

UNITED STATES SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

FORM 10-Q

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

For the quarterly period September 30, 2023
ended 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 001-41196
Number:



USCB Financial Holdings, Inc.
(Exact name of registrant as specified in its charter)

Florida

(State or other jurisdiction
of incorporation or
organization)

87-4070846

(I.R.S. Employer
Identification No.)

2301 N.W. 87th, Doral, FL 33172
Avenue (Address of principal executive offices) (zip code)

Registrant's telephone number, including area code: (305) 715-5200

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

<u>Title of each Class</u>	<u>Trading Symbol(s)</u>	<u>Name of each exchange on which registered</u>
Class A common stock, \$1.00 par value per share	USCB	The Nasdaq Stock Market LLC

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 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) 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 pursuant to 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 such files). Yes No

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, a smaller reporting company or an emerging growth company. See the definitions of "large accelerated filer," "accelerated filer," "non-accelerated filer" 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 new or revised financial accounting standards provided pursuant to Section 13(a) of the Exchange Act. No

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

Yes
Indicate the number of shares outstanding of each of the issuer's classes of common stock, as of the latest practicable date. As of October 30, 2023 the registrant had 19,542,290 shares of Class A common stock outstanding.



FORM 10-Q
September 30, 2023

TABLE OF CONTENTS

<u>PART I</u>		
<u>Item 1.</u>	<u>Financial Statements</u>	<u>3</u>
	Consolidated Balance Sheets as of September 30, 2023 (Unaudited) and December 31, 2022	3
	Consolidated Statements of Operations for the three and nine months ended September 30, 2023 and 2022 (Unaudited)	3
	Consolidated Statements of Comprehensive Income (Loss) for the three and nine months ended September 30, 2022 (Unaudited)	4
	Consolidated Statements of Changes in Stockholders' Equity for the three and nine months ended September 30, 2022 (Unaudited)	5
	Consolidated Statements of Cash Flows for the nine months ended September 30, 2023 and 2022 (Unaudited)	6
	Notes to the Consolidated Financial Statements (Unaudited)	7
	Management's Discussion and Analysis of Financial Condition and Results of Operations	32
<u>Item 2.</u>	Quantitative and Qualitative Disclosures About Market	55
<u>Item 3.</u>		55
<u>Item 4.</u>	<u>Controls and Procedures</u>	<u>56</u>
<u>PART II</u>		
<u>Item 1.</u>	<u>Legal Proceedings</u>	<u>56</u>
<u>Item 1A.</u>	Risk Factors	56
<u>Item 2.</u>	Unregistered Sales of Equity Securities and Use of Proceeds	56
<u>Item 3.</u>	Upon Senior Securities	57
<u>Item 4.</u>	Mine Safety Disclosures	57
<u>Item 5.</u>	Other Information	57
<u>Item 6.</u>	Index	58
	Signatures	

[Table of Contents](#)

PART I
Item 1. Financial Statements

USCB FINANCIAL HOLDINGS, INC
Consolidated Balance Sheets – Unaudited
(Dollars in thousands, except share data)

