loan losses, subject to certain limitations. We are also required to maintain capital at a minimum level based on total average assets, which is known as the Tier 1 leverage ratio.

Regulatory capital rules adopted in July 2013 and fully-phased in as of January 1, 2019, which we refer to Basel III, impose minimum capital requirements for bank holding companies and banks. The Basel III rules apply to all national and state banks and savings associations regardless of size and bank holding companies and savings and loan holding companies other than "small bank holding companies," generally holding companies with consolidated assets of less than $3 billion (such as the Company). In order to avoid restrictions on capital distributions or discretionary bonus payments to executives, a covered banking organization must maintain a "capital conservation buffer" on top of our minimum risk-based capital requirements. This buffer must consist solely of common equity Tier 1, but the buffer applies to all three measurements (common equity Tier 1, Tier 1 capital and total capital). The capital conservation buffer consists of an additional amount of CET1 equal to 2.5% of risk-weighted assets.

To be considered "well-capitalized" for purposes of certain rules and prompt corrective action requirements, the Bank must maintain a minimum total risked-based capital ratio of at least 10%, a total Tier 1 capital ratio of at least 8%, a common equity Tier 1 capital ratio of at least 6.5%, and a leverage ratio of at least 5%. As of December 31, 2020, our capital ratios exceed these ratios and we remain "well capitalized."

The following table summarizes the capital amounts and ratios of the Bank and the regulatory minimum requirements. See Note 23 to the Consolidated Financial Statements for ratios of the Company.

(dollars in thousands)	Amount	Actual Ratio	Amount	For capital adequacy purposes minimum [(1)] Ratio	Amount	To be well capitalized under prompt corrective action provisions minimum Ratio
As of December 31, 2020						
Total Capital (to risk weighted assets)	$ 279,414	13.92%	$ 160,554	8.00%	$ 200,693	10.00%
Tier 1 Capital (to risk weighted assets)	254,092	12.66%	120,416	6.00%	160,554	8.00%
Common Equity Tier 1 (to risk weighted assets)	254,092	12.66%	90,312	4.50%	130,451	6.50%
Tier 1 Capital (to average assets)	254,092	10.26%	99,094	4.00%	123,867	5.00%
As of December 31, 2019						
Total Capital (to risk weighted assets)	$ 250,847	13.31%	$ 150,807	8.00%	$ 188,510	10.00%
Tier 1 Capital (to risk weighted assets)	234,205	12.42%	113,106	6.00%	150,807	8.00%
Common Equity Tier 1 (to risk weighted assets)	234,205	12.42%	84,829	4.50%	122,531	6.50%
Tier 1 Capital (to average assets)	234,205	10.80%	86,772	4.00%	108,465	5.00%
As of December 31, 2018						
Total Capital (to risk weighted assets)	198,195	12.16%	130,368	8.00%	162,960	10.00%
Tier 1 Capital (to risk weighted assets)	182,433	11.20%	97,776	6.00%	130,368	8.00%
Common Equity Tier 1 (to risk weighted assets)	182,433	11.20%	73,332	4.50%	105,924	6.50%
Tier 1 Capital (to average assets)	182,433	9.84%	74,126	4.00%	92,658	5.00%

[1] Ratios do not include the capital conservation buffer of 2.5% in 2020 and 2019 and 1.875% in 2018.

On September 30, 2019, the Company sold and issued $23.0 million in aggregate principal amount of its 4.75% Fixed-to-Floating Rate Subordinated Notes due 2029 to eligible purchasers in a private offering. The Company intends to use the proceeds from the offering, which were approximately $22.5 million, for general corporate purposes, including providing capital to the Bank and supporting organic growth. The Notes rank junior in right to payment to the Company's current and future senior indebtedness. The Notes are intended to qualify as Tier 2 capital for regulatory capital purposes for the Company.

The ability of the Company to pay cash dividends is dependent upon receiving cash in the form of dividends from the Bank. The dividends that may be paid by the Bank to the Company are subject to legal limitations and regulatory capital requirements.

Effect of Inflation and Changing Prices

The effect of relative purchasing power over time due to inflation has not been taken into account in our consolidated financial statements. Rather, our financial statements have been prepared on an historical cost basis in accordance with generally accepted accounting principles.

Unlike most industrial companies, our assets and liabilities are primarily monetary in nature. Therefore, the effect of changes in interest rates will have a more significant impact on our performance than will the effect of changing prices and inflation in general. In addition, interest rates may generally increase as the rate of inflation increases, although not necessarily in the same magnitude. As discussed previously, we seek to manage the relationships between interest sensitive assets and liabilities in order to protect against wide rate fluctuations, including those resulting from inflation.

Off-Balance Sheet Risk

Commitments to extend credit are agreements to lend to a client as long as the client has not violated any material condition established in the contract. Commitments generally have fixed expiration dates or other termination clauses and may require the payment of a fee. At December 31, 2020, unfunded commitments to extend credit were approximately $480.1 million, of which $114.6 million were at fixed rates and $365.5 million were at variable rates. At December 31, 2019, unfunded commitments to extend credit were $426.6 million, of which approximately $105.0 million were at fixed rates and $321.7 million were at variable rates. A majority of the unfunded commitments related to commercial business lines of credit and home equity lines of credit. Based on historical experience, we anticipate that a significant portion of these lines of credit will not be funded. We evaluate each client's credit worthiness on a case-by-case basis. The amount of collateral obtained, if deemed necessary by us upon extension of credit, is based on our credit evaluation of the borrower. The type of collateral varies but may include accounts receivable, inventory, property, plant and equipment, and commercial and residential real estate.

At December 31, 2020 and 2019, there were $8.7 million and $9.9 million of commitments under letters of credit, respectively. The credit risk and collateral involved in issuing letters of credit is essentially the same as that involved in extending loan facilities to clients. Since most of the letters of credit are expected to expire without being drawn upon, they do not necessarily represent future cash requirements.

Except as disclosed in this Annual Report, we are not involved in off-balance sheet contractual relationships, unconsolidated related entities that have off-balance sheet arrangements or transactions that could result in liquidity needs or other commitments that significantly impact earnings.

Market Risk and Interest Rate Sensitivity

Market risk is the risk of loss from adverse changes in market prices and rates, which principally arises from interest rate risk inherent in our lending, investing, deposit gathering, and borrowing activities. Other types of market risks, such as foreign currency exchange rate risk and commodity price risk, do not generally arise in the normal course of our business.

We actively monitor and manage our interest rate risk exposure in order to control the mix and maturities of our assets and liabilities utilizing a process we call asset/liability management. The essential purposes of asset/liability management are to ensure adequate liquidity and to maintain an appropriate balance between interest sensitive assets and liabilities in order to minimize potentially adverse impacts on earnings from changes in market interest rates. Our asset/liability management committee (“ALCO”) monitors and considers methods of managing exposure to interest rate risk. We have both an internal ALCO consisting of senior management that meets at various times during each month and a board ALCO that meets monthly. The ALCOs are responsible for maintaining the level of interest rate sensitivity of our interest sensitive assets and liabilities within board-approved limits.

As of December 31, 2020, the following table summarizes the forecasted impact on net interest income using a base case scenario given upward and downward movements in interest rates of 100, 200, and 300 basis points based on forecasted assumptions of prepayment speeds, nominal interest rates and loan and deposit repricing rates. Estimates are based on current economic conditions, historical interest rate cycles and other factors deemed to be relevant. However, underlying assumptions may be impacted in future periods which were not known to management at the time of the issuance of the Consolidated Financial Statements. Therefore, management’s assumptions may or may not prove valid. No assurance can be given that changing economic conditions and other relevant factors impacting our net interest income will not cause actual occurrences to differ from underlying assumptions. In addition, this analysis does not consider any strategic changes to our balance sheet which management may consider as a result of changes in market conditions.

Interest rate scenario	Change in net interest income from base
Up 300 basis points	15.22%
Up 200 basis points	10.18%
Up 100 basis points	5.12%
Base	-
Down 100 basis points	(3.41)%
Down 200 basis points	(5.30)%
Down 300 basis points	(6.81)%

Contractual Obligations

We utilize a variety of short-term and long-term borrowings to supplement our supply of lendable funds, to assist in meeting deposit withdrawal requirements, and to fund growth of interest-earning assets in excess of traditional deposit growth. Certificates of deposit, structured repurchase agreements, FHLB advances, and subordinated debentures serve as our primary sources of such funds.

Obligations under noncancelable operating lease agreements are payable over several years with the longest obligation expiring in 2029. We do not feel that any existing noncancelable operating lease agreements are likely to materially impact our financial condition or results of operations in an adverse way. Contractual obligations relative to these agreements are noted in the table below. Option periods that we have not yet exercised are not included in this analysis as they do not represent contractual obligations until exercised.

The following table provides payments due by period for obligations under long-term borrowings and operating lease obligations as of December 31, 2020.

	December 31, 2020 Payments Due by Period					
(dollars in thousands)	Within One Year	Over One to Two Years	Over Two to Three Years	Over Three to Four Years	After Five Years	Total
Certificates of deposit	$ 200,657	13,244	8,373	2,370	2,766	227,410
FHLB advances and other borrowings	25,000	-	-	-	-	25,000
Subordinated debentures	-	-	-	-	36,403	36,403
Operating lease obligations	2,335	1,587	1,462	1,501	17,430	24,315
Total	$ 227,992	14,831	9,835	3,871	56,599	313,128

Accounting, Reporting, and Regulatory Matters

See Note 1 – Summary of Significant Accounting Policies and Activities in our “Notes to Consolidated Financial Statements” for a discussion on the effects of recently issued accounting pronouncements.

Item 7A. Quantitative and Qualitative Disclosures about Market Risk

See Item 7. Management’s Discussion and Analysis of Financial Condition and Results of Operations – Market Risk and Interest Rate Sensitivity and – Liquidity and Capital Resources.

Item 8. Financial Statements and Supplementary Data

MANAGEMENT'S REPORT ON INTERNAL CONTROL OVER FINANCIAL REPORTING

Management of Southern First Bancshares, Inc. is responsible for establishing and maintaining adequate internal control over financial reporting as defined in Rule 13a-15(f) of the Securities Exchange Act of 1934, as amended. The Company's internal control over financial reporting is a process designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with accounting principles generally accepted in the U.S. The Company's internal control over financial reporting includes those policies and procedures that (1) pertain to the maintenance of records, that in reasonable detail, accurately and fairly reflect the transactions and disposition of the Company's assets; (2) provide reasonable assurance that transactions are recorded as necessary to permit the preparation of the financial statements in accordance with generally accepted accounting principles and that receipts and expenditures of the Company are being made only in accordance with the authorizations of the Company's management and directors; and (3) provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use or disposition of the Company's assets that could have a material impact on the financial statements.

Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Also, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate due to changes in conditions, or that the degree of compliance with the policies and procedures may deteriorate.

Management conducted an evaluation of the effectiveness of the internal control over financial reporting based on the framework in *Internal Control — Integrated Framework* issued by the Committee of Sponsoring Organizations of the Treadway Commission ("COSO") in 2013. Based on this evaluation under the COSO criteria, management concluded that the internal control over financial reporting was effective as of December 31, 2020.

The effectiveness of the internal control structure over financial reporting as of December 31, 2020 has been audited by Elliott Davis, LLC, an independent registered public accounting firm, as stated in their report included in this Annual Report on Form 10-K, which expresses an unqualified opinion on the effectiveness of the Company's internal control over financial reporting as of December 31, 2020.

/s/ R. Arthur Seaver, Jr.
Chief Executive Officer
Southern First Bancshares, Inc.

/s/ Michael D. Dowling
Chief Financial Officer & Chief Operating Officer
Southern First Bancshares, Inc.

Report of Independent Registered Public Accounting Firm

To the Shareholders and Board of Directors of
Southern First Bancshares, Inc. and Subsidiary

Opinion on the Internal Control Over Financial Reporting

We have audited Southern First Bancshares, Inc. and Subsidiary's (the "Company") internal control over financial reporting as of December 31, 2020, based on criteria established in *Internal Control — Integrated Framework* issued by the Committee of Sponsoring Organizations of the Treadway Commission in 2013. In our opinion, the Company maintained, in all material respects, effective internal control over financial reporting as of December 31, 2020, based on criteria established in *Internal Control — Integrated Framework* issued by the Committee of Sponsoring Organizations of the Treadway Commission in 2013.

We have also audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States) (PCAOB), the consolidated balance sheets of the Company as of December 31, 2020 and 2019 and the related consolidated statements of income, comprehensive income, shareholders' equity, and cash flows for each of the three years in the period ended December 31, 2020 of the Company and our report dated March 2, 2021 expressed an unqualified opinion.

Basis for Opinion

The Company's management is responsible for maintaining effective internal control over financial reporting and for its assessment of the effectiveness of internal control over financial reporting in the accompanying Management's Report on Internal Control over Financial Reporting. Our responsibility is to express an opinion on the Company's internal control over financial reporting based on our audit. We are a public accounting firm registered with the PCAOB and are required to be independent with respect to the Company in accordance with U.S. federal securities laws and the applicable rules and regulations of the Securities and Exchange Commission and the PCAOB.

We conducted our audit in accordance with the standards of the PCAOB. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether effective internal control over financial reporting was maintained in all material respects. Our audit included obtaining an understanding of internal control over financial reporting, assessing the risk that a material weakness exists, and testing and evaluating the design and operating effectiveness of internal control based on the assessed risk. Our audit also included performing such other procedures as we considered necessary in the circumstances. We believe that our audit provides a reasonable basis for our opinion.

Definition and Limitations of Internal Control Over Financial Reporting

A company's internal control over financial reporting is a process designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles. A company's internal control over financial reporting includes those policies and procedures that (1) pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect the transactions and dispositions of the assets of the company; (2) provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with generally accepted accounting principles, and that receipts and expenditures of the company are being made only in accordance with authorizations of management and directors of the company; and (3) provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use or disposition of the company's assets that could have a material effect on the financial statements.

Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Also, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

/s/ Elliott Davis, LLC

Greenville, South Carolina
March 2, 2021

Report of Independent Registered Public Accounting Firm

To the Shareholders and Board of Directors of
Southern First Bancshares, Inc. and Subsidiary

Opinion on the Financial Statements

We have audited the accompanying consolidated balance sheets of Southern First Bancshares, Inc. and Subsidiary (the "Company") as of December 31, 2020 and 2019, the related consolidated statements of income, comprehensive income, shareholders' equity, and cash flows for each of the three years in the period ended December 31, 2020, and the related notes to the consolidated financial statements (collectively, the "financial statements"). In our opinion, the financial statements present fairly, in all material respects, the financial position of the Company as of December 31, 2020 and 2019, and the results of its operations and its cash flows for each of the three years in the period ended December 31, 2020, in conformity with accounting principles generally accepted in the United States of America.

We have also audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States) (PCAOB), the Company's internal control over financial reporting as of December 31, 2020, based on criteria established in *Internal Control — Integrated Framework* issued by the Committee of Sponsoring Organizations of the Treadway Commission in 2013, and our report dated March 2, 2021 expressed an unqualified opinion on the effectiveness of the Company's internal control over financial reporting.

Basis for Opinion

These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on the Company's financial statements based on our audits. We are a public accounting firm registered with the PCAOB and are required to be independent with respect to the Company in accordance with U.S. federal securities laws and the applicable rules and regulations of the Securities and Exchange Commission and the PCAOB.

We conducted our audits in accordance with the standards of the PCAOB. Those standards require that we plan and perform the audits to obtain reasonable assurance about whether the financial statements are free of material misstatement, whether due to error or fraud. Our audits included performing procedures to assess the risks of material misstatement of the financial statements, whether due to error or fraud, and performing procedures that respond to those risks. Such procedures included examining, on a test basis, evidence regarding the amounts and disclosures in the financial statements. Our audits also included evaluating the accounting principles used and significant estimates made by management, as well as evaluating the overall presentation of the financial statements. We believe that our audits provide a reasonable basis for our opinion.

Critical Audit Matters

The critical audit matters communicated below are matters arising from the current period audit of the financial statements that were communicated or required to be communicated to the audit committee and that: (1) relate to accounts or disclosures that are material to the consolidated financial statements and (2) involved our especially challenging, subjective, or complex judgments. The communication of critical audit matters does not alter in any way our opinion on the financial statements, taken as a whole, and we are not, by communicating the critical audit matters below, providing separate opinions on the critical audit matters or on the accounts or disclosures to which they relate.

Allowance for Loan Losses

As described in Note 4 to the Company's consolidated financial statements, the Company has a gross loan portfolio of $2.1 billion and related allowance for loan losses of $44.1 million as of December 31, 2020. As described by the Company in Note 1, the evaluation of the allowance for loan losses is inherently subjective as it requires estimates that are susceptible to significant revision as more information becomes available. The allowance for loan losses is evaluated on a regular basis and is based upon the Company's review of the collectability of the loans in light of historical experience, the nature and volume of the loan portfolio, adverse situations that may affect the borrower's ability to repay, estimated value of any underlying collateral, and prevailing economic conditions.

We identified the Company's estimate of the allowance for loan losses as a critical audit matter. The principal considerations for our determination of the allowance for loan losses as a critical audit matter related to the high degree of subjectivity in the Company's judgments in determining the qualitative factors. Auditing these complex judgments and assumptions by the Company involves especially challenging auditor judgment due to the nature and extent of audit evidence and effort required to address these matters, including the extent of specialized skill or knowledge needed.

The primary procedures we performed to address this critical audit matter included the following:

- We tested the design and operating effectiveness of controls relating to the Company's determination of the allowance for loan losses, including controls over qualitative factors.
- We evaluated the relevance and the reasonableness of assumptions related to evaluation of the loan portfolio, current economic conditions, and other risk factors used in development of the qualitative factors for collectively evaluated loans.
- We evaluated the reasonableness of assumptions and data used by the Company in developing the qualitative factors by comparing these data points to internally developed and third-party sources, and other audit evidence gathered.

/s/ Elliott Davis, LLC

We have served as the Company's auditor since 1999.

Greenville, South Carolina
March 2, 2021

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SOUTHERN FIRST BANCSHARES, INC. AND SUBSIDIARY
CONSOLIDATED BALANCE SHEETS

(dollars in thousands, except share data)		December 31, 2020	2019
ASSETS			
Cash and cash equivalents:			
Cash and due from banks	$	12,920	19,196
Federal funds sold		21,744	89,256
Interest-bearing deposits with banks		66,023	19,364
Total cash and cash equivalents		100,687	127,816
Investment securities:			
Investment securities available for sale		94,729	67,694
Other investments		3,635	6,948
Total investment securities		98,364	74,642
Mortgage loans held for sale		60,257	27,046
Loans		2,142,867	1,943,525
Less allowance for loan losses		(44,149)	(16,642)
Loans, net		2,098,718	1,926,883
Bank owned life insurance		41,102	40,011
Property and equipment, net		60,236	58,478
Deferred income taxes, net		9,518	4,275
Other assets		13,705	8,044
Total assets	$	2,482,587	2,267,195
LIABILITIES			
Deposits	$	2,142,758	1,876,124
Federal Home Loan Bank advances and other borrowings		25,000	110,000
Subordinated debentures		35,998	35,890
Other liabilities		50,537	39,321
Total liabilities		2,254,293	2,061,335
SHAREHOLDERS' EQUITY			
Preferred stock, par value $.01 per share, 10,000,000 shares authorized		-	-
Common stock, par value $.01 per share, 10,000,000 shares authorized, 7,772,748 and 7,672,678 shares issued and outstanding at December 31, 2020 and 2019, respectively		78	77
Nonvested restricted stock		(698)	(803)
Additional paid-in capital		108,831	106,152
Accumulated other comprehensive income (loss)		1,023	(298)
Retained earnings		119,060	100,732
Total shareholders' equity		228,294	205,860
Total liabilities and shareholders' equity	$	2,482,587	2,267,195

See notes to consolidated financial statements that are an integral part of these consolidated statements.

SOUTHERN FIRST BANCSHARES, INC. AND SUBSIDIARY
CONSOLIDATED STATEMENTS OF INCOME

		For the years ended December 31,	
(dollars in thousands, except per share data)	**2020**	**2019**	**2018**
Interest income			
Loans	$ 93,133	88,929	73,718
Investment securities	1,415	2,101	1,801
Federal funds sold and interest-bearing deposits with banks	270	1,622	1,138
Total interest income	94,818	92,652	76,657
Interest expense			
Deposits	13,055	23,730	14,836
Borrowings	1,953	1,653	1,669
Total interest expense	15,008	25,383	16,505
Net interest income	79,810	67,269	60,152
Provision for loan losses	29,600	2,300	1,900
Net interest income after provision for loan losses	50,210	64,969	58,252
Noninterest income			
Mortgage banking income	19,785	9,923	5,544
Service fees on deposit accounts	860	1,061	1,040
ATM and debit card income	1,741	1,728	1,490
Income from bank owned life insurance	1,091	1,001	878
Gain on sale of investment securities, net	3	727	7
Loss on extinguishment of debt	(37)	(1,496)	-
Net lender fees on PPP loan sale	2,247	-)	-
Other income	1,663	2,039	1,242
Total noninterest income	27,353	14,983	10,201
Noninterest expenses			
Compensation and benefits	26,287	23,826	22,328
Mortgage production costs	9,898	6,436	4,152
Occupancy	6,226	5,513	5,035
Other real estate owned (income) expenses, net	1,223	(26)	116
Outside service and data processing costs	4,223	3,782	3,022
Insurance	1,380	813	1,284
Professional fees	1,771	1,327	1,345
Marketing	628	791	758
Other	2,108	2,011	1,723
Total noninterest expenses	53,744	44,473	39,763
Income before income tax expense	23,819	35,479	28,690
Income tax expense	5,491	7,621	6,401
Net income available to common shareholders	$ 18,328	27,858	22,289
Earnings per common share			
Basic	$ 2.37	3.70	3.02
Diluted	$ 2.34	3.58	2.88
Weighted average common shares outstanding			
Basic	7,718,615	7,528,283	7,384,200
Diluted	7,824,214	7,772,544	7,737,495

See notes to consolidated financial statements that are an integral part of these consolidated statements.

SOUTHERN FIRST BANCSHARES, INC. AND SUBSIDIARY
CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME

	For the years ended December 31,		
(dollars in thousands)	**2020**	**2019**	**2018**
Net income	$ 18,328	27,858	22,289
Other comprehensive income:			
Unrealized gain (loss) on securities available for sale:			
Unrealized holding gain (loss) arising during the period, pretax	1,675	1,510	(575)
Tax (expense) benefit	(352)	(317)	120
Reclassification of realized gain	(3)	(727)	(7)
Tax expense	1	153	1
Other comprehensive income (loss)	1,321	619	(461)
Comprehensive income	$ 19,649	28,477	21,828

See notes to consolidated financial statements that are an integral part of these consolidated statements.

SOUTHERN FIRST BANCSHARES, INC. AND SUBSIDIARY
CONSOLIDATED STATEMENTS OF SHAREHOLDERS' EQUITY
FOR THE YEARS ENDED DECEMBER 31, 2020, 2019 AND 2018

	Common stock		**Preferred stock**		**Nonvested restricted stock**	**Additional paid-in capital**	**Accumulated other comprehensive income (loss)**	**Retained Earnings**	**Total**
(dollars in thousands, except share data)	**Shares**	**Amount**	**Shares**	**Amount**					
December 31, 2017	**7,347,851**	**73**	**-**	**-**	**(502)**	**99,986**	**(456)**	**50,585**	**149,686**
Net income	-	-	-	-	-	-	-	22,289	22,289
Proceeds from exercise of stock options	105,630	2	-	-	-	898	-	-	900
Issuance of restricted stock	13,000	-	-	-	(558)	558	-	-	-
Compensation expense related to restricted stock, net of tax	-	-	-	-	319	-	-	-	319
Compensation expense related to stock options, net of tax	-	-	-	-	-	1,183	-	-	1,183
Other comprehensive loss	-	-	-	-	-	-	(461)	-	(461)
December 31, 2018	**7,466,481**	**75**	**-**	**-**	**(741)**	**102,625**	**(917)**	**72,874**	**173,916**
Net income	-	-	-	-	-	-	-	27,858	27,858
Proceeds from exercise of stock options	191,497	2	-	-	-	1,767	-	-	1,769
Issuance of restricted stock	14,700	-	-	-	(490)	490	-	-	-
Compensation expense related to restricted stock, net of tax	-	-	-	-	428	-	-	-	428
Compensation expense related to stock options, net of tax	-	-	-	-	-	1,270	-	-	1,270
Other comprehensive income	-	-	-	-	-	-	619	-	619
December 31, 2019	**7,672,678**	**$ 77**	**-**	**$ -**	**$ (803)**	**$ 106,152**	**$ (298)**	**$ 100,732**	**$ 205,860**
Net income	-	-	-	-	-	-	-	18,328	18,328
Proceeds from exercise of stock options	93,870	1	-	-	-	1,387	-	-	1,388
Issuance of restricted stock, net of forfeitures	6,200	-	-	-	(275)	275	-	-	-
Compensation expense related to restricted stock, net of tax	-	-	-	-	380	-	-	-	380
Compensation expense related to stock options, net of tax	-	-	-	-	-	1,017	-	-	1,017
Other comprehensive income	-	-	-	-	-	-	1,321	-	1,321
December 31, 2020	**7,772,748**	**$ 78**	**-**	**$ -**	**$ (698)**	**$ 108,831**	**$ 1,023**	**$ 119,060**	**$ 228,294**

See notes to consolidated financial statements that are an integral part of these consolidated statements.

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SOUTHERN FIRST BANCSHARES, INC. AND SUBSIDIARY
CONSOLIDATED STATEMENTS OF CASH FLOWS

		For the years ended December 31,	
(dollars in thousands)	**2020**	**2019**	**2018**
Operating activities			
Net income	$ 18,328	27,858	22,289
Adjustments to reconcile net income to cash provided by operating activities:			
Provision for loan losses	29,600	2,300	1,900
Depreciation and other amortization	2,190	1,915	1,755
Accretion and amortization of securities discounts and premiums, net	710	432	437
Write-down of real estate owned	1,029	-	117
Gain on sale of investment securities available for sale	(3)	(727)	(7)
Gain on sale of fixed assets	(196)	-	(8)
Net change in operating leases	180	585	-
Compensation expense related to stock options and restricted stock grants	1,397	1,698	1,502
Gain on sale of loans held for sale	(21,186)	(10,219)	(5,144)
Loans originated and held for sale	(594,289)	(380,632)	(204,429)
Proceeds from sale of loans held for sale	582,264	373,046	212,122
Increase in cash surrender value of bank owned life insurance	(1,091)	(1,001)	(878)
Increase in deferred tax asset	(2,741)	(420)	(115)
(Increase) decrease in other assets, net	(4,670)	(600)	216
Increase in other liabilities, net	9,097	4,074	1,946
Net cash provided by operating activities	20,619	18,309	31,703
Investing activities			
Increase (decrease) in cash realized from:			
Increase in loans, net	(203,632)	(267,613)	(291,923)
Purchase of property and equipment	(7,276)	(8,431)	(1,943)
Purchase of investment securities:			
Available for sale	(50,854)	(39,930)	(23,181)
Other investments	(2,338)	(4,675)	(46)
Proceeds from maturities, calls and repayments of investment securities:			
Available for sale	24,784	19,212	9,025
Other investments	5,651	1,848	387
Proceeds from sale of investment securities available for sale	-	29,006	5,841
Purchase of life insurance policies	-	(5,000)	-
Proceeds from sale of fixed assets	2,895	-	-
Proceeds from sale of other real estate owned	-	-	132
Net cash used for investing activities	(230,770)	(275,583)	(301,708)
Financing activities			
Increase (decrease) in cash realized from:			
Increase in deposits, net	266,634	227,988	267,013
Increase (decrease) in Federal Home Loan Bank advances and other borrowings	(85,000)	60,000	(17,200)
Increase of subordinated debt	-	22,460	-
Proceeds from the exercise of stock options	1,388	1,769	900
Net cash provided by financing activities	183,022	312,217	250,713
Net increase (decrease) in cash and cash equivalents	(27,129)	54,943	(19,292)
Cash and cash equivalents, beginning of year	127,816	72,873	92,165
Cash and cash equivalents, end of year	$ 100,687	127,816	72,873
Supplemental information			
Cash paid for			
Interest	$ 16,312	25,156	15,410
Income taxes	2,741	7,883	5,451
Schedule of non-cash transactions			
Foreclosure of other real estate	2,198	-	-
Unrealized (gain) loss on securities, net of income taxes	(1,323)	(1,193)	455
Right-of-use assets obtained in exchange for lease obligations:			
Operating leases	2,115	21,459	-

See notes to consolidated financial statements that are an integral part of these consolidated statements.

NOTE 1 – Summary of Significant Accounting Policies and Activities

Southern First Bancshares, Inc. (the "Company") is a South Carolina corporation that owns all of the capital stock of Southern First Bank (the "Bank") and all of the stock of Greenville First Statutory Trust I and II (collectively, the "Trusts"). The Trusts are special purpose non-consolidated entities organized for the sole purpose of issuing trust preferred securities. The Bank's primary federal regulator is the Federal Deposit Insurance Corporation (the "FDIC"). The Bank is also regulated and examined by the South Carolina Board of Financial Institutions. The Bank is primarily engaged in the business of accepting demand deposits and savings deposits insured by the FDIC, and providing commercial, consumer and mortgage loans to the general public.

Basis of Presentation

The accompanying consolidated financial statements include the accounts of the Company and its wholly owned subsidiary, Southern First Bank. In consolidation, all significant intercompany transactions have been eliminated. The accounting and reporting policies conform to accounting principles generally accepted in the United States of America. In accordance with guidance issued by the Financial Accounting Standards Board (“FASB”), the operations of the Trusts have not been consolidated in these financial statements.

Business Segments

ASC Topic 280-10, “Segment Reporting,” requires selected segment information of operating segments based on a management approach. The Company’s three reportable segments represent the distinct product lines the Company offers and are viewed separately for strategic planning by management. Please refer to “Note 24 – Reportable Segments” for further information on the reporting for the Company’s three business segments.

Use of Estimates

The preparation of consolidated 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 as of the date of the consolidated financial statements and the reported amount of income and expenses during the reporting periods. 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, derivatives, real estate acquired in settlement of loans, fair value of financial instruments, evaluating other-than-temporary-impairment of investment securities and valuation of deferred tax assets.

Risks and Uncertainties

In the normal course of its business, the Company encounters two significant types of risks: economic and regulatory. There are three main components of economic risk: interest rate risk, credit risk and market risk. The Company is subject to interest rate risk to the degree that its interest-bearing liabilities mature or reprice at different speeds, or on different bases, than its interest-earning assets. Credit risk is the risk of default within the Company’s loan portfolio that results from borrowers’ inability or unwillingness to make contractually required payments. Market risk reflects changes in the value of collateral underlying loans receivable and the valuation of real estate held by the Company.

The Company is subject to the regulations of various governmental agencies. These regulations can and do change significantly from period to period. The Company also undergoes periodic examinations by the regulatory agencies, which may subject it to changes with respect to valuation of assets, amount of required loan loss allowance and operating restrictions resulting from the regulators’ judgments based on information available to them at the time of their examinations.

The Bank makes loans to individuals and businesses in the Upstate, Midlands, and Lowcountry regions of South Carolina as well as the Triangle and Triad regions of North Carolina and Atlanta, Georgia for various personal and commercial purposes. The Bank’s loan portfolio has a concentration of real estate loans. As of December 31, 2020 and 2019, real estate loans represented 84.6% and 82.8%, respectively, of total loans. However, borrowers’ ability to repay their loans is not dependent upon any specific economic sector.

The impact of the coronavirus (COVID-19) pandemic is fluid and continues to evolve, adversely affecting many of the Bank’s clients. The unprecedented and rapid spread of COVID-19 and its associated impacts on trade (including supply chains and export levels), travel, employee productivity, unemployment, consumer spending, and other economic activities has resulted in less economic activity, lower equity market valuations and significant volatility and disruption in financial markets, and has had an adverse effect on the Company’s business, financial condition and results of operations. The ultimate extent of the impact of the COVID-19 pandemic on our business, financial condition and results of operations is currently uncertain and will depend on various developments and other factors, including governmental and private sector initiatives, the effect of the recent rollout of vaccinations for the virus, whether such vaccinations will be effective against any resurgence of the virus, including any new strains, and the ability for customers and businesses to return to their pre-pandemic routine.

The Company's business, financial condition and results of operations generally rely upon the ability of the Bank's borrowers to repay their loans, the value of collateral underlying the Bank's secured loans, and demand for loans and other products and services the Bank offers, which are highly dependent on the business environment in the Bank's primary markets where it operates and in the United States as a whole.

On March 3, 2020, the Federal Reserve reduced the target federal funds rate by 50 basis points, followed by an additional reduction of 100 basis points on March 16, 2020. These reductions in interest rates and other effects of the COVID-19 pandemic have had, and are expected to continue to have, possibly materially, an adverse effect on Company's business, financial condition and results of operations. For instance, the pandemic has had negative effects on the Bank's interest income, provision for loan losses, and certain transaction-based line items of noninterest income. Other financial impacts could occur though such potential impact is unknown at this time.

As of December 31, 2020, the Company's and the Bank's capital ratios were in excess of all regulatory requirements. While management believes that we have sufficient capital to withstand an extended economic recession brought about by the COVID-19 pandemic, our reported and regulatory capital ratios could be adversely impacted by further credit losses.

The Company maintains access to multiple sources of liquidity, including a $15.0 million holding company line of credit with another bank which could be used to support capital ratios at the subsidiary bank. As of December 31, 2020, the $15.0 million line was unused.

Subsequent Events

Subsequent events are events or transactions that occur after the balance sheet date but before financial statements are issued. Recognized subsequent events are events or transactions that provide additional evidence about conditions that existed at the date of the balance sheet, including the estimates inherent in the process of preparing financial statements. Non-recognized subsequent events are events that provide evidence about conditions that did not exist at the date of the balance sheet but arose after that date. Management performed an evaluation to determine whether there have been any subsequent events since the balance sheet date and determined that no subsequent events occurred requiring accrual or disclosure.

Reclassifications

Certain amounts, previously reported, have been reclassified to state all periods on a comparable basis and had no effect on shareholders' equity or net income.

Cash and Cash Equivalents

Cash and cash equivalents include cash and due from banks, interest bearing deposits and federal funds sold. Cash and cash equivalents have original maturities of three months or less, and federal funds sold are generally purchased and sold for one-day periods. Accordingly, the carrying value of these instruments is deemed to be a reasonable estimate of fair value. At December 31, 2020 and 2019, included in cash and cash equivalents was $12.6 million and $6.0 million, respectively, on deposit with the Federal Reserve Bank.

Investment Securities

We classify our investment securities as held to maturity securities, trading securities and available for sale securities as applicable.

Investment securities are designated as held to maturity if we have the intent and the ability to hold the securities to maturity. Held to maturity securities are carried at amortized cost, adjusted for the amortization of any related premiums or the accretion of any related discounts into interest income using a methodology which approximates a level yield of interest over the estimated remaining period until maturity. Unrealized losses on held to maturity securities, reflecting a decline in value judged by us to be other than temporary, are charged to income in the Consolidated Statements of Income.

Investment securities that are purchased and held principally for the purpose of selling in the near term are reported as trading securities. Trading securities are carried at fair value with unrealized holding gains and losses included in earnings.

We classify investment securities as available for sale when at the time of purchase we determine that such securities may be sold at a future date or if we do not have the intent or ability to hold such securities to maturity. Securities designated as available for sale are recorded at fair value. Changes in the fair value of available for sale debt securities are included in shareholders' equity as unrealized gains or losses, net of the related tax effect. Unrealized losses on available for sale securities, reflecting a decline in value judged to be other than temporary, are charged to income in the Consolidated Statements of Income. Realized gains or losses on available for sale securities are computed on the specific identification basis.