	<u>September 30, 2023</u>	<u>December 31, 2022</u>
ASSETS:		
Cash and due from banks	\$ 5,074	\$ 6,605
Interest-bearing deposits in banks	<u>28,361</u>	<u>47,563</u>
Total cash and cash equivalents	33,435	54,168
Investment securities held to maturity, net of allowance of \$6 and \$0, respectively (fair value \$171,294 and \$169,088, respectively)	197,311	188,699
Investment securities available for sale, at fair value	218,609	230,140
Federal Home Loan Bank stock, at cost	6,305	2,882
Loans held for investment, net of allowance of \$9,493 and \$17,487, respectively	1,657,027	1,489,851
Accrued interest receivable	8,920	7,546
Premises and equipment, net	4,951	5,263
Bank owned life insurance	51,377	42,781
Deferred tax assets, net	40,430	42,360
Lease right-of-use asset	12,166	14,395
Other assets	14,071	7,749
Total assets	<u>\$ 2,244,602</u>	<u>\$ 2,085,834</u>
LIABILITIES:		
Deposits:		
Demand deposits	\$ 573,546	\$ 629,776
Money market and savings accounts	1,016,564	915,853
Interest-bearing checking	46,537	66,675
Total deposits	<u>284,275</u>	<u>216,977</u>
Federal Home Loan Bank advances	102,000	46,000
Lease liability	12,166	14,395
Accrued interest and other liabilities	26,630	13,730
Total liabilities	<u>2,061,718</u>	<u>1,903,406</u>
Commitments and contingencies (See Notes 5 and 10)		
STOCKHOLDERS' EQUITY:		
Preferred stock - Class C; 1.00 par value; \$1,000 per share liquidation authorized; 0 and 0 issued and outstanding as of September 30, 2023 and December 31, 2022	52,748 shares	-
Preferred stock - Class D; 1.00 par value; \$6.00 per share liquidation authorized; 0 and 0 issued and outstanding as of September 30, 2023 and December 31, 2022	12,309,480 shares	-
Preferred stock - Class E; 1.00 par value; \$1,000 per share liquidation authorized; 0 and 0 issued and outstanding as of September 30, 2023 and December 31, 2022	3,185,024 shares	-
Common stock - Class A Voting; 1.00 par value; 45,000,000 shares authorized; 19,542,290 issued and outstanding as of September 30, 2023 and December 31, 2022	19,542	20,001
Common stock - Class B Non-voting; 1.00 par value; 8,000,000 shares authorized; 0 and 0 issued and outstanding as of September 30, 2023 and December 31, 2022	-	-
Additional paid-in capital on common stock	305,837	311,282
Accumulated deficit	(91,269)	(104,104)
Accumulated other comprehensive loss	(51,226)	(44,751)
Total stockholders' equity	<u>182,884</u>	<u>182,428</u>
Total liabilities and stockholders' equity	<u>\$ 2,244,602</u>	<u>\$ 2,085,834</u>

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

[Table of Contents](#)

USCB FINANCIAL HOLDINGS, INC.
Consolidated Statements of Operations - Unaudited
(Dollars in thousands, except per share data)

	<u>Three Months Ended September 30, Nine Months Ended September 30,</u>		<u>2023</u>	<u>2022</u>	<u>2023</u>	<u>2022</u>
Interest income:						
Loans, including fees	\$ 22,523	\$ 15,954	\$ 63,081	\$ 42,989		
Investment securities	2,833	2,201	7,501	7,040		
Interest-bearing deposits in financial institutions	1,026	322	2,459	474		
Total interest income	26,382	18,477	73,041	50,503		
Interest expense:						
Interest-bearing checking	331	19	574	52		
Money market and savings accounts	8,779	1,141	20,532	2,307		
Time deposits	2,565	363	5,767	893		
Federal Home Loan Bank advances and other borrowings	685	180	1,976	456		
Total interest expense	12,360	1,703	28,849	3,708		
Net interest income before provision for credit losses	14,022	16,774	44,192	46,795		
Provision for credit losses	653	910	892	1,615		
Net interest income after provision for credit losses	13,369	15,864	43,300	45,180		
Non-interest income:						
Service fees	1,329	934	3,707	2,917		
(Loss) gain on sale of securities available for sale, net	(955)	(558)	(976)	(540)		
Gain on sale of loans held for sale, net	255	330	696	686		
Loan settlement	-	-	-	161		
Other non-interest income	1,532	1,083	2,650	2,127		
Total non-interest income	2,161	1,789	6,077	5,351		
Non-interest expense:						
Salaries and employee benefits	6,066	6,075	18,325	17,863		
Regulatory assessment and fees	1,350	1,281	3,968	3,802		
Consulting and legal fees	365	269	1,041	708		
Network and information technology services	513	604	1,257	1,519		
Other operating expense	481	488	1,464	1,323		
Total non-interest expense	1,686	1,415	5,034	4,080		
Income before income tax expense	5,069	7,521	18,288	21,236		
Income tax expense	1,250	1,963	4,464	5,529		
Net income	\$ 3,819	\$ 5,558	\$ 13,824	\$ 15,707		
Per share information:						
Net income per share, basic	\$ 0.20	\$ 0.28	\$ 0.70	\$ 0.79		
Net income per share, diluted	\$ 0.19	\$ 0.28	\$ 0.70	\$ 0.78		