Other Investments

The Bank, as a member institution, is required to own a stock investment in the Federal Home Loan Bank of Atlanta ("FHLB"). This stock is generally pledged against any borrowings from the FHLB and cash dividends on our FHLB stock are recorded in investment income. No ready market exists for these stocks and they have no quoted market value. However, redemption of this stock has historically been at par value. Other investments also include a $403,000 investment in the Trusts.

Loans

Loans are stated at the principal balance outstanding. Unamortized net loan fees and the allowance for possible loan losses are deducted from total loans on the balance sheets. Interest income is recognized over the term of the loan based on the principal amount outstanding. The net of loan origination fees received and direct costs incurred in the origination of loans is deferred and amortized to interest income over the contractual life of the loans adjusted for actual principal prepayments using a method approximating the interest method.

Nonaccrual and Past Due Loans

Loans are generally placed on nonaccrual status when principal or interest becomes 90 days past due, or when payment in full is not anticipated. When a loan is placed on nonaccrual status, interest accrued but not received is generally reversed against interest income. Cash receipts on nonaccrual loans are not recorded as interest income, but are used to reduce the loan's principal balance. A nonaccrual loan is generally returned to accrual status and accrual of interest is resumed when payments have been made according to the terms and conditions of the loan for a continuous six month period. Our loans are considered past due when contractually required principal or interest payments have not been made on the due dates.

Nonperforming Assets

Nonperforming assets include real estate acquired through foreclosure or deed taken in lieu of foreclosure, loans on nonaccrual status and loans past due 90 days or more and still accruing interest. Loans are placed on nonaccrual status when, in the opinion of management, the collection of additional interest is uncertain. Thereafter no interest is taken into income until such time as the borrower demonstrates the ability to pay both principal and interest.

Impaired Loans

Our impaired loans include loans on nonaccrual status and loans modified in a troubled debt restructuring ("TDR"), whether on accrual or nonaccrual status. For loans that are classified as impaired, an allowance is established when the fair value (discounted cash flows, collateral value, or observable market price) of the impaired loan less costs to sell, are lower than the carrying value of that loan. A loan is considered impaired when, based on current information and events, it is probable that the Company will be unable to collect the scheduled payments of principal or interest when due according to the contractual terms of the loan agreement. Factors considered by management in determining impairment include payment status, collateral value, and the probability of collecting scheduled principal and interest payments when due, among other factors. Loans that experience insignificant payment delays and payment shortfalls 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 the borrower, including, without limitation, 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. Impairment is measured on a loan by loan basis for commercial and consumer loans by either the present value of expected future cash flows discounted at the loan's effective interest rate, the loan's obtainable market price, or the fair value of the collateral if the loan is collateral dependent.

Loan Charge-off Policy

For commercial loans, we generally fully charge off or charge collateralized loans down to net realizable value when management determines the loan to be uncollectible; repayment is deemed to be projected beyond reasonable time frames; the loan has been classified as a loss by either our internal loan review process or our banking regulatory agencies; the client has filed bankruptcy and the loss becomes evident owing to a lack of assets; or the loan is 120 days past due unless both well-secured and in the process of collection. For consumer loans, we generally charge down to net realizable value when the loan is 180 days past due.

Troubled Debt Restructuring (TDRs)

The Company considers a loan to be a TDR when the debtor experiences financial difficulties and the Company provides concessions such that we will not collect all principal and interest in accordance with the original terms of the loan agreement. Concessions can relate to the contractual interest rate, maturity date, or payment structure of the note. As part of our workout plan for individual loan relationships, we may restructure loan terms to assist borrowers facing challenges in the current economic environment.

In accordance with the CARES Act, the Company implemented loan modification programs in response to the COVID-19 pandemic, and the Company elected the accounting policy in the CARES Act to not apply TDR accounting to loans modified for borrowers impacted by the COVID-19 pandemic. In 2020, the Company granted short-term loan deferrals to six client relationships, with loans totaling $3.2 million at December 31, 2020, which were considered TDRs due to the client experiencing financial difficulty before the pandemic.

Our policy with respect to accrual of interest on loans restructured in a TDR follows relevant supervisory guidance. That is, if a borrower has demonstrated performance under the previous loan terms and shows capacity to perform under the restructured loan terms; continued accrual of interest at the restructured interest rate is likely. If a borrower was materially delinquent on payments prior to the restructuring, but shows capacity to meet the restructured loan terms, the loan will likely continue as nonaccrual going forward. Lastly, if the borrower does not perform under the restructured terms, the loan is placed on nonaccrual status. We will continue to closely monitor these loans and will cease accruing interest on them if management believes that the borrowers may not continue performing based on the restructured note terms. If, after previously being classified as a TDR, a loan is restructured a second time and the borrower continues to experience financial difficulties, then that loan is automatically placed on nonaccrual status. Our policy with respect to nonperforming loans requires the borrower to make a minimum of six consecutive payments of principal and interest in accordance with the loan terms before that loan can be placed back on accrual status. Further, the borrower must show capacity to continue performing into the future prior to restoration of accrual status. In addition, our policy, in accordance with supervisory guidance, also provides for a loan to be removed from TDR status if the loan is modified or renewed at terms consistent with current market rates and the loan has been performing under modified terms for an extended period of time or under certain circumstances.

In the determination of the allowance for loan losses, management considers TDRs on commercial and consumer loans and subsequent defaults in these restructurings by measuring impairment, on a loan by loan basis, based on either the present value of expected future cash flows discounted at the loan's effective interest rate, the loan's obtainable market price, or the fair value of the collateral, less costs to sell, if the loan is collateral dependent.

Allowance for Loan Losses

The allowance for loan losses is management's estimate of credit losses inherent in the loan portfolio. 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 uncollectibility of a loan balance is confirmed. Subsequent recoveries, if any, are credited to the allowance. The allowance for loan losses is evaluated on a regular basis by management and is based upon management's periodic review of the collectability of the loans in light of historical experience, the nature and volume of the loan portfolio, adverse situations that may affect the borrower's ability to repay, the estimated value of any underlying collateral and prevailing economic conditions. This evaluation is inherently subjective as it requires estimates that are susceptible to significant revision as more information becomes available.

We have an established process to determine the adequacy of the allowance for loan losses that assesses the losses inherent in our portfolio. While we attribute portions of the allowance to specific portfolio segments, the entire allowance is available to absorb credit losses inherent in the total loan portfolio. Our process involves procedures to appropriately consider the unique risk characteristics of our commercial and consumer loan portfolio segments. For each portfolio segment, impairment is measured individually for each impaired loan. Our allowance levels are influenced by loan volume, loan grade or delinquency status, historic loss experience and other economic conditions. See Note 4 to the Consolidated Financial Statements for additional information on the allowance for loan losses.

Other Real Estate Owned

Real estate acquired through foreclosure is initially recorded at the lower of cost or estimated fair value less selling costs. Subsequent to the date of acquisition, it is carried at the lower of cost or fair value, adjusted for net selling costs. Fair values of real estate owned are reviewed regularly and write-downs are recorded when it is determined that the carrying value of real estate exceeds the fair value less estimated costs to sell. Costs relating to the development and improvement of such property are capitalized, whereas those costs relating to holding the property are expensed.

Property and Equipment

Property and equipment are stated at cost. Major repairs are charged to operations, while major improvements are capitalized. Depreciation is computed using the straight-line method over the estimated useful lives of the related assets. Upon retirement, sale, or other disposition of property and equipment, the cost and accumulated depreciation are eliminated from the accounts, and gain or loss is included in income from operations.

Construction in progress is stated at cost, which includes the cost of construction and other direct costs attributable to the construction. No provision for depreciation is made on construction in progress until such time as the relevant assets are completed and put into use.

Bank Owned Life Insurance Policies

Bank owned life insurance policies represent the cash value of policies on certain officers of the Company.

Comprehensive Income

Comprehensive income (loss) consists of net income and net unrealized gains (losses) on securities and is presented in the statements of shareholders' equity and comprehensive income. The statement requires only additional disclosures in the consolidated financial statements; it does not affect our results of operations.

Revenue from Contracts with Customers

The Company records revenue from contracts with customers in accordance with Accounting Standards Codification Topic 606, "Revenue from Contracts with Customers" ("Topic 606"). Under Topic 606, the Company must identify the contract with a customer, identify the performance obligations in the contract, determine the transaction price, allocate the transaction price to the performance obligations in the contract, and recognize revenue when (or as) the Company satisfies a performance obligation. Significant revenue has not been recognized in the current reporting period that results from performance obligations satisfied in previous periods.

The Company's primary sources of revenue are derived from interest and dividends earned on loans, investment securities, and other financial instruments that are not within the scope of Topic 606. The Company has evaluated the nature of its contracts with customers and determined that further disaggregation of revenue from contracts with customers into more granular categories beyond what is presented in the Consolidated Statements of Income was not necessary. The Company generally fully satisfies its performance obligations on its contracts with customers as services are rendered and the transaction prices are typically fixed; charged either on a periodic basis or based on activity. Our accounting policies did not change materially since the principles of revenue recognition from Topic 606 are largely consistent with existing guidance and current practices applied by our business. The following is a discussion of revenues within the scope of the guidance:

- *Service fees on deposit accounts* - The Company earns fees from its deposit clients for various transaction-based, account maintenance, and overdraft or non-sufficient funds ("NSF") services. Transaction-based fees, which include services such as stop payment charges, statement rendering, and ACH fees, are recognized at the time the transaction is executed as that is the point in time the Company fulfills the client's request. Account maintenance fees, which relate primarily to monthly maintenance and account management, are earned over the course of a month, representing the period over which the Company satisfies the performance obligation. Overdraft and NSF fees are recognized at the point in time that the overdraft occurs or the NSF item is presented. Service charges on deposits are withdrawn from the client's account balance.

- *ATM and debit card income* - The Company earns interchange fees from debit cardholder transactions conducted through the payment networks. Interchange fees from cardholder transactions represent a percentage of the underlying transaction value and are recognized daily, concurrently with the transaction processing services provided to the cardholder.

Income Taxes

The financial statements have been prepared on the accrual basis. When income and expenses are recognized in different periods for financial reporting purposes versus for the purposes of computing income taxes currently payable, deferred taxes are provided on such temporary differences. Deferred tax assets and liabilities are recognized for the expected future tax consequences of events that have been recognized in the consolidated financial statements or tax returns. Deferred tax assets and liabilities are measured using the enacted tax rates expected to apply to taxable income in the years in which those temporary differences are expected to be realized or settled. The Company believes that its income tax filing positions taken or expected to be taken on its tax returns will more likely than not be sustained upon audit by the taxing authorities and does not anticipate any adjustments that will result in a material adverse impact on the Company's financial condition, results of operations, or cash flow. Therefore, no reserves for uncertain income tax positions have been recorded. The Company's federal and state income tax returns are open and subject to examination from the 2017 tax return year and forward.

Stock-Based Compensation

The Company has a stock-based employee compensation plan. Compensation cost is recognized for all stock options granted and for any outstanding unvested awards as if the fair value method had been applied to those awards as of the date of grant.

Newly Issued, But Not yet Effective Accounting Standards

In June 2016, the FASB issued ASU 2016-13, *"Financial Instruments – Credit Losses (Topic 326): Measurement of Credit Losses on Financial Instruments"*. Among other things, ASU 2016-13 requires the measurement of all expected credit losses for financial assets held at the reporting date based on historical experience, current conditions, and reasonable and supportable forecasts. Financial institutions and other organizations will now use forward-looking information to form their credit loss estimates. Many of the loss estimation techniques applied today will still be permitted, although the inputs to those techniques will change to reflect the full amount of expected credit losses. In addition, ASU 2016-13 amends the accounting for credit losses on debt securities and purchased financial assets with credit deterioration. ASU 2016-13 was originally effective for all annual and interim periods beginning after December 31, 2019, with early adoption permitted for fiscal years beginning after December 15, 2018. Adoption will be applied through a cumulative-effect adjustment to retained earnings as of the beginning of the first reporting period in which the guidance is effective. The Company has established a team of individuals from credit, finance and risk management to evaluate the requirements of the new standard and the impact it will have on its processes.

In November 2019, the FASB issued guidance that addresses issues raised by stakeholders during the implementation of ASU 2016-13, *"Financial Instruments – Credit Losses (Topic 326): Measurement of Credit Losses on Financial Instruments"*. The amendments affect a variety of Topics in the Accounting Standards Codification. For public business entities that meet the definition of a smaller reporting company, such as the Company, the amendments are effective for fiscal years beginning after December 15, 2022 including interim periods within those fiscal years. Early adoption is permitted in any interim period as long as the Company has adopted to amendments in ASU 2016-13. Currently, the Company does not expect to adopt the ASU before the effective period.

In October 2020, the FASB updated various Topics of the Accounting Standards Codification to align the guidance in various SEC sections of the Codification with the requirements of certain SEC final rules. The amendments were effective upon issuance and did not have a material effect on the financial statements.

Other accounting standards that have been issued or proposed by the FASB or other standards-setting bodies that do not require adoption until a future date are not expected to have a material impact on the consolidated financial statements upon adoption.

NOTE 2 – Investment Securities

The amortized costs and fair value of investment securities are as follows:

					December 31, 2020
		Amortized	Gross Unrealized		Fair
(dollars in thousands)		Cost	Gains	Losses	Value
Available for sale					
US government agencies	$	6,500	1	8	6,493
SBA securities		504	-	19	485
State and political subdivisions		18,614	804	30	19,388
Asset-backed securities		11,587	15	73	11,529
Mortgage-backed securities					
FHLMC		12,157	206	47	12,316
FNMA		35,893	507	91	36,309
GNMA		8,179	53	23	8,209
Total mortgage-backed securities		56,229	766	161	56,834
Total	$	93,434	1,586	291	94,729

(dollars in thousands)		Amortized Cost	Gross Unrealized Gains	Losses	December 31, 2019 Fair Value
Available for sale					
US government agencies	$	500	-	1	499
SBA securities		550	-	19	531
State and political subdivisions		4,205	3	24	4,184
Asset-backed securities		13,351	-	184	13,167
Mortgage-backed securities					
FHLMC		10,609	14	15	10,608
FNMA		35,275	34	169	35,140
GNMA		3,581	5	21	3,565
Total mortgage-backed securities		49,465	53	205	49,313
Total	$	68,071	56	433	67,694

During 2020, approximately $2.0 million of investment securities were either sold or called, subsequently resulting in a gain on sale of investment securities of $3,000.

The amortized costs and fair values of investment securities available for sale at December 31, 2020 and 2019, by contractual maturity, are shown below. Expected maturities may differ from contractual maturities because issuers have the right to prepay the obligations.

(dollars in thousands)		2020 Amortized Cost	2020 Fair Value		December 31, 2019 Amortized Cost	December 31, 2019 Fair Value
Available for sale						
Due within one year	$	-	-	$	-	-
Due after one through five years		4,957	5,015		4,699	4,675
Due after five through ten years		17,345	17,575		10,454	10,414
Due after ten years		71,132	72,139		52,918	52,605
	$	93,434	94,729	$	68,071	67,694

The tables below summarize gross unrealized losses on investment securities and the fair market value of the related securities, aggregated by investment category and length of time that individual securities have been in a continuous unrealized loss position, at December 31, 2020 and 2019.

(dollars in thousands)	Less than 12 months #	Fair value	Unrealized losses	12 months or longer #	Fair value	Unrealized losses	Total #	Fair value	Unrealized losses
As of December 31, 2020									
Available for sale									
US government agencies	3	$ 2,992	$ 8	-	$ -	$ -	3	$ 2,992	$ 8
SBA securities	-	-	-	1	484	19	1	484	19
State and political subdivisions	8	4,861	30	-	-	-	8	4,861	30
Asset-backed	-	-	-	6	6,998	73	6	6,998	73
Mortgage-backed									
FHLMC	4	5,313	47	-	-	-	4	5,313	47
FNMA	9	11,659	66	3	1,984	25	12	13,643	91
GNMA	2	3,838	23	-	-	-	2	3,838	23
	26	$ 28,663	$ 174	10	$ 9,466	$ 117	36	$ 38,129	$ 291

(dollars in thousands)	#	Less than 12 months Fair value	Unrealized losses	#	12 months or longer Fair value	Unrealized losses	#	Total Fair value	Unrealized losses
As of December 31, 2019									
Available for sale									
US government agencies	1	$ 499	$ 1	-	$ -	$ -	1	$ 499	$ 1
SBA securities	-	-	-	1	531	19	1	531	19
State and political subdivisions	2	2,093	24	-	-	-	2	2,093	24
Asset-backed	5	5,921	68	5	7,246	116	10	13,167	184
Mortgage-backed									
FHLMC	4	3,842	2	4	2,323	13	8	6,165	15
FNMA	14	15,500	67	11	9,462	102	25	24,962	169
GNMA	2	2,240	6	1	734	15	3	2,974	21
	28	$ 30,095	$ 168	22	$ 20,296	$ 265	50	$ 50,391	$ 433

At December 31, 2020, the Company had 26 individual investments with a fair market value of $28.7 million that were in an unrealized loss position for less than 12 months and 10 individual investments with a fair market value of $9.5 million that were in an unrealized loss position for 12 months or longer. The unrealized losses were primarily attributable to changes in interest rates, rather than deterioration in credit quality. The individual securities are each investment grade securities. The Company considers the length of time and extent to which the fair value of available-for-sale debt securities have been less than cost to conclude that such securities were not other-than-temporarily impaired. We also consider other factors such as the financial condition of the issuer including credit ratings and specific events affecting the operations of the issuer, volatility of the security, underlying assets that collateralize the debt security, and other industry and macroeconomic conditions. As the Company has no intent to sell securities with unrealized losses and it is not more-likely-than-not that the Company will be required to sell these securities before recovery of amortized cost, we have concluded that the securities are not impaired on an other-than-temporary basis.

Other investments are comprised of the following and are recorded at cost which approximates fair value:

(dollars in thousands)	2020	December 31, 2019
Federal Home Loan Bank stock	$ 3,103	$ 6,386
Other investments	129	159
Investment in Trust Preferred subsidiaries	403	403
	$ 3,635	$ 6,948

The Company has evaluated the FHLB stock for impairment and determined that the investment in FHLB stock is not other than temporarily impaired as of December 31, 2020 and ultimate recoverability of the par value of this investment is probable. All of the FHLB stock is used to collateralize advances with the FHLB.

At December 31, 2020 and 2019, there were no securities pledged as collateral for repurchase agreements from brokers.

NOTE 3 – Mortgage Loans Held for Sale

Mortgage loans originated and intended for sale in the secondary market are reported as loans held for sale and carried at fair value under the fair value option with changes in fair value recognized in current period earnings. Loans held for sale include mortgage loans which are saleable into the secondary mortgage markets and their fair values are estimated using observable quoted market or contracted prices or market price equivalents, which would be used by other market participants. At the date of funding of the mortgage loan held for sale, the funded amount of the loan, the related derivative asset or liability of the associated interest rate lock commitment, less direct loan costs becomes the initial recorded investment in the loan held for sale. Such amount approximates the fair value of the loan. At December 31, 2020, mortgage loans held for sale totaled $60.2 million compared to $27.0 million at December 31, 2019.

Mortgage loans held for sale are considered de-recognized, or sold, when the Company surrenders control over the financial assets. Control is considered to have been surrendered when the transferred assets have been isolated from the Company, beyond the reach of the Company and its creditors; the purchaser obtains the right (free of conditions that constrain it from taking advantage of that right) to pledge or exchange the transferred assets; and the Company does not maintain effective control over the transferred assets through an agreement that both entitles and obligates the Company to repurchase or redeem the transferred assets before their maturity or the ability to unilaterally cause the holder to return specific assets.

Gains and losses from the sale of mortgage loans are recognized based upon the difference between the sales proceeds and carrying value of the related loans upon sale and are recorded in mortgage banking income in the statement of income. Mortgage banking income also includes the unrealized gains and losses associated with the loans held for sale and the realized and unrealized gains and losses from derivatives.

Mortgage loans sold to investors by the Company, and which were believed to have met investor and agency underwriting guidelines at the time of sale, may be subject to repurchase or indemnification in the event of specific default by the borrower or subsequent discovery that underwriting standards were not met. The Company may, upon mutual agreement, agree to repurchase the loans or indemnify the investor against future losses on such loans. In such cases, the Company bears any subsequent credit loss on the loans. As appropriate, the Company establishes mortgage repurchase reserves related to various representations and warranties that reflect management's estimate of losses.

NOTE 4 – Loans and Allowance for Loan Losses

The Company makes loans to individuals and small businesses for various personal and commercial purposes primarily in the Upstate, Midlands, and Lowcountry regions of South Carolina, the Triangle and Triad regions of North Carolina as well as Atlanta, Georgia. The Company's loan portfolio is not concentrated in loans to any single borrower or a relatively small number of borrowers. The Company focuses its lending activities primarily on the professional markets in these regions including doctors, dentists, and small business owners. The principal component of the loan portfolio is loans secured by real estate mortgages which account for 84.6% of total loans at December 31, 2020. Commercial loans comprise 59.5% of total real estate loans and consumer loans account for 40.5%. Commercial real estate loans are further categorized into owner occupied which represents 20.2% of total loans and non-owner occupied loans represent 27.3%. Commercial construction loans represent only 2.9% of the total loan portfolio.

In addition to monitoring potential concentrations of loans to particular borrowers or groups of borrowers, industries and geographic regions, management monitors exposure to credit risk from concentrations of lending products and practices such as loans that subject borrowers to substantial payment increases (e.g. principal deferral periods, loans with initial interest-only periods, etc.), and loans with high loan-to-value ratios. Additionally, there are industry practices that could subject the Company to increased credit risk should economic conditions change over the course of a loan's life. For example, the Company makes variable rate loans and fixed rate principal-amortizing loans with maturities prior to the loan being fully paid (i.e. balloon payment loans). The various types of loans are individually underwritten and monitored to manage the associated risks.

The allowance for loan losses is management's estimate of credit losses inherent in the loan portfolio at the balance sheet date. We have an established process to determine the adequacy of the allowance for loan losses that assesses the losses inherent in our portfolio. While we attribute portions of the allowance to specific portfolio segments, the entire allowance is available to absorb credit losses inherent in the total loan portfolio. Our process involves procedures to appropriately consider the unique risk characteristics of our commercial and consumer loan portfolio segments. For each portfolio segment, impairment is measured individually for each impaired loan. Our allowance levels are influenced by loan volume, loan grade or delinquency status, historic loss experience and other economic conditions.

Paycheck Protection Program ("PPP")

On March 27, 2020, President Trump signed the Coronavirus Aid, Relief, and Economic Security Act (the "CARES" Act or the "Act") to provide emergency assistance and health care response for individuals, families, and businesses affected by the coronavirus pandemic. The Small Business Administration ("SBA") received funding and authority through the Act to modify existing loan programs and establish a new loan program to assist small businesses nationwide adversely impacted by the COVID-19 emergency. The Act temporarily permits the SBA to guarantee 100% of certain loans under a new program titled the "Paycheck Protection Program" and also provides for forgiveness of up to the full principal amount of qualifying loans guaranteed under the PPP.

In an effort to assist our clients as best we could through the pandemic, we became an approved SBA lender in March 2020 and processed 853 loans under the PPP for a total of $97.5 million, receiving SBA lender fee income of $3.9 million. As the regulations and guidance for PPP loans and the forgiveness process continued to change and evolve, management recognized the operational risk and complexity associated with this portfolio and decided to pursue the sale of the PPP loan portfolio to a third party better suited to support and serve our PPP clients through the loan forgiveness process. The loan sale allowed our team to focus on serving our clients and proactively monitoring and addressing credit risk brought on by the pandemic. On June 26, 2020, we completed the sale of our PPP loan portfolio to The Loan Source Inc., together with its servicing partner, ACAP SME LLC, and immediately recognized SBA lender fee income of $2.2 million, net of sale and processing costs, which is included in other noninterest income in the consolidated financial statements.

Portfolio Segment Methodology

Commercial
Commercial loans are assessed for estimated losses by grading each loan using various risk factors identified through periodic reviews. The Company applies historic grade-specific loss factors to each loan class. In the development of statistically derived loan grade loss factors, the Company observes historical losses over 20 quarters for each loan grade. These loss estimates are adjusted as appropriate based on additional analysis of external loss data or other risks identified from current economic conditions and credit quality trends. The allowance also includes an amount for the estimated impairment on nonaccrual commercial loans and commercial loans modified in a TDR, whether on accrual or nonaccrual status.

Consumer
For consumer loans, the Company determines the allowance on a collective basis utilizing historical losses over 20 quarters to represent its best estimate of inherent loss. The Company pools loans, generally by loan class with similar risk characteristics. The allowance also includes an amount for the estimated impairment on nonaccrual consumer loans and consumer loans modified in a TDR, whether on accrual or nonaccrual status.

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The following table summarizes the composition of our loan portfolio. Total gross loans are recorded net of deferred loan fees and costs, which totaled $3.9 million and $3.3 million as of December 31, 2020 and December 31, 2019, respectively.

(dollars in thousands)		2020		December 31, 2019
Commercial				
Owner occupied RE	$ 433,320	20.2%	$ 407,851	21.0%
Non-owner occupied RE	585,269	27.3%	501,878	25.8%
Construction	61,467	2.9%	80,486	4.1%
Business	307,599	14.4%	308,123	15.9%
Total commercial loans	1,387,655	64.8%	1,298,338	66.8%
Consumer				
Real estate	536,311	25.0%	398,245	20.5%
Home equity	156,957	7.3%	179,738	9.3%
Construction	40,525	1.9%	41,471	2.1%
Other	21,419	1.0%	25,733	1.3%
Total consumer loans	755,212	35.2%	645,187	33.2%
Total gross loans, net of deferred fees	2,142,867	100.0%	1,943,525	100.0%
Less – allowance for loan losses	(44,149)		(16,642)	
Total loans, net	$ 2,098,718		$ 1,926,883	

The composition of gross loans by rate type is as follows:

(dollars in thousands)	2020	December 31, 2019
Floating rate loans	$ 400,506	$ 432,540
Fixed rate loans	1,742,361	1,510,985
	$ 2,142,867	$ 1,943,525

At December 31, 2020, approximately $868.5 million of the Company's mortgage loans were pledged as collateral for advances from the FHLB, as set forth in Note 10.

Credit Quality Indicators

Commercial
We manage a consistent process for assessing commercial loan credit quality by monitoring our loan grading trends and past due statistics. All loans are subject to individual risk assessment. Our risk categories include Pass, Special Mention, Substandard, and Doubtful, each of which is defined by banking regulatory agencies. Delinquency statistics are also an important indicator of credit quality in the establishment of our allowance for credit losses.

We categorize our loans into risk categories based on relevant information about the ability of the borrower to service their debt such as current financial information, historical payment experience, credit documentation, public information, and current economic trends, among other factors. A description of the general characteristics of the risk grades is as follows:

- Pass—These loans range from minimal credit risk to average however still acceptable credit risk.
- Special mention—A special mention loan has potential weaknesses that deserve management's close attention. If left uncorrected, these potential weaknesses may result in deterioration of the repayment prospects for the loan or the institution's credit position at some future date.
- Substandard—A substandard loan is inadequately protected by the current sound worth and paying capacity of the obligor or of the collateral pledged, if any. Loans so classified must have a well-defined weakness, or weaknesses, that may jeopardize the liquidation of the debt. A substandard loan is characterized by the distinct possibility that the Bank will sustain some loss if the deficiencies are not corrected.

- Doubtful—A doubtful loan has all of the weaknesses inherent in one classified as substandard with the added characteristic that the weaknesses make collection or liquidation in full, on the basis of the currently existing facts, conditions and values, highly questionable and improbable.

The following tables provide past due information for outstanding commercial loans and include loans on nonaccrual status.

						December 31, 2020
(dollars in thousands)		Owner occupied RE	Non-owner occupied RE	Construction	Business	Total
Current	$	432,711	584,565	61,467	307,261	1,386,004
30-59 days past due		403	282	-	35	720
60-89 days past due		-	-	-	266	266
Greater than 90 days		206	422	-	37	665
	$	433,320	585,269	61,467	307,599	1,387,655

						December 31, 2019
		Owner occupied RE	Non-owner occupied RE	Construction	Business	Total
Current	$	406,594	501,676	80,486	307,710	1,296,466
30-59 days past due		706	151	-	178	1,035
60-89 days past due		-	-	-	-	-
Greater than 90 days		551	51	-	235	837
	$	407,851	501,878	80,486	308,123	1,298,338

As of December 31, 2020 and 2019, loans 30 days or more past due represented 0.17% and 0.23% of our total loan portfolio, respectively. Commercial loans 30 days or more past due were 0.08% and 0.10% as of December 31, 2020 and 2019, respectively.

The tables below provide a breakdown of outstanding commercial loans by risk category.

						December 31, 2020
(dollars in thousands)		Owner occupied RE	Non-owner occupied RE	Construction	Business	Total
Pass	$	430,291	576,095	61,328	301,838	1,369,552
Special Mention		624	587	-	1,703	2,914
Substandard		2,405	8,587	139	4,058	15,189
Doubtful		-	-	-	-	-
	$	433,320	585,269	61,467	307,599	1,387,655

						December 31, 2019
(dollars in thousands)		Owner occupied RE	Non-owner occupied RE	Construction	Business	Total
Pass	$	404,237	492,941	80,486	301,504	1,279,168
Special Mention		1,312	744	-	3,108	5,164
Substandard		2,302	8,193	-	3,511	14,006
Doubtful		-	-	-	-	-
	$	407,851	501,878	80,486	308,123	1,298,338

Consumer

We manage a consistent process for assessing consumer loan credit quality by monitoring our loan grading trends and past due statistics. All loans are subject to individual risk assessment. Our risk categories include Pass, Special Mention, Substandard, and Doubtful, which are defined above. Delinquency statistics are also an important indicator of credit quality in the establishment of our allowance for loan losses.

The following tables provide past due information for outstanding consumer loans and include loans on nonaccrual status.

(dollars in thousands)		Real estate	Home equity	Construction	Other	December 31, 2020 Total
Current	$	534,648	156,657	40,525	21,419	753,249
30-59 days past due		-	-	-	-	-
60-89 days past due		332	-	-	-	332
Greater than 90 days		1,331	300	-	-	1,631
	$	536,311	156,957	40,525	21,419	755,212

		Real estate	Home equity	Construction	Other	December 31, 2019 Total
Current	$	396,445	179,051	41,471	25,650	642,617
30-59 days past due		799	369	-	83	1,251
60-89 days past due		-	118	-	-	118
Greater than 90 days		1,001	200	-	-	1,201
	$	398,245	179,738	41,471	25,733	645,187

Consumer loans 30 days or more past due were 0.09% and 0.13% as of December 31, 2020 and 2019, respectively.

The tables below provide a breakdown of outstanding consumer loans by risk category.

(dollars in thousands)		Real estate	Home equity	Construction	Other	December 31, 2020 Total
Pass	$	530,515	152,154	40,525	21,290	744,484
Special Mention		1,968	1,005	-	91	3,064
Substandard		3,828	3,798	-	38	7,664
Doubtful		-	-	-	-	-
	$	536,311	156,957	40,525	21,419	755,212

(dollars in thousands)		Real estate	Home equity	Construction	Other	December 31, 2019 Total
Pass	$	392,572	176,532	41,471	25,421	635,996
Special Mention		2,267	775	-	261	3,303
Substandard		3,406	2,431	-	51	5,888
Doubtful		-	-	-	-	-
	$	398,245	179,738	41,471	25,733	645,187

Nonperforming assets

The following table shows the nonperforming assets and the related percentage of nonperforming assets to total assets and gross loans. Generally, a loan is placed on nonaccrual status when it becomes 90 days past due as to principal or interest, or when we believe, after considering economic and business conditions and collection efforts, that the borrower's financial condition is such that collection of the contractual principal or interest on the loan is doubtful. A payment of interest on a loan that is classified as nonaccrual is recognized as a reduction in principal when received.

(dollars in thousands)	2020	December 31, 2019
Commercial		
Owner occupied RE	$ -	$ -
Non-owner occupied RE	1,143	188
Construction	139	-
Business	195	235
Consumer		
Real estate	2,536	1,829
Home equity	547	431
Construction	-	-
Other	-	-
Nonaccruing troubled debt restructurings	3,509	4,111
Total nonaccrual loans, including nonaccruing TDRs	8,069	6,794
Other real estate owned	1,169	-
Total nonperforming assets	$ 9,238	$ 6,794
Nonperforming assets as a percentage of:		
Total assets	0.37%	0.30%
Gross loans	0.43%	0.35%
Total loans over 90 days past due	$ 2,296	$ 2,038
Loans over 90 days past due and still accruing	-	-
Accruing TDRs	4,893	5,219

Foregone interest income on the nonaccrual loans for the year ended December 31, 2020 was approximately $61,000 and approximately $23,000 for the same period in 2019.

Impaired Loans

The table below summarizes key information for impaired loans. Our impaired loans include loans on nonaccrual status and loans modified in a TDR, whether on accrual or nonaccrual status. These impaired loans may have estimated impairment which is included in the allowance for loan losses. Our commercial and consumer impaired loans are evaluated individually to determine the related allowance for loan losses.

			December 31, 2020		
			Recorded investment		
(dollars in thousands)	Unpaid Principal Balance	Impaired loans	Impaired loans with no related allowance for loan losses	Impaired loans with related allowance for loan losses	Related allowance for loan losses
Commercial					
Owner occupied RE	$ 1,753	1,649	1,497	152	76
Non-owner occupied RE	3,212	2,188	705	1,483	366
Construction	141	139	139	-	-
Business	2,892	2,449	279	2,170	897
Total commercial	7,998	6,425	2,620	3,805	1,339
Consumer					
Real estate	4,362	4,031	3,108	923	190
Home equity	2,498	2,371	2,096	275	163
Construction	-	-	-	-	-
Other	135	135	-	135	17
Total consumer	6,995	6,537	5,204	1,333	370
Total	$ 14,993	12,962	7,824	5,138	1,709

(dollars in thousands)	Unpaid Principal Balance	Impaired loans	Recorded investment Impaired loans with no related allowance for loan losses	Impaired loans with related allowance for loan losses	December 31, 2019 Related allowance for loan losses
Commercial					
Owner occupied RE	$ 2,791	2,726	2,270	456	75
Non-owner occupied RE	4,512	4,051	2,419	1,632	465
Construction	-	-	-	-	-
Business	1,620	1,531	558	973	452
Total commercial	8,923	8,308	5,247	3,061	992
Consumer					
Real estate	2,727	2,720	1,638	1,082	364
Home equity	885	838	459	379	66
Construction	-	-	-	-	-
Other	147	147	-	147	16
Total consumer	3,759	3,705	2,097	1,608	446
Total	$ 12,682	12,013	7,344	4,669	1,438

The following table provides the average recorded investment in impaired loans and the amount of interest income recognized on impaired loans after impairment by portfolio segment and class.