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

[Table of Contents](#)

USCB FINANCIAL HOLDINGS, INC.
Consolidated Statements of Comprehensive Income (Loss) - Unaudited
(Dollars in thousands)

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2023	2022	2023	2022
Net income	\$ 3,819	\$ 5,558	\$ 13,824	\$ 15,707
Other comprehensive income (loss):				
Unrealized loss on investment securities	(7,858)	(11,679)	(11,145)	(57,577)
Amortization of net unrealized (loss) gain on securities transferred from available-for-sale to held-to-maturity	64	(52)	184	(177)
Reclassification adjustment for loss included in net income	955	558	976	540
Unrealized gain on cash flow hedge	266	-	1,312	-
Tax effect	1,666	2,832	2,198	14,528
Total other comprehensive loss, net of tax	(4,907)	(8,341)	(6,475)	(42,686)
Total comprehensive income (loss)	\$ (1,088)	\$ (2,783)	\$ 7,349	\$ (26,979)

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

[Table of Contents](#)

USCB FINANCIAL HOLDINGS, INC.
Consolidated Statements of Changes in Stockholders' Equity - Unaudited
(Dollars in thousands, except per share data)

Common Stock						
	Shares	Par Value	Additional Paid-in Capital on Common Stock	Accumulated Deficit	Accumulated Other Comprehensive Loss	Total Stockholders' Equity
Balance at July 1, 2023	19,544,777	\$ 19,545	\$ 305,547	\$ (95,088)	\$ (46,319)	\$ 183,685
Net income	-	-	-	3,819	-	3,819
Other comprehensive loss	-	-	-	-	(4,907)	(4,907)
Restricted stock forfeiture	(2,487)	(3)	3	-	-	-
Stock-based compensation	-	-	287	-	-	287
Balance at September 30, 2023	<u>19,542,290</u>	<u>\$ 19,542</u>	<u>\$ 305,837</u>	<u>\$ (91,269)</u>	<u>\$ (51,226)</u>	<u>\$ 182,884</u>
Balance at July 1, 2022	20,000,753	\$ 20,001	\$ 311,024	\$ (114,096)	\$ (36,861)	\$ 180,068
Net income	-	-	-	5,558	-	5,558
Other comprehensive loss	-	-	-	-	(8,341)	(8,341)
Stock-based compensation	-	-	132	-	-	132
Balance at September 30, 2022	<u>20,000,753</u>	<u>\$ 20,001</u>	<u>\$ 311,156</u>	<u>\$ (108,538)</u>	<u>\$ (45,202)</u>	<u>\$ 177,417</u>

Common Stock						
	Shares	Par Value	Additional Paid-in Capital on Common Stock	Accumulated Deficit	Accumulated Other Comprehensive Loss	Total Stockholders' Equity
Balance at January 1, 2023	20,000,753	\$ 20,001	\$ 311,282	\$ (104,104)	\$ (44,751)	\$ 182,428
After tax cumulative effect of adoption of accounting principle related to ASC 326	-	-	-	(989)	-	(989)
Adjusted beginning balance after cumulative effect adjustment	<u>20,000,753</u>	<u>\$ 20,001</u>	<u>\$ 311,282</u>	<u>\$ (105,093)</u>	<u>\$ (44,751)</u>	<u>\$ 181,439</u>
Net income	-	-	-	13,824	-	13,824
Other comprehensive loss	-	-	-	-	(6,475)	(6,475)
Repurchase of Class A common stock	(577,603)	(577)	(6,036)	-	-	(6,613)
Restricted stock issued	121,627	121	(121)	-	-	-
Restricted stock forfeiture	(2,487)	(3)	3	-	-	-
Stock-based compensation	-	-	709	-	-	709
Balance at September 30, 2023	<u>19,542,290</u>	<u>\$ 19,542</u>	<u>\$ 305,837</u>	<u>\$ (91,269)</u>	<u>\$ (51,226)</u>	<u>\$ 182,884</u>
Balance at January 1, 2022	19,991,753	\$ 19,992	\$ 310,666	\$ (124,245)	\$ (2,516)	\$ 203,897
Net income	-	-	-	15,707	-	15,707
Other comprehensive loss	-	-	-	-	(42,686)	(42,686)
Exercise of stock options	9,000	9	93	-	-	102
Stock-based compensation	-	-	397	-	-	397
Balance at September 30, 2022	<u>20,000,753</u>	<u>\$ 20,001</u>	<u>\$ 311,156</u>	<u>\$ (108,538)</u>	<u>\$ (45,202)</u>	<u>\$ 177,417</u>