					Year ended December 31,	
		2020		2019		2018
(dollars in thousands)	Average recorded investment	Recognized interest income	Average recorded investment	Recognized interest income	Average recorded investment	Recognized interest income
Commercial						
Owner occupied RE	$ 2,423	88	$ 2,739	128	2,784	142
Non-owner occupied RE	4,217	221	4,161	255	2,860	174
Construction	56	6	-	-	-	-
Business	2,306	243	1,582	79	2,883	162
Total commercial	9,002	558	8,482	462	8,527	478
Consumer						
Real estate	3,372	170	2,771	131	2,930	151
Home equity	2,128	5	853	42	1,453	99
Construction	-	-	-	-	-	-
Other	141	79	153	5	174	5
Total consumer	5,641	254	3,777	178	4,557	255
Total	$ 14,643	812	$ 12,259	640	13,084	733

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Allowance for Loan Losses

The following table summarizes the activity related to our allowance for loan losses:

(dollars in thousands)	2020	Year ended December 31, 2019	2018
Balance, beginning of period	$ 16,642	$ 15,762	15,523
Provision for loan losses	29,600	2,300	1,900
Loan charge-offs:			
Commercial			
Owner occupied RE	(94)	(110)	-
Non-owner occupied RE	(1,508)	(239)	(432)
Construction	-	-	-
Business	(1,309)	(910)	(695)
Total commercial	(2,911)	(1,259)	(1,127)
Consumer			
Real estate	(134)	-	(749)
Home equity	(299)	(174)	(217)
Construction	-	-	-
Other	(70)	(82)	(53)
Total consumer	(503)	(256)	(1,019)
Total loan charge-offs	(3,414)	(1,515)	(2,146)
Loan recoveries:			
Commercial			
Owner occupied RE	65	-	-
Non-owner occupied RE	670	2	132
Construction	-	-	-
Business	470	43	229
Total commercial	1,205	45	361
Consumer			
Real estate	18	37	5
Home equity	69	2	115
Construction	-	-	-
Other	29	11	4
Total consumer	116	50	124
Total recoveries	1,321	95	485
Net loan charge-offs	(2,093)	(1,420)	(1,661)
Balance, end of period	$ 44,149	$ 16,642	15,762

The following tables summarize the activity in the allowance for loan losses by our commercial and consumer portfolio segments.

(dollars in thousands)	Commercial	Year ended December 31, 2020 Consumer	Total
Balance, beginning of period	$ 11,372	5,270	16,642
Provision	19,500	10,100	29,600
Loan charge-offs	(2,911)	(503)	(3,414)
Loan recoveries	1,205	116	1,321
Net loan charge-offs	(1,706)	(387)	(2,093)
Balance, end of period	$ 29,166	14,983	44,149

	Commercial	Year ended December 31, 2019 Consumer	Total
Balance, beginning of period	$ 10,768	4,994	15,762
Provision	1,818	482	2,300
Loan charge-offs	(1,259)	(256)	(1,515)
Loan recoveries	45	50	95
Net loan charge-offs	(1,214)	(206)	(1,420)

		Year ended December 31, 2019	
	Commercial	Consumer	Total
Balance, end of period	$ 11,372	5,270	16,642

The following table disaggregates our allowance for loan losses and recorded investment in loans by method of impairment evaluation.

				December 31, 2020		
	Allowance for loan losses			Recorded investment in loans		
(dollars in thousands)	Commercial	Consumer	Total	Commercial	Consumer	Total
Individually evaluated	$ 1,339	370	1,709	6,425	6,537	12,962
Collectively evaluated	27,826	14,614	42,440	1,381,230	748,675	2,129,905
Total	$ 29,165	14,984	44,149	1,387,655	755,212	2,142,867

				December 31, 2019		
	Allowance for loan losses			Recorded investment in loans		
(dollars in thousands)	Commercial	Consumer	Total	Commercial	Consumer	Total
Individually evaluated	$ 992	446	1,438	8,308	3,705	12,013
Collectively evaluated	10,380	4,824	15,204	1,290,030	641,482	1,931,512
Total	$ 11,372	5,270	16,642	1,298,338	645,187	1,943,525

NOTE 5 – Troubled Debt Restructurings

At December 31, 2020, we had 20 loans totaling $8.4 million and at December 31, 2019 we had 19 loans totaling $9.3 million, which we considered as TDRs. The Company considers a loan to be a TDR when the debtor experiences financial difficulties and the Company grants a concession to the debtor that it would not normally consider. Concessions can relate to the contractual interest rate, maturity date, or payment structure of the note. As part of our workout plan for individual loan relationships, we may restructure loan terms to assist borrowers facing challenges in the current economic environment.

A restructuring that results in only a delay in payments that is insignificant is not considered an economic concession. In accordance with the CARES Act, the Company implemented loan modification programs in response to the COVID-19 pandemic, and the Company elected the accounting policy in the CARES Act to not apply TDR accounting to loans modified for borrowers impacted by the COVID-19 pandemic. Under the CARES Act, the Company granted short-term loan deferrals to 864 loan clients, of which two clients remain under deferral as of December 31, 2020. In addition, short-term loan deferrals were granted to six clients with loans totaling $3.2 million at December 31, 2020, which were considered TDRs due to the client experiencing financial difficulty before the pandemic.

The following table summarizes the concession at the time of modification and the recorded investment in our TDRs before and after their modification.

						For the year ended December 31, 2020	
(dollars in thousands)	Renewals deemed a concession	Reduced or deferred payments	Converted to interest only	Maturity date extensions	Total number of loans	Pre-modification outstanding recorded investment	Post-modification outstanding recorded Investment
Commercial							
Business	1	-	-	-	1	$ 1,037	$ 1,037
Consumer							
Real estate	2	-	-	-	2	647	647
Home equity	2	-	-	-	2	1,448	1,448
Total loans	5	-	-	-	5	$ 3,132	$ 3,132

						For the year ended December 31, 2019	
	Renewals deemed a concession	Reduced or deferred payments	Converted to interest only	Maturity date extensions	Total number of loans	Pre-modification outstanding recorded investment	Post-modification outstanding recorded Investment
Commercial							
Business	1	-	-	-	1	$ 1,823	$ 1,823
Total loans	1	-	-	-	1	$ 1,823	$ 1,823

As of December 31, 2020 and 2019 there were no loans modified as TDRs for which there was a payment default (60 days past due) within 12 months of the restructuring date.

NOTE 6 – Property and Equipment

Property and equipment are stated at cost less accumulated depreciation. Components of property and equipment included in the consolidated balance sheets are as follows:

(dollars in thousands)		2020	December 31, 2019
Land	$	10,678	11,531
Buildings		21,966	24,136
Leasehold improvements		5,503	4,486
Furniture and equipment		10,459	10,219
Software		386	367
Construction in process		6,179	939
Accumulated depreciation and amortization		(13,703)	(12,705)
Property and equipment, excluding ROU assets		41,468	38,973
ROU assets		18,768	19,505
Total property and equipment	$	60,236	58,478

On October 9, 2020 we sold two of our office locations in Columbia, South Carolina and recognized a gain of $180,000 in the transaction.

Construction in process at December 31, 2020 and 2019 primarily included costs associated with the new bank headquarters building. Depreciation and amortization expense for the years ended December 31, 2020 and 2019 was $2.1 million and $1.9 million, respectively. Depreciation and amortization are charged to operations utilizing a straight-line method over the estimated useful lives of the assets. The estimated useful lives for the principal items follow:

Type of Asset	Life in Years
Software	3
Furniture and equipment	5 to 7
Leasehold improvements	5 to 15
Buildings	40

NOTE 7 – Leases

Effective January 1, 2019, the Company adopted ASU 2016-02, “Leases (Topic 842)”. Upon adoption, the Company elected practical expedients including existing leases retaining their classification as operating leases and combining lease and non-lease components. The Company also elected to not recognize right-of-use assets and lease liabilities arising from short-term leases. As of December 31, 2020, the Company leased six of our offices under various operating lease agreements. The lease agreements have maturity dates ranging from February 2022 to October 2029, some of which include options for multiple five-year extensions. The weighted average remaining life of the lease term for these leases was 7.30 years and 7.97 years as of December 31, 2020 and 2019, respectively.

The discount rate used in determining the lease liability for each individual lease was the FHLB fixed advance rate which corresponded with the remaining lease term as of January 1, 2019 for leases that existed at adoption and as of the lease commencement date for leases subsequently entered in to. The weighted average discount rate for leases was 2.70% and 2.86% as of December 31, 2020 and 2019, respectively.

Total operating lease costs were $2.4 million and $2.2 million for the years ended December 31, 2020 and 2019, respectively. The ROU asset, included in property and equipment, and lease liability, included in other liabilities, were $18.8 million and $19.5 million as of December 31, 2020, respectively, compared to $19.5 million and $20.1 million as of December 31, 2019, respectively. The ROU asset and lease liability are recognized at lease commencement by calculating the present value of lease payments over the lease term.

Maturities of lease liabilities as of December 31, 2020 were as follows:

(dollars in thousands)		Operating Leases
2021	$	2,335
2022		1,587
2023		1,462
2024		1,501
2025		1,544
Thereafter		15,886
Total undiscounted lease payments		24,315
Discount effect of cash flows		4,783
Total lease liability	$	19,532

NOTE 8 – Other Real Estate Owned

Other real estate owned is comprised of real estate acquired in settlement of loans and is included in other assets on the balance sheet. At December 31, 2020 there was one commercial property owned totaling $1.2 million compared to no other real estate owned at December 31, 2019. The following summarizes the activity in the real estate acquired in settlement of loans portion of other real estate owned:

(dollars in thousands)		For the year ended December 31, 2020		2019
Balance, beginning of year	$	-	$	-
Additions		2,198		-
Sales		-		-
Write-downs, net		(1,029)		-
Balance, end of year	$	1,169	$	-

NOTE 9 – Deposits

The following is a detail of the deposit accounts:

(dollars in thousands)		December 31, 2020	2019
Noninterest bearing	$	576,610	397,331
Interest bearing:			
NOW accounts		268,739	228,680
Money market accounts		1,042,745	898,923
Savings		27,254	16,258
Time, less than $100,000		36,454	47,941
Time, $100,000 and over		190,956	286,991
Total deposits	$	2,142,758	1,876,124

At December 31, 2020 and 2019, time deposits greater than $250,000 were $130.9 million and $220.1 million, respectively.

Also, at December 31, 2020 and 2019, the Company had approximately $22.0 million and $67.4 million, respectively, of time deposits that were obtained outside of the Company’s primary market. Interest expense on time deposits greater than $100,000 was $4.6 million for the year ended December 31, 2020, $6.9 million for the year ended December 31, 2019, and $4.7 million for the year ended December 31, 2018.

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At December 31, 2020 the scheduled maturities of certificates of deposit are as follows:

(dollars in thousands)		
2021	$	200,657
2022		13,244
2023		8,373
2024		2,370
2025 and after		2,766
	$	227,410

NOTE 10 – Federal Home Loan Bank Advances and Other Borrowings

At December 31, 2020 and 2019, the Company had $25.0 million and $110.0 million in FHLB Advances, respectively. The FHLB advances are secured with approximately $868.5 million of mortgage loans and $3.1 million of stock in the FHLB.

Listed below is a summary of the terms and maturities of the advances outstanding at December 31, 2020 and 2019. The $25.0 million outstanding at December 31, 2020 was at a variable rate.

(dollars in thousands)			2020			December 31, 2019
Maturity		**Amount**	**Rate**		**Amount**	**Rate**
December 31, 2020	$	-	-%	$	110,000	1.78%
December 31, 2021		25,000	0.36%		-	-%
	$	25,000	0.36%	$	110,000	1.78%

The Company also has an unsecured, interest only line of credit for $15 million with another financial institution which was unused at December 31, 2020. The line of credit bears interest at LIBOR plus 3.50% and matures on December 31, 2021. The loan agreement contains various financial covenants related to capital, earnings and asset quality.

NOTE 11 – Subordinated Debentures

On June 26, 2003, Greenville First Statutory Trust I (a non-consolidated subsidiary) issued $6.0 million floating rate trust preferred securities with a maturity of June 26, 2033. At December 31, 2020, the interest rate was 3.35% and is indexed to the 3-month LIBOR rate plus 3.10% and adjusted quarterly. The Company received from the Trust the $6.0 million proceeds from the issuance of the securities and the $186,000 initial proceeds from the capital investment in the Trust, and accordingly has shown the funds due to the Trust as $6.2 million junior subordinated debentures.

On December 22, 2005, Greenville First Statutory Trust II (a non-consolidated subsidiary) issued $7.0 million floating rate trust preferred securities with a maturity of December 22, 2035. At December 31, 2020, the interest rate was 1.68% and is indexed to the 3-month LIBOR rate plus 1.44% and adjusted quarterly. The Company received from the Trust the $7.0 million proceeds from the issuance of the securities and the $217,000 initial proceeds from the capital investment in the Trust, and accordingly has shown the funds due to the Trust as $7.2 million junior subordinated debentures.

The current regulatory rules allow certain amounts of junior subordinated debentures to be included in the calculation of regulatory capital. However, provisions within the Dodd-Frank Act prohibit institutions that had more than $15 billion in assets on December 31, 2009 from including trust preferred securities as Tier 1 capital beginning in 2013, with one-third phased out over the two years ending in 2015. Financial institutions with less than $15 billion in total assets, such as the Bank, may continue to include their trust preferred securities issued prior to May 19, 2010 in Tier 1 capital, but cannot include in Tier 1 capital trust preferred securities issued after such date.

On September 30, 2019, the Company entered into Subordinated Note Purchase Agreements (collectively, the “Purchase Agreement”) with certain qualified institutional buyers and accredited investors (the “Purchasers”) pursuant to which the Company sold and issued $23.0 million in aggregate principal amount of its 4.75% Fixed-to-Floating Rate Subordinated Notes due 2029 (the “Notes”). The Notes were offered and sold by the Company to eligible purchasers in a private offering in reliance on the exemption from the registration requirements of Section 4(a)(2) of the Securities Act of 1933, as amended (the “Securities Act”) and the provisions of Regulation D promulgated thereunder (the “Private Placement”). The Company intends to use the proceeds from the offering, which were approximately $22.5 million, for general corporate purposes, including providing capital to the Bank and supporting organic growth.

The Notes have a ten-year term and, from and including the date of issuance to but excluding September 30, 2024, will bear interest at a fixed annual rate of 4.75%, payable semi-annually in arrears, for the first five years of the term. From and including September 30, 2024 to but excluding the maturity date or early redemption date, the interest rate shall reset quarterly to an interest rate per annum equal to a benchmark rate (which is expected to be Three-Month Term SOFR) plus 340.8 basis points, payable quarterly in arrears. As provided in the Notes, the interest rate on the Notes during the applicable floating rate period may be determined based on a rate other than Three-Month Term SOFR.

The Notes are redeemable, in whole or in part, on September 30, 2024, on any interest payment date thereafter, and at any time upon the occurrence of certain events. The Purchase Agreement contains certain customary representations, warranties and covenants made by the Company, on the one hand, and the Purchasers, severally and not jointly, on the other hand.

On September 30, 2019, in connection with the sale and issuance of the Notes, the Company entered into a Registration Rights Agreement (the “Registration Rights Agreement”) with the Purchasers. Under the terms of the Registration Rights Agreement, the Company has agreed to take certain actions to provide for the exchange of the Notes for subordinated notes that are registered under the Securities Act and have substantially the same terms as the Notes (the “Exchange Notes”). Under certain circumstances, if the Company fails to meet its obligations under the Registration Rights Agreement, it would be required to pay additional interest to the holders of the Notes.

The Notes were issued under an Indenture, dated September 30, 2019 (the “Indenture”), by and between the Company and UMB Bank, National Association, as trustee. The Notes are not subject to any sinking fund and are not convertible into or, other than with respect to the Exchange Notes, exchangeable for any other securities or assets of the Company or any of its subsidiaries. The Notes are not subject to redemption at the option of the holder. The Notes are unsecured, subordinated obligations of the Company only and are not obligations of, and are not guaranteed by, any subsidiary of the Company. The Notes rank junior in right to payment to the Company’s current and future senior indebtedness. The Notes are intended to qualify as Tier 2 capital for regulatory capital purposes for the Company.

NOTE 12 – Unused Lines of Credit

At December 31, 2020, the Company had five lines of credit to purchase federal funds that totaled $118.5 million which were unused at December 31, 2020. The lines of credit are available on a one to 14 day basis for general corporate purposes of the Company. The lender has reserved the right to withdraw the line at their option. The Company has an additional line of credit with the FHLB to borrow funds, subject to a pledge of qualified collateral. The Company has collateral that would support approximately $512.5 million in additional borrowings with the FHLB at December 31, 2020.

NOTE 13 – Derivative Financial Instruments

The Company utilizes derivative financial instruments primarily to hedge its exposure to changes in interest rates. All derivative financial instruments are recognized as either assets or liabilities and measured at fair value. The Company accounts for all of its derivatives as free-standing derivatives and does not designate any of these instruments for hedge accounting. Therefore, the gain or loss resulting from the change in the fair value of the derivative is recognized in the Company’s statement of income during the period of change.

The Company enters into commitments to originate residential mortgage loans held for sale, at specified interest rates and within a specified period of time, with clients who have applied for a loan and meet certain credit and underwriting criteria (interest rate lock commitments). These interest rate lock commitments (“IRLCs”) meet the definition of a derivative financial instrument and are reflected in the balance sheet at fair value with changes in fair value recognized in current period earnings. Unrealized gains and losses on the IRLCs are recorded as derivative assets and derivative liabilities, respectively, and are measured based on the value of the underlying mortgage loan, quoted mortgage-backed securities (“MBS”) prices and an estimate of the probability that the mortgage loan will fund within the terms of the interest rate lock commitment, net of estimated commission expenses.

The Company manages the interest rate and price risk associated with its outstanding IRLCs and mortgage loans held for sale by entering into derivative instruments such as forward sales of MBS. Management expects these derivatives will experience changes in fair value opposite to changes in fair value of the IRLCs and mortgage loans held for sale, thereby reducing earnings volatility. The Company takes into account various factors and strategies in determining the portion of the mortgage pipeline (IRLCs and mortgage loans held for sale) it wants to economically hedge.

The following table summarizes the Company's outstanding financial derivative instruments at December 31, 2020 and December 31, 2019.

(dollars in thousands)		Notional	Balance Sheet Location		December 31, 2020 Fair Value Asset/(Liability)
Mortgage loan interest rate lock commitments	$	107,569	Other assets	$	2,385
MBS forward sales commitments		75,500	Other liabilities		(501)
Total derivative financial instruments	$	183,069		$	1,884

		Notional	Balance Sheet Location		December 31, 2019 Fair Value Asset/(Liability)
Mortgage loan interest rate lock commitments	$	26,446	Other assets	$	344
MBS forward sales commitments		20,500	Other liabilities		(39)
Total derivative financial instruments	$	46,946		$	305

NOTE 14 – Fair Value Accounting

FASB ASC 820, "Fair Value Measurement and Disclosures Topic," defines fair value as the exchange price that would be received for an asset or paid to transfer a liability (an exit price) in the principal or most advantageous market for the asset or liability in an orderly transaction between market participants on the measurement date. FASB ASC 820 also establishes a fair value hierarchy which requires an entity to maximize the use of observable inputs and minimize the use of unobservable inputs when measuring fair value. The standard describes three levels of inputs that may be used to measure fair value:

Level 1 – Quoted market price in active markets
Quoted prices in active markets for identical assets or liabilities. Level 1 assets and liabilities include certain debt and equity securities that are traded in an active exchange market.
Level 2 – Significant other observable inputs
Observable inputs other than Level 1 prices such as quoted prices for similar assets or liabilities; quoted prices in markets that are not active; or other inputs that are observable or can be corroborated by observable market data for substantially the full term of the assets or liabilities. Level 2 assets and liabilities include fixed income securities and mortgage-backed securities that are held in the Company's available-for-sale portfolio and valued by a third-party pricing service, as well as certain impaired loans.
Level 3 – Significant unobservable inputs
Unobservable inputs that are supported by little or no market activity and that are significant to the fair value of the assets or liabilities. Level 3 assets and liabilities include financial instruments whose value is determined using pricing models, discounted cash flow methodologies, or similar techniques, as well as instruments for which the determination of fair value requires significant management judgment or estimation. These methodologies may result in a significant portion of the fair value being derived from unobservable data.

Fair Value of Financial Instruments
Financial instruments require disclosure of fair value information, whether or not recognized in the consolidated balance sheets, when it is practical to estimate the fair value. A financial instrument is defined as cash, evidence of an ownership interest in an entity or a contractual obligation which requires the exchange of cash. Certain items are specifically excluded from the disclosure requirements, including the Company's common stock, premises and equipment and other assets and liabilities.

The following is a description of valuation methodologies used to estimate fair value for assets recorded at fair value. Fair value approximates carrying value for the following financial instruments due to the short-term nature of the instrument: cash and due from banks, federal funds sold, other investments, federal funds purchased, and securities sold under agreement to repurchase.

Investment Securities
Securities available for sale are valued on a recurring basis at quoted market prices where available. If quoted market prices are not available, fair values are based on quoted market prices of comparable securities. Level 1 securities include those traded on an active exchange, such as the New York Stock Exchange or U.S. Treasury securities that are traded by dealers or brokers in active over-the-counter markets and money market funds. Level 2 securities include mortgage-backed securities and debentures issued by government sponsored entities, municipal bonds and corporate debt securities. In certain cases where there is limited activity or less transparency around inputs to valuations, securities are classified as Level 3 within the valuation hierarchy. Securities held to maturity are valued at quoted market prices or dealer quotes similar to securities available for sale. The carrying value of Other Investments, such as Federal Reserve Bank and FHLB stock, approximates fair value based on their redemption provisions.

Mortgage Loans Held for Sale
Loans held for sale include mortgage loans which are saleable into the secondary mortgage markets and their fair values are estimated using observable quoted market or contracted prices or market price equivalents, which would be used by other market participants. These saleable loans are considered Level 2.

Impaired Loans
The Company does not record loans at fair value on a recurring basis. However, from time to time, a loan may be considered impaired and an allowance for loan losses may be established. Loans for which it is probable that payment of interest and principal will not be made in accordance with the contractual terms of the loan agreement are considered impaired. Once a loan is identified as individually impaired, management measures the impairment in accordance with FASB ASC 310, “Receivables.” The fair value of impaired loans is estimated using one of several methods, including collateral value, market value of similar debt, enterprise value, liquidation value and discounted cash flows. 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. In accordance with FASB ASC 820, “Fair Value Measurement and Disclosures,” impaired loans where an allowance is established based on the fair value of collateral require classification in the fair value hierarchy. When the fair value of the collateral is based on an observable market price or a current appraised value, the Company considers the impaired loan as nonrecurring Level 2. The Company’s current loan and appraisal policies require the Company to obtain updated appraisals on an “as is” basis at renewal, or in the case of an impaired loan, on an annual basis, either through a new external appraisal or an appraisal evaluation. When an appraised value is not available or management determines the fair value of the collateral is further impaired below the appraised value and there is no observable market price, the Company considers the impaired loan as nonrecurring Level 3. The fair value of impaired loans may also be estimated using the present value of expected future cash flows to be realized on the loan, which is also considered a Level 3 valuation. These fair value estimates are subject to fluctuations in assumptions about the amount and timing of expected cash flows as well as the choice of discount rate used in the present value calculation.

Other Real Estate Owned
OREO, consisting of properties obtained through foreclosure or in satisfaction of loans, is reported at the lower of cost or fair value, determined on the basis of current appraisals, comparable sales, and other estimates of value obtained principally from independent sources, adjusted for estimated selling costs (Level 2). At the time of foreclosure, any excess of the loan balance over the fair value of the real estate held as collateral is treated as a charge against the allowance for loan losses. Gains or losses on sale and generally any subsequent adjustments to the value are recorded as a component of real estate owned activity. When an appraised value is not available or management determines the fair value of the collateral is further impaired below the appraised value and there is no observable market price, the Company considers the OREO as nonrecurring Level 3.

Derivative Financial Instruments
The Company estimates the fair value of IRLCs based on the value of the underlying mortgage loan, quoted MBS prices and an estimate of the probability that the mortgage loan will fund within the terms of the IRLC, net of commission expenses (Level 2). The Company estimates the fair value of forward sales commitments based on quoted MBS prices (Level 2).

Assets and Liabilities Recorded at Fair Value on a Recurring Basis
The tables below present the recorded amount of assets and liabilities measured at fair value on a recurring basis.

(dollars in thousands)	Level 1	Level 2	Level 3	December 31, 2020 Total
Assets				
Securities available for sale:				
US government agencies	$ -	6,493	-	6,493
SBA securities	-	485	-	485
State and political subdivisions	-	19,388	-	19,388
Asset-backed securities	-	11,529	-	11,529
Mortgage-backed securities	-	56,834	-	56,834
Mortgage loans held for sale	-	60,257	-	60,257
Mortgage loan interest rate lock commitments	-	2,385	-	2,385
Total assets measured at fair value on a recurring basis	$ -	157,371	-	157,371
Liabilities				
MBS forward sales commitments	$ -	501	-	501
Total liabilities measured at fair value on a recurring basis	$ -	501	-	501

(dollars in thousands)	Level 1	Level 2	Level 3	December 31, 2019 Total
Assets				
Securities available for sale:				
US government agencies	$ -	499	-	499
SBA securities	-	531	-	531
State and political subdivisions	-	4,184	-	4,184
Asset-backed securities	-	13,167	-	13,167
Mortgage-backed securities	-	49,313	-	49,313
Mortgage loans held for sale	-	27,046	-	27,046
Mortgage loan interest rate lock commitments	-	344	-	344
Total assets measured at fair value on a recurring basis	$ -	95,084	-	95,084
Liabilities				
MBS forward sales commitments	$ -	39	-	39
Total liabilities measured at fair value on a recurring basis	$ -	39	-	39

Assets and Liabilities Recorded at Fair Value on a Nonrecurring Basis
The Company is predominantly an asset based lender with real estate serving as collateral on approximately 85% of loans as of December 31, 2020. Loans which are deemed to be impaired are valued net of the allowance for loan losses, and other real estate owned is valued at the lower of cost or net realizable value of the underlying real estate collateral. Such market values are generally obtained using independent appraisals, which the Company considers to be level 2 inputs. The tables below present the recorded amount of assets and liabilities measured at fair value on a nonrecurring basis.

(dollars in thousands)	Level 1	Level 2	Level 3	December 31, 2020 Total
Assets				
Impaired loans	$ -	8,144	3,109	11,253
Other real estate owned	-	1,169	-	1,169
Total assets measured at fair value on a nonrecurring basis	$ -	9,313	3,109	12,422

	Level 1	Level 2	Level 3	December 31, 2019 Total
Assets				
Impaired loans	$ -	5,634	4,941	10,575
Total assets measured at fair value on a nonrecurring basis	$ -	5,634	4,941	10,575

The Company had no liabilities carried at fair value or measured at fair value on a nonrecurring basis.

For Level 3 assets and liabilities measured at fair value on a recurring or nonrecurring basis as of December 31, 2020, the significant unobservable inputs used in the fair value measurements were as follows:

	Valuation Technique	Significant Unobservable Inputs	Range of Inputs
Impaired loans	Appraised Value/Discounted Cash Flows	Discounts to appraisals or cash flows for estimated holding and/or selling costs or age of appraisal	0-25%
Other real estate owned	Appraised Value/Comparable Sales	Discounts to appraisals for estimated holding or selling costs	0-25%

Fair Value of Financial Instruments
Financial instruments require disclosure of fair value information, whether or not recognized in the consolidated balance sheets, when it is practical to estimate the fair value. A financial instrument is defined as cash, evidence of an ownership interest in an entity or a contractual obligation which requires the exchange of cash. Certain items are specifically excluded from the disclosure requirements, including the Company's common stock, premises and equipment and other assets and liabilities.

The following is a description of valuation methodologies used to estimate fair value for certain other financial instruments.

Fair value approximates carrying value for the following financial instruments due to the short-term nature of the instrument: cash and due from banks, federal funds sold, other investments, federal funds purchased, and securities sold under agreement to repurchase.

Loans – The valuation of loans held for investment is estimated using the exit price notion which incorporates factors, such as enhanced credit risk, illiquidity risk and market factors that sometimes exist in exit prices in dislocated markets. This credit risk assumption is intended to approximate the fair value that a market participant would realize in a hypothetical orderly transaction. The Company's loan portfolio is initially fair valued using a segmented approach, using the eight categories as disclosed in Note 4 – Loans and Allowance for Loan Losses. Loans are considered a Level 3 classification.

Deposits – Fair value for demand deposit accounts and interest-bearing accounts with no fixed maturity date is equal to the carrying value. The fair value of certificate of deposit accounts are estimated by discounting cash flows from expected maturities using current interest rates on similar instruments.

FHLB Advances and Other Borrowings – Fair value for FHLB advances and other borrowings are estimated by discounting cash flows from expected maturities using current interest rates on similar instruments.

Subordinated debentures – Fair value for subordinated debentures are estimated by discounting cash flows from expected maturities using current interest rates on similar instruments.

The Company has used management's best estimate of fair value based on the above assumptions. Thus, the fair values presented may not be the amounts that could be realized in an immediate sale or settlement of the instrument. In addition, any income taxes or other expenses, which would be incurred in an actual sale or settlement, are not taken into consideration in the fair value presented.

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The estimated fair values of the Company's financial instruments at December 31, 2020 and 2019 are as follows:

					December 31, 2020
(dollars in thousands)	Carrying Amount	Fair Value	Level 1	Level 2	Level 3
Financial Assets:					
Other investments, at cost	$ 3,635	3,635	-	-	3,635
Loans[(1)]	2,085,756	2,060,698	-	-	2,060,698
Financial Liabilities:					
Deposits	2,142,758	2,008,317	-	2,008,317	-
FHLB and other borrowings	25,000	24,972	-	24,972	-
Subordinated debentures	35,998	30,371	-	30,371	-

					December 31, 2019
(dollars in thousands)	Carrying Amount	Fair Value	Level 1	Level 2	Level 3
Financial Assets:					
Other investments, at cost	$ 6,948	6,948	-	-	6,948
Loans[(1)]	1,914,870	1,900,216	-	-	1,900,216
Financial Liabilities:					
Deposits	1,876,124	1,772,121	-	1,772,121	-
FHLB and other borrowings	110,000	109,737	-	109,737	-
Subordinated debentures	35,890	33,250	-	33,250	-

(1) Carrying amount is net of the allowance for loan losses and previously presented impaired loans.

NOTE 15 – Earnings Per Common Share

The following schedule reconciles the numerators and denominators of the basic and diluted earnings per share computations for the years ended December 31, 2020, 2019 and 2018. Dilutive common shares arise from the potentially dilutive effect of the Company's stock options and warrants that are outstanding. The assumed conversion of stock options and warrants can create a difference between basic and dilutive net income per common share.

At December 31, 2020, 2019 and 2018, options totaling 318,825, 94,885, and 195,425, respectively, were anti-dilutive in the calculation of earnings per share as their exercise price exceeded the fair market value. These options were therefore excluded from the diluted earnings per share calculation.

			December 31,
(dollars in thousands, except share data)	2020	2019	2018
Numerator:			
Net income	$ 18,328	$ 27,858	$ 22,289
Net income available to common shareholders	$ 18,328	$ 27,858	$ 22,289
Denominator:			
Weighted-average common shares outstanding - basic	7,718,615	7,528,283	7,384,200
Common stock equivalents	105,599	244,261	353,295
Weighted-average common shares outstanding - diluted	7,824,214	7,772,544	7,737,495
Earnings per common share:			
Basic	$ 2.37	$ 3.70	$ 3.02
Diluted	$ 2.34	$ 3.58	$ 2.88

NOTE 16 – Commitments and Contingencies

The Company has entered into a three year employment agreement with its chief executive officer and a two year employment agreement with 10 executive vice presidents. These agreements also include a) an incentive program, b) a stock option plan, c) a one-year non-compete agreement upon termination and a severance payment equal to one year of compensation. The total estimated aggregate salary commitment is approximately $3.0 million.

The Company has an agreement with a data processor which expires in 2023 to provide certain item processing, electronic banking, and general ledger processing services. Components of this contract vary based on transaction and account volume, monthly charges and certain termination fees.

At December 31, 2020, the Company has a contract with a construction company for $28.2 million to construct a new bank headquarters in Greenville, South Carolina.

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The Company may be subject to litigation and claims in the normal course of business. As of December 31, 2020, management believes there is no material litigation pending.

NOTE 17 – Income Taxes

The components of income tax expense were as follows:

		For the years ended December 31,	
(dollars in thousands)	2020	2019	2018
Current income taxes:			
Federal	$ 10,244	6,791	5,536
State	841	1,250	990
Total current tax expense	11,085	8,041	6,526
Deferred income tax expense (benefit)	(5,594)	(420)	(125)
Income tax expense	$ 5,491	7,621	6,401

The following is a summary of the items that caused recorded income taxes to differ from taxes computed using the statutory tax rate:

		For the years ended December 31,	
(dollars in thousands)	2020	2019	2018
Tax expense at statutory rate	$ 5,002	7,451	6,025
Effect of state income taxes, net of federal benefit	664	987	782
Exempt income	(27)	(26)	(34)
Effect of stock-based compensation	(30)	(693)	(248)
Other	(118)	(98)	(124)
Income tax expense	$ 5,491	7,621	6,401

The components of the deferred tax assets and liabilities are as follows:

		December 31,
(dollars in thousands)	2020	2019
Deferred tax assets:		
Allowance for loan losses	$ 9,271	3,495
Unrealized loss on securities available for sale	-	79
Net deferred loan fees	812	697
Deferred compensation	1,728	1,404
Write-down of real estate owned	216	-
Lease liabilities	4,102	4,219
Other	187	234
	16,316	10,128
Deferred tax liabilities:		
Property and equipment	1,610	1,398
Unrealized gain on securities available for sale	272	-
Hedging transactions	855	227
Prepaid expenses	120	132
ROU assets	3,941	4,096
	6,798	5,853
Net deferred tax asset	$ 9,518	4,275

The Company has analyzed the tax positions taken or expected to be taken in its tax returns and concluded it has no liability related to uncertain tax positions.

NOTE 18 – Related Party Transactions

Certain directors, executive officers, and companies with which they are affiliated, are clients of and have banking transactions with the Company in the ordinary course of business. These loans were made on substantially the same terms, including interest rates and collateral, as those prevailing at the time for comparable transactions with persons not related to the lender.

A summary of loan transactions with directors and executive officers, including their affiliates is as follows:

	For the years ended December 31,		
(dollars in thousands)		2020	2019
Balance, beginning of year	$	10,891	13,969
New loans		4,389	6,709
Less loan payments		(9,490)	(9,787)
Balance, end of year	$	5,790	10,891

Deposits by executive officers and directors and their related interests at December 31, 2020 and 2019, were $5.1 million and $2.5 million, respectively.

The Company has a land lease with a director on the property for a branch office, with monthly payments of $9,311. In addition, the Company periodically enters into various consulting agreements with the director for development, administration and advisory services related to the purchase of property and construction of current and future branch office sites, including the development of the new bank headquarters in Greenville, South Carolina. Payments totaling $600,000 were made to the director for these services during the years ended December 31, 2019 and 2020.

The Company is of the opinion that the lease payments and consulting fees represent market costs that could have been obtained in similar “arms length” transactions.

NOTE 19 – Financial Instruments With Off-Balance Sheet Risk

In the ordinary course of business, and to meet the financing needs of its clients, the Company is a party to various financial instruments with off-balance sheet risk. These financial instruments, which include commitments to extend credit and standby letters of credit, involve, to varying degrees, elements of credit and interest rate risk in excess of the amounts recognized in the balance sheets. The contract amount of those instruments reflects the extent of involvement the Company has in particular classes of financial instruments.

The Company’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 amounts of those instruments. The Company uses the same credit policies in making commitments and conditional obligations as it does for on-balance sheet instruments.

Commitments to extend credit are agreements to lend to a client as long as there is no violation of any material condition established in the contract. Commitments generally have fixed expiration dates or other termination clauses and may require the payment of a fee. At December 31, 2020, unfunded commitments to extend credit were approximately $480.1 million, of which $114.6 million is at fixed rates and $365.5 million is at variable rates. At December 31, 2019, unfunded commitments to extend credit were approximately $426.6 million, of which $105.0 million is at fixed rates and $321.6 million is at variable rates. The Company evaluates each client’s credit-worthiness on a case-by-case basis. The amount of collateral obtained, if deemed necessary by the Company upon extension of credit, is based on management’s credit evaluation of the borrower. Collateral varies but may include accounts receivable, inventory, property, plant and equipment, and commercial and residential real estate.

At December 31, 2020 and 2019, there was a $8.7 million and $9.9 million commitment, respectively, under letters of credit. The credit risk involved in issuing letters of credit is essentially the same as that involved in extending loan facilities to clients. Collateral varies but may include accounts receivable, inventory, equipment, marketable securities and property. Since most of the letters of credit are expected to expire without being drawn upon, they do not necessarily represent future cash requirements. The fair value of off balance sheet lending commitments are based on fees currently charged to enter into similar agreements, taking into account the remaining terms of the agreements and the counterparties credit standing. The total fair value of such instruments is not material.

NOTE 20 – Employee Benefit Plan

On January 1, 2000, the Company adopted the Southern First Bancshares, Inc. Profit Sharing and 401(k) Plan for the benefit of all eligible employees. The Company contributes to the Plan annually upon approval by the Board of Directors. Contributions made to the Plan for the years ended December 31, 2020, 2019, and 2018 amounted to $881,000, $693,000, and $587,000, respectively.

The Company also provides a nonqualified deferred compensation plan for 26 executive officers in the form of a Supplemental Executive Retirement Plan (“SERP”). The SERP provides retirement income for these officers. As of December 31, 2020 and 2019, the Company had an accrued benefit obligation of $8.2 million and $6.7 million, respectively. The Company incurred expenses related to this plan of $1.6 million, $657,000, and $940,000 in 2020, 2019, and 2018, respectively.

NOTE 21 – Stock-Based Compensation

Compensation cost is recognized for stock options and restricted stock awards issued to employees and non-employee directors. Compensation cost is measured as the fair value of these awards on their date of grant. A Black-Scholes model is utilized to estimate the fair value of stock options, while the market price of the Company’s common stock at the date of grant is used as the fair value of restricted stock awards. Compensation cost is recognized over the required service period, generally defined as the vesting period for stock option and restricted stock awards.

The Company’s stock incentive programs are long-term retention programs intended to attract, retain, and provide incentives for key employees and non-employee directors in the form of incentive and non-qualified stock options and restricted stock.

Stock-based compensation expense was recorded as follows:

		For the years ended December 31,		
(dollars in thousands)		**2020**	**2019**	**2018**
Stock option expense	$	1,017	1,270	1,183
Restricted stock grant expense		380	428	319
Total stock-based compensation expense	$	1,397	1,698	1,502

Stock Options

The Company’s 2010 Incentive Plan, as amended, had available for issuance a total of 566,025 shares (adjusted for the 10% stock dividends in 2013, 2012, and 2011). The Plan expired on March 16, 2020 and no further shares may be issued from the plan.

On March 15, 2016, the Company adopted the 2016 Equity Incentive Plan, making available for issuance 400,000 stock options. The options may be exercised at an exercise price per share based on the fair market value and determined on the date of grant and expire 10 years from the grant date. As of December 31, 2020, there were 123,827 options available for grant under the 2016 Equity Incentive Plan.

On March 17, 2020, the Company adopted the 2020 Equity Incentive Plan, making available for issuance up to 450,000 stock options. The options may be exercised at an exercise price per share based on the fair market value and determined on the date of grant and expire 10 years from the grant date. As of December 31, 2020, there were no shares issued under this plan.

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A summary of the status of the stock option plan and changes for the period is presented below:

	For the years ended December 31,								
			2020			2019			2018
	Shares	Weighted average exercise price	Weighted Average Remaining Contractual Life	Shares	Weighted average exercise price	Weighted Average Remaining Contractual Life	Shares	Weighted average exercise price	Weighted Average Remaining Contractual Life
Outstanding at beginning of year	541,414	$ 26.65		648,311	$ 20.74		662,841	$ 15.70	
Granted	101,700	37.77		101,350	32.81		94,700	43.13	
Exercised	(93,870)	14.79		(191,497)	9.24		(105,630)	8.51	
Forfeited or expired	(54,049)	38.15		(16,750)	34.01		(3,600)	40.03	
Outstanding at end of year	495,195	$ 29.93	6.4 years	541,414	$ 26.65	6.3 years	648,311	$ 20.74	5.6 years
Options exercisable at year-end	287,548	$ 24.93	5.0 years	305,991	$ 20.00	4.9 years	404,851	$ 12.58	4.0 years
Weighted average fair value of options granted during the year		$ 11.37			$ 11.81			$ 16.76	
Shares available for grant	136,339			183,990			270,090		

The aggregate intrinsic value (the difference between the Company's closing stock price on the last trading day of the year and the exercise price, multiplied by the number of in-the-money options) of 495,570 and 541,414 stock options outstanding at December 31, 2020 and 2019 was $3.7 million and $8.6 million, respectively. The aggregate intrinsic value of 287,548 and 305,991 stock options exercisable at December 31, 2020 and 2019 was $3.3 million and $6.9 million, respectively.

The fair value of the option grant is estimated on the date of grant using the Black-Scholes option-pricing model. The following assumptions were used for grants:

	2020	2019	2018
Dividend yield	-	-	-
Expected life	7 years	7 years	7 years
Expected volatility	25.51%	28.21%	32.07%
Risk-free interest rate	1.29%	2.59%	2.50%

At December 31, 2020, there was $1.6 million of total unrecognized compensation cost related to nonvested stock option grants. The cost is expected to be recognized over a weighted-average period of 2.5 years. The fair value of stock option grants that vested during 2020, 2019, and 2018 was $1.2 million, $1.2 million and $973,000, respectively.

Restricted Stock Grants

On May 17, 2016, the Company adopted the 2016 Equity Incentive Plan which included a provision for the issuance of 50,000 shares of common stock to be issuable as restricted stock grants. As of December 31, 2020, 25,524 shares of restricted stock were available for grant.

On May 12, 2020, the Company adopted the 2020 Equity Incentive Plan which included a provision for the issuance of 450,000 shares of common stock to be issuable as either stock options or restricted stock grants. As of December 31, 2020, there were no issuances of stock options or restricted stock under this plan.

Shares of restricted stock granted to employees under the stock plans are subject to restrictions as to continuous employment for a specified time period following the date of grant. During this period, the holder is entitled to full voting rights and dividends.

A summary of the status of the Company's nonvested restricted stock and changes for the years ended December 31, 2020, 2019, and 2018 is as follows:

		2020		2019		December 31, 2018
	Restricted Shares	Weighted Average Grant-Date Fair Value	Restricted Shares	Weighted Average Grant-Date Fair Value	Restricted Shares	Weighted Average Grant-Date Fair Value
Nonvested at beginning of year	32,825	$ 34.78	29,625	$ 34.00	25,000	$ 26.43
Granted	13,200	39.87	14,700	33.64	13,000	42.87
Vested	(14,051)	32.06	(10,375)	31.61	(8,375)	25.17
Forfeited	(5,875)	37.74	(1,125)	28.03	-	-
Nonvested at end of year	26,099	$ 38.05	32,825	$ 34.78	29,625	$ 34.00

At December 31, 2020, there was $700,000 of total unrecognized compensation cost related to nonvested restricted stock grants. The cost is expected to be recognized over a weighted-average period of 2.5 years.

NOTE 22 – Dividends

The ability of the Company to pay cash dividends is dependent upon receiving cash in the form of dividends from the Bank. The dividends that may be paid by the Bank to the Company are subject to legal limitations and regulatory capital requirements.

Also, the payment of cash dividends on the Company's common stock by the Company in the future will be subject to certain other legal and regulatory limitations (including the requirement that the Company's capital be maintained at certain minimum levels) and will be subject to ongoing review by banking regulators. The Federal Reserve has issued a policy statement regarding the payment of dividends by bank holding companies. In general, the Federal Reserve's policies provide that dividends should be paid only out of current earnings and only if the prospective rate of earnings retention by the bank holding company appears consistent with the organization's capital needs, asset quality and overall financial condition.

NOTE 23 – Regulatory Matters

The Bank is subject to various regulatory capital requirements administered by the federal banking agencies. The capital rules require banks and bank holding companies (other than bank holding companies, such as the Company, that qualify under the Federal Reserve's Small Bank Holding Company Policy Statement) to maintain a minimum total risked-based capital ratio of at least 8%, a total Tier 1 capital ratio of at least 6%, a minimum common equity Tier 1 capital ratio of at least 4.5%, and a leverage ratio of at least 4%. Bank holding companies and banks are also required to hold a capital conservation buffer of common equity Tier 1 capital of 2.5% to avoid limitations on capital distributions and discretionary executive compensation payments. The capital conservation buffer was phased in incrementally over time, becoming fully effective on January 1, 2019, and consists of an additional amount of common equity equal to 2.5% of risk-weighted assets.

To be considered "well-capitalized" for purposes of certain rules and prompt corrective action requirements, the Bank must maintain a minimum total risked-based capital ratio of at least 10%, a total Tier 1 capital ratio of at least 8%, a common equity Tier 1 capital ratio of at least 6.5%, and a leverage ratio of at least 5%. As of December 31, 2020, our capital ratios exceed these ratios and we remain "well capitalized."

The following table summarizes the capital amounts and ratios of the Bank and the Company and the regulatory minimum requirements at December 31, 2020 and 2019.

(dollars in thousands)	Amount	Actual Ratio	Amount	For capital adequacy purposes minimum Ratio	Amount	To be well capitalized under prompt corrective action provisions minimum Ratio
As of December 31, 2020						
The Bank						
Total Capital (to risk weighted assets)	$ 279,414	13.92%	$ 160,554	8.00%	$ 200,693	10.00%
Tier 1 Capital (to risk weighted assets)	254,092	12.66%	120,416	6.00%	160,554	8.00%
Common Equity Tier 1 Capital (to risk weighted assets)	254,092	12.66%	90,312	4.50%	130,451	6.50%
Tier 1 Capital (to average assets)	254,092	10.26%	99,094	4.00%	123,867	5.00%
The Company[1]						
Total Capital (to risk weighted assets)	288,593	14.38%	160,554	8.00%	n/a	n/a
Tier 1 Capital (to risk weighted assets)	240,271	11.97%	120,416	6.00%	n/a	n/a
Common Equity Tier 1 Capital (to risk weighted assets)	227,271	11.32%	90,312	4.50%	n/a	n/a
Tier 1 Capital (to average assets)	240,271	9.70%	99,094	4.00%	n/a	n/a

(dollars in thousands)	Amount	Actual Ratio	Amount	For capital adequacy purposes minimum Ratio	Amount	To be well capitalized under prompt corrective action provisions minimum Ratio
As of December 31, 2019						
The Bank						
Total Capital (to risk weighted assets)	$ 250,847	13.31%	$ 150,807	8.00%	$ 188,510	10.00%
Tier 1 Capital (to risk weighted assets)	234,205	12.42%	113,106	6.00%	150,807	8.00%
Common Equity Tier 1 Capital (to risk weighted assets)	234,205	12.42%	84,829	4.50%	122,531	6.50%
Tier 1 Capital (to average assets)	234,205	10.80%	86,772	4.00%	108,465	5.00%
The Company[1]						
Total Capital (to risk weighted assets)	258,800	13.73%	150,807	8.00%	n/a	n/a
Tier 1 Capital (to risk weighted assets)	219,158	11.63%	113,106	6.00%	n/a	n/a
Common Equity Tier 1 Capital (to risk weighted assets)	206,158	10.94%	84,829	4.50%	n/a	n/a
Tier 1 Capital (to average assets)	219,158	10.10%	86,772	4.00%	n/a	n/a

(1) *Under the Federal Reserve's Small Bank Holding Company Policy Statement, the Company is not subject to the minimum capital adequacy and capital conservation buffer capital requirements at the holding company level, unless otherwise advised by the Federal Reserve (such capital requirements are applicable only at the Bank level). Although the minimum regulatory capital requirements are not applicable to the Company, we calculate these ratios for our own planning and monitoring purposes.*

NOTE 24 – Reportable Segments

The Company's reportable segments represent the distinct product lines the Company offers and are viewed separately for strategic planning purposes by management. The three segments include Commercial and Retail Banking, Mortgage Banking, and Corporate Operations. The following schedule presents financial information for each reportable segment.

(dollars in thousands)		Commercial and Retail Banking	Mortgage Banking	Corporate Operations	Eliminations	Consolidated
						Year ended December 31, 2020
Interest income	$	93,640	1,178	17	(17)	94,818
Interest expense		13,317	-	1,708	(17)	15,008
Net interest income (loss)		80,323	1,178	(1,691)	-	79,810
Provision for loan losses		29,600	-	-	-	29,600
Noninterest income		7,568	19,785	-	-	27,353
Noninterest expense		43,563	9,898	283	-	53,744
Net income (loss) before taxes		14,728	11,065	(1,974)	-	23,819
Income tax provision (benefit)		3,582	2,324	(415)	-	5,491
Net income (loss)	$	11,146	8,741	(1,559)	-	18,328
Total assets	$	2,419,245	62,910	264,566	(264,134)	2,482,587

		Commercial and Retail Banking	Mortgage Banking	Corporate Operations	Eliminations	Consolidated
						Year ended December 31, 2019
Interest income	$	91,923	729	13	(13)	92,652
Interest expense		24,467	-	929	(13)	25,383
Net interest income (loss)		67,456	729	(916)	-	67,269
Provision for loan losses		2,300	-	-	-	2,300
Noninterest income		5,060	9,923	-	-	14,983
Noninterest expense		37,797	6,436	240	-	44,473
Net income (loss) before taxes		32,419	4,216	(1,156)	-	35,479
Income tax expense (benefit)		6,979	885	(243)	-	7,621
Net income (loss)	$	25,440	3,331	(913)	-	27,858
Total assets	$	2,239,430	27,356	242,069	(241,660)	2,267,195

Commercial and retail banking. The Company's primary business is to provide traditional deposit and lending products and services to its commercial and retail banking clients.

Mortgage banking. The mortgage banking segment provides mortgage loan origination services for loans that will be sold in the secondary market to investors.

Corporate operations. Corporate operations is comprised primarily of compensation and benefits for certain members of management and interest on parent company debt.

NOTE 25 – Parent Company Financial Information

Following is condensed financial information of Southern First Bancshares, Inc. (parent company only):

Condensed Balance Sheets

(dollars in thousands)		2020	December 31, 2019
Assets			
Cash and cash equivalents	$	9,019	7,753
Investment in subsidiaries		255,518	234,310
Other assets		29	6
Total assets	$	264,566	242,069
Liabilities and Shareholders' Equity			
Accounts payable and accrued expenses	$	274	319
Subordinated debentures		35,998	35,890
Shareholders' equity		228,294	205,860
Total liabilities and shareholders' equity	$	264,566	242,069

Condensed Statements of Income

(dollars in thousands)		For the years ended December 31, 2020	2019	2018
Revenues				
Interest income	$	17	13	9
Total revenue		17	13	9
Expenses				
Interest expense		1,708	929	592
Other expenses		283	240	240
Total expenses		1,991	1,169	832
Income tax benefit		415	243	173
Loss before equity in undistributed net income of subsidiaries		(1,559)	(913)	(650)
Equity in undistributed net income of subsidiaries		19,887	28,771	22,939
Net income	$	18,328	27,858	22,289

Condensed Statements of Cash Flows

(dollars in thousands)		For the years ended December 31, 2020	2019	2018
Operating activities				
Net income	$	18,328	27,858	22,289
Adjustments to reconcile net income to cash provided by (used for) operating activities				
Equity in undistributed net income of subsidiaries		(19,887)	(28,771)	(22,939)
Compensation expense related to stock options and restricted stock grants		1,397	1,698	1,502
(Increase) decrease in other assets		(23)	12	12
Increase (decrease) in accounts payable and accrued expenses		63	(202)	2
Net cash provided by (used for) operating activities		(122)	595	866
Investing activities				
Investment in subsidiaries, net		-	-	-
Net cash used for investing activities		-	-	-
Financing activities				
Issuance of common stock		-	-	-
Proceeds from the exercise of stock options and warrants		1,388	1,769	900
Net cash provided by financing activities		1,388	1,769	900
Net increase in cash and cash equivalents		1,266	2,364	1,766
Cash and cash equivalents, beginning of year		7,753	5,389	3,623
Cash and cash equivalents, end of year	$	9,019	7,753	5,389

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NOTE 26 – Selected Condensed Quarterly Financial Data (Unaudited)

				2020
				For the quarters ended
(dollars in thousands, except share data)	March 31	June 30	September 30	December 31
Interest income	$ 23,866	23,991	23,415	23,547
Interest expense	5,768	4,217	2,778	2,244
Net interest income	18,098	19,774	20,637	21,303
Provision for loan losses	6,000	10,200	11,100	2,300
Noninterest income	3,916	9,207	7,584	6,644
Noninterest expenses	12,372	12,644	14,183	14,544
Income before income tax expense	3,642	6,137	2,938	11,103
Income tax expense	810	1,459	721	2,502
Net income available to common shareholders	$ 2,832	4,678	2,217	8,601
Earnings per common share				
Basic	$ 0.37	0.61	0.29	1.11
Diluted	$ 0.36	0.60	0.28	1.10
Weighted average common shares outstanding				
Basic	7,678,598	7,722,419	7,732,293	7,740,755
Diluted	7,827,173	7,818,651	7,815,265	7,835,739

				2019
				For the quarters ended
	March 31	June 30	September 30	December 31
Interest income	$ 21,612	23,088	24,056	23,896
Interest expense	5,794	6,549	6,777	6,263
Net interest income	15,818	16,539	17,279	17,633
Provision for loan losses	300	300	650	1,050
Noninterest income	2,994	4,090	4,396	3,503
Noninterest expenses	10,648	11,368	11,484	10,973
Income before income tax expense	7,864	8,961	9,541	9,113
Income tax expense	1,855	1,722	2,129	1,915
Net income available to common shareholders	$ 6,009	7,239	7,412	7,198
Earnings per common share				
Basic	$ 0.81	0.97	0.98	0.94
Diluted	$ 0.78	0.93	0.95	0.92
Weighted average common shares outstanding				
Basic	7,459,342	7,495,508	7,548,184	7,608,241
Diluted	7,741,860	7,756,044	7,780,504	7,810,922

Item 9. Changes in and Disagreements with Accountants on Accounting and Financial Disclosure

None.

Item 9A. Controls and Procedures

Evaluation of Disclosure Controls and Procedures

Based on our management’s evaluation (with the participation of our principal executive officer and principal financial officer), as of the end of the period covered by this report, our principal executive officer and principal financial officer have concluded that our disclosure controls and procedures (as defined in Rules 13a-15(e) and 15d-15(e) under the Securities Exchange Act of 1934, as amended, (the “Exchange Act”)) are effective to ensure that information required to be disclosed by us in reports that we file or submit under the Exchange Act is recorded, processed, summarized and reported within the time periods specified in Securities and Exchange Commission rules and forms and is accumulated and communicated to our management, including our principal executive officer and principal financial officer, as appropriate to allow timely decisions regarding required disclosure.

For management’s report on internal control over financial reporting and the attestation report thereon issued by our independent registered public accounting firm, see Item 8. Financial Statements and Supplementary Data.

Internal Control over Financial Reporting

There was no change in our internal control over financial reporting during our fourth quarter of fiscal 2020 that has materially affected, or is reasonably likely to materially affect, our internal control over financial reporting.

Item 9B. Other Information

None

PART III

Item 10. Directors, Executive Officers and Corporate Governance.

In response to this Item, this information is contained in our Proxy Statement for the Annual Meeting of Shareholders to be held on May 18, 2021 and is incorporated herein by reference.

Item 11. Executive Compensation.

In response to this Item, this information is contained in our Proxy Statement for the Annual Meeting of Shareholders to be held on May 18, 2021 and is incorporated herein by reference.

Item 12. Security Ownership of Certain Beneficial Owners and Management and Related Shareholder Matters.

In response to this Item, the information required by Item 201(d) is contained in Item 5 of this report. The other information required by this item is contained in our Proxy Statement for the Annual Meeting of Shareholders to be held on May 18, 2021 and is incorporated herein by reference.

Item 13. Certain Relationships and Related Transactions, and Director Independence.

The information is contained in our Proxy Statement for the Annual Meeting of Shareholders to be held on May 18, 2021 is incorporated herein by reference.

Item 14. Principal Accounting Fees and Services.

In response to this Item, this information is contained in our Proxy Statement for the Annual Meeting of Shareholders to be held on May 18, 2021 and is incorporated herein by reference.

Item 15. Exhibits, Financial Statement Schedules

(a) (1) Financial Statements

The following consolidated financial statements are located in Item 8 of this report.

Management's Report on Internal Control Over Financial Reporting

Report of Independent Registered Public Accounting Firm

Consolidated Balance Sheets as of December 31, 2020 and 2019

Consolidated Statements of Income for the years ended December 31, 2020, 2019 and 2018

Consolidated Statements of Comprehensive Income for the years ended December 31, 2020, 2019 and 2018

Consolidated Statements of Changes in Shareholders' Equity for the years ended December 31, 2020, 2019 and 2018

Consolidated Statements of Cash Flows for the years ended December 31, 2020, 2019 and 2018

Notes to the Consolidated Financial Statements

(2) Financial Statement Schedules

These schedules have been omitted because they are not required, are not applicable or have been included in our consolidated financial statements.

(3) Exhibits

See the "Exhibit Index" immediately following the signature page of this report.

EXHIBIT INDEX

3.1	Amended and Restated Articles of Incorporation (incorporated by reference to Exhibit 3.1 of the Company's Registration Statement on Form SB-2 filed on July 27, 1999, File No. 333-83851).
3.2	Amended and Restated Bylaws dated March 18, 2008 (incorporated by reference to Exhibit 3.4 of the Company's Form 10-K filed March 24, 2008).
3.3	Amendment to Amended and Restated Bylaws dated March 18, 2008 (incorporated by reference to Exhibit 3.1 of the Company's Form 10-Q filed on November 2, 2020).
4.1	Description of the Company's Securities Registered Pursuant to Section 12 of the Securities Exchange Act of 1934 (incorporated by reference to Exhibit 4.1 of the Company's Form 10-K filed on March 2, 2020).
4.2	Form of certificate of common stock (incorporated by reference to Exhibit 4.2 of the Company's Registration Statement on Form SB-2, File No. 333-83851).
4.3	Indenture dated as of September 30, 2019 between Southern First Bancshares, Inc. and UMB Bank, National Association, as trustee (incorporated by reference to Exhibit 4.1 of the Company's Form 8-K filed on September 30, 2019).
4.4	Form of 4.75% Fixed-to-Floating Subordinated Note due 2029 of Southern First Bancshares, Inc. (incorporated by reference to Exhibit 4.2 of the Company's Form 8-K filed on September 30, 2019).
4.5	Form of Global 4.75% Fixed-to-Floating Subordinated Note due 2029 of Southern First Bancshares, Inc. (incorporated by reference to the Exhibit 2 to Exhibit 4.1 of the Company's Form 8-K filed on September 30, 2019).
10.1	Southern First Bancshares, Inc. 2010 Stock Incentive Plan (incorporated by reference to Appendix A of the Company's Proxy Statement on Schedule 14A filed April 6, 2010).*
10.2	Amendment to Southern First Bancshares, Inc. 2010 Stock Incentive Plan (incorporated by reference to Appendix A of the Company's Proxy Statement on Schedule 14A filed on April 15, 2014).*
10.3	Amendment to Southern First Bancshares, Inc. 2010 Stock Incentive Plan (incorporated by reference to Appendix A of the Company's Proxy Statement on Schedule 14A filed on April 14, 2015).*
10.4	Form of Award Agreement for Stock Options (incorporated by reference to Exhibit 4.6 of the Company's Form S-8 filed on August 12, 2010).*
10.5	Form of Award Agreement for Restricted Stock (incorporated by reference to Exhibit 4.7 of the Company's Form S-8 filed on August 12, 2010).*
10.6	Sublease Agreement between Greenville First Bank, N.A. and Augusta Road Holdings, LLC dated February 26, 2004 (incorporated by reference to Exhibit 10.6 of the Company's Form 10-QSB for the period ended June 30, 2004).
10.7	Bonaventure I Office Lease Agreement with Greenville First Bank, N.A., dated September 20, 2005 (incorporated by reference to Exhibit 10.1 of the Company's Form 10-Q for the period ended September 30, 2005).
10.8	First Amendment to Office Lease Agreement with Greenville First Bank, N.A., dated September 20, 2005 (incorporated by reference to Exhibit 10.2 of the Company's Form 10-Q for the period ended September 30, 2005).
10.9	R. Arthur Seaver, Jr. Amended and Restated Employment Agreement (incorporated by reference to Exhibit 10.5 of the Company's Form 8-K filed October 3, 2013).*
10.10	F. Justin Strickland Amended and Restated Employment Agreement (incorporated by reference to Exhibit 10.6 of the Company's Form 8-K filed October 3, 2013).*
10.11	Michael D. Dowling Amended and Restated Employment Agreement (incorporated by reference to Exhibit 10.8 of the Company's Form 8-K filed October 3, 2013).*

10.12	Form of Split Dollar Agreement between certain executives and Southern First Bancshares, Inc. (incorporated by reference to Exhibit 10.1 of the Company's Form 8-K filed February 18, 2009).*
10.13	Form of Southern First Bank, N.A. Salary Continuation Agreement dated December 17, 2008 (incorporated by reference to Exhibit 10.1 of the Company's Form 8-K filed December 23, 2008).*
10.14	Form of First Amendment to Southern First Bank, N.A. Salary Continuation Agreement dated December 17, 2008 (incorporated by reference to Exhibit 10.2 of the Company's Form 8-K filed December 23, 2008).*
10.15	Michael D. Dowling Salary Continuation Agreement (incorporated by reference to Exhibit 10.1 of the Company's Form 8-K filed October 3, 2013).*
10.16	F. Justin Strickland First Amendment to Salary Continuation Agreement (incorporated by reference to Exhibit 10.2 of the Company's Form 8-K filed October 3, 2013).*
10.17	R. Arthur Seaver, Jr. Second Amendment to Salary Continuation Agreement (incorporated by reference to Exhibit 10.4 of the Company's Form 8-K filed October 3, 2013).*
10.18	Southern First Bancshares, Inc. 2016 Equity Incentive Plan (incorporated by reference to Appendix A of the Company's Proxy Statement on Schedule 14A filed on April 12, 2016).*
10.19	Form of Award Agreement for Stock Options (incorporated by reference to Exhibit 4.6 of the Company's Form S-8 filed on August 18, 2016).*
10.20	Form of Award Agreement for Restricted Stock (incorporated by reference to Exhibit 4.7 of the Company's Form S-8 filed on August 18, 2016).*
10.21	Amendment dated as of January 31, 2019 to R. Arthur Seaver, Jr. Amended and Restated Employment Agreement (incorporated by reference to Exhibit 10.1 of the Company's Form 8-K filed on February 6, 2019).*
10.22	Amendment dated as of January 31, 2019 to F. Justin Strickland Amended and Restated Employment Agreement (incorporated by reference to Exhibit 10.2 of the Company's Form 8-K filed on February 6, 2019).*
10.23	Amendment dated as of January 31, 2019 to Michael D. Dowlling Amended and Restated Employment Agreement (incorporated by reference to Exhibit 10.3 of the Company's Form 8-K filed on February 6, 2019).*
10.24	Development Services Agreement dated as of April 9, 2019 between Southern First Bank and Cothran Properties, LLC (incorporated by reference to Exhibit 10.1 of the Company's Form 10-Q filed on August 2, 2019).
10.25	Form of Subordinated Note Purchase Agreement dated as of September 30, 2019 by and among Southern First Bancshares, Inc. and certain qualified institutional buyers and accredited investors (incorporated by reference to Exhibit 10.1 of the Company's Form 8-K filed on September 30, 2019).
10.26	Form of Registration Rights Agreement dated as of September 30, 2019 by and among Southern First Bancshares, Inc. and certain qualified institutional buyers and accredited investors (incorporated by reference to Exhibit 10.2 of the Company's Form 8-K filed on September 30, 2019).
10.27	Consulting Agreement dated as of January 23, 2020 between Southern First Bancshares, Inc., Southern First Bank, and F. Justin Strickland (incorporated by reference to Exhibit 10.1 of the Company's Form 8-K filed on January 23, 2020).*
10.28	General Waiver and Release Agreement dated as of January 23, 2020 between Southern First Bank and F. Justin Strickland (incorporated by reference to Exhibit 10.2 of the Company's Form 8-K filed on January 23, 2020).*
10.29	Pledge Agreement, dated as of June 30, 2017, by and between Southern First Bancshares, Inc. and CenterState Bank, National Association (incorporated by reference to Exhibit 10.3 of the Company's Form 8-K filed on July 3, 2017).

10.30	Amended and Restated Loan and Security Agreement, dated as of June 29, 2020, by and between Southern First Bancshares, Inc. and CenterState Bank, National Association (incorporated by reference to Exhibit 10.1 of the Company's Form 10-Q filed on August 3, 2020).
10.31	Amended and Restated Promissory Note, dated as of June 29, 2020, by and between Southern First Bancshares, Inc. and CenterState Bank, National Association (incorporated by reference to Exhibit 10.2 of the Company's Form 10-Q filed on August 3, 2020).
21	Subsidiaries.
23	Consent of Independent Public Accountants.
24	Power of Attorney (contained herein as part of the signature pages).
31.1	Rule 13a-14(a) Certification of the Principal Executive Officer.
31.2	Rule 13a-14(a) Certification of the Principal Financial Officer.
32	Section 1350 Certifications of the Principal Executive Officer and Principal Financial Officer.
101	The following materials from the Company's Annual Report on Form 10-K for the year ended December 31, 2020, formatted in eXtensible Business Reporting Language (XBRL); (i) the Consolidated Balance Sheets at December 31, 2020 and December 31, 2019, (ii) Consolidated Statements of Income for the years ended December 31, 2020, 2019, and 2018, (iii) Consolidated Statements of Changes in Shareholders' Equity and Comprehensive Income for the years ended December 31, 2020, 2019, and 2018, (iv) Consolidated Statements of Cash Flows for the years ended December 31, 2020, 2019, and 2018, and (iv) Notes to Consolidated Financial Statements.
104	Cover Page Interactive Data File (embedded within the Inline XBRL Document)

* Management contract or compensatory plan or arrangement

SIGNATURES

Pursuant to the requirements of Section 13 or 15(d) of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned, thereunto duly authorized.

SOUTHERN FIRST BANCSHARES, INC.

Date:	March 2, 2021	By:	/s/ R. Arthur Seaver, Jr. Chief Executive Officer

KNOW ALL MEN BY THESE PRESENTS, that each person whose signature appears below constitutes and appoints R. Arthur Seaver, Jr., his true and lawful attorney-in-fact and agent, with full power of substitution and resubstitution, for him and in his name, place and stead, in any and all capacities, to sign any and all amendments to this Annual Report on Form 10-K, and to file the same, with all exhibits thereto, and other documents in connection therewith, with the Securities and Exchange Commission, granting unto the attorney-in-fact and agent full power and authority to do and perform each and every act and thing requisite or necessary to be done in and about the premises, as fully to all intents and purposes as he might or could do in person, hereby ratifying and confirming all that the attorney-in-fact and agent, or his substitute or substitutes, may lawfully do or cause to be done by virtue hereof.

Pursuant to the requirements of the securities Exchange Act of 1934, this report has been signed below by the following persons on behalf of the registrant in the capacities and on the dates indicated.

Signature	**Title**	**Date**
/s/ R. Arthur Seaver, Jr. R. Arthur Seaver, Jr.	Director, Chief Executive Officer *(Principal Executive Officer)*	March 2, 2021
/s/ Michael D. Dowling Michael D. Dowling	Chief Financial Officer, Chief Operating Officer *(Principal Financial and Accounting Officer)*	March 2, 2021
/s/ Andrew B. Cajka, Jr. Andrew B. Cajka, Jr.	Director	March 2, 2021
/s/ Mark A. Cothran Mark A. Cothran	Director	March 2, 2021
/s/ Leighton M. Cubbage Leighton M. Cubbage	Director	March 2, 2021
/s/ David G. Ellison David G. Ellison	Director	March 2, 2021
/s/ Anne S. Ellefson Anne S. Ellefson	Director	March 2, 2021
/s/ Tecumseh Hooper, Jr. Tecumseh Hooper, Jr.	Director	March 2, 2021
/s/ Rudolph G. Johnstone, III M.D. Rudolph G. Johnstone, III, M.D.	Director	March 2, 2021
/s/ Anna T. Locke Anna T. Locke	Director	March 2, 2021
/s/ James B. Orders, III James B. Orders, III	Director, Chairman	March 2, 2021

Exhibit 21

Subsidiaries

Southern First Bank
Greenville Statutory Trust I and II

Exhibit 23

CONSENT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

We consent to incorporation by reference in Registration Statement No. 333-252143, 333-213188, 333-133379, 333-168779 and 333-181198 on Form S-8 and Registration Statement No. 333-235465 on Form S-4/A of Southern First Bancshares, Inc. and Subsidiary of our reports dated March 2, 2021, relating to our audits of the consolidated financial statements and the effectiveness of internal control over financial reporting of Southern First Bancshares, Inc. and Subsidiary appearing in the Annual Report to Shareholders, which is incorporated in this Annual Report on Form 10-K of Southern First Bancshares, Inc. and Subsidiary for the year ended December 31, 2020.

/s/ Elliott Davis, LLC

Greenville, South Carolina
March 2, 2021

Exhibit 31.1

Rule 13a-14(a) Certification of the Chief Executive Officer

I, R. Arthur Seaver, Jr., chief executive officer, certify that:

1. I have reviewed this annual report on Form 10-K of Southern First Bancshares, Inc.

2. Based on my knowledge, this annual report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;

3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;

4. The registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:

   a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;

   b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;

   c) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures as of the end of the period covered by this report based on such evaluation; and

   d) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of this annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and

5. The registrant's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):

   a) All significant deficiencies and material weaknesses in the design or operation of internal controls over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and

   b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: March 2, 2021

By: /s/R. Arthur Seaver, Jr.
R. Arthur Seaver, Jr.
Chief Executive Officer
(principal executive officer)

Exhibit 31.2

Rule 13a-14(a) Certification of the Principal Financial Officer

I, Michael D. Dowling, principal financial officer, certify that:

1. I have reviewed this annual report on Form 10-K of Southern First Bancshares, Inc.

2. Based on my knowledge, this annual report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;

3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;

4. The registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:

   a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;

   b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;

   c) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures as of the end of the period covered by this report based on such evaluation; and

   d) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of this annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and

5. The registrant's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):

   a) All significant deficiencies and material weaknesses in the design or operation of internal controls over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and

   b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: March 2, 2021

By: /s/Michael D. Dowling
Michael D. Dowling
Chief Financial Officer
(principal financial officer)

Exhibit 32

CERTIFICATION PURSUANT TO 18 U.S.C. SECTION 1350,
AS ADOPTED PURSUANT TO
SECTION 906 OF THE SARBANES-OXLEY ACT OF 2003

The undersigned, the Chief Executive Officer and the Principal Financial Officer of Southern First Bancshares, Inc. (the “company”), each certify that, to his knowledge on the date of this certification:

1. The annual report of the company for the period ended December 31, 2020 as filed with the Securities and Exchange Commission on this date (the “Report”) fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934; and

2. The information contained in the Report fairly presents, in all material respects, the financial condition and result of operations of the company.

Date: March 2, 2021	By:	/s/R. Arthur Seaver, Jr. R. Arthur Seaver, Jr. Chief Executive Officer
Date: March 2, 2021	By:	/s/Michael D. Dowling Michael D. Dowling Chief Financial Officer, Principal Financial Officer