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

[Table of Contents](#)

USCB FINANCIAL HOLDINGS, INC.
Consolidated Statements of Cash Flows - Unaudited
(Dollars in thousands)

	<u>Nine Months Ended September 30,</u>	
	<u>2023</u>	<u>2022</u>
Cash flows from operating activities:		
Net income	\$ 13,824	\$ 15,707
Adjustments to reconcile net income to net cash provided by operating activities:		
Provision for credit losses	892	1,615
Depreciation and amortization	443	530
(Accretion) amortization of premiums on securities, net	(651)	412
Accretion of deferred loan fees, net	(236)	(1,364)
Stock-based compensation	709	397
Loss (gain) on sale of available for sale securities	976	540
Gain on sale of loans held for sale	(696)	(686)
Increase in cash surrender value of bank owned life insurance	(775)	(794)
Bank owned life insurance enhancement	(981)	-
Decrease in deferred tax assets	4,465	5,529
Net change in operating assets and liabilities:		
Accrued interest receivable	(1,374)	(593)
Other assets	(751)	(4,163)
Accrued interest and other liabilities	<u>12,679</u>	<u>14,432</u>
Net cash provided by operating activities	<u>28,524</u>	<u>31,562</u>
Cash flows from investing activities:		
Purchase of investment securities held to maturity	(86,788)	(2,432)
Proceeds from maturities and pay-downs of investment securities held to maturity	79,085	9,689
Purchase of investment securities available for sale	(26,792)	(49,808)
Proceeds from maturities and pay-downs of investment securities available for sale	11,679	35,502
Proceeds from sales of investment securities available for sale	15,409	45,647
Net increase in loans held for investment	(165,662)	(177,916)
Purchase of loans held for investment	(13,277)	(70,175)
Additions to premises and equipment	(131)	(175)
Proceeds from the sale of loans held for sale	10,715	8,641
Purchase of Bank owned life insurance	(11,100)	-
Proceeds from the redemption of Federal Home Loan Bank stock	6,517	2,250
Purchase of Federal Home Loan Bank stock	(9,940)	(2,052)
Net cash used in investment activities	<u>(190,285)</u>	<u>(200,829)</u>
Cash flows from financing activities:		
Proceeds from issuance of Class A common stock, net	-	102
Repurchase of Class A common stock	(6,613)	-
Net increase in deposits	91,641	206,263
Proceeds from Federal Home Loan Bank advances	259,350	60,000
Repayments on Federal Home Loan Bank advances	(203,350)	(70,000)
Net cash provided by financing activities	<u>141,028</u>	<u>196,365</u>
Net increase in cash and cash equivalents	(20,733)	27,098
Cash and cash equivalents at beginning of period	54,168	46,228
Cash and cash equivalents at end of period	<u>\$ 33,435</u>	<u>\$ 73,326</u>
Supplemental disclosure of cash flow information:		
Interest paid	<u>\$ 27,872</u>	<u>\$ 3,675</u>
Supplemental schedule of non-cash investing and financing activities:		
Transfer of loans held for investment to loans held for sale	<u>\$ 10,019</u>	<u>\$ 7,955</u>
Transfer of investment securities from available-for-sale to held-to-maturity	<u>\$ -</u>	<u>\$ 74,444</u>
Lease liability arising from obtaining right-of-use asset	<u>\$ -</u>	<u>\$ 1,550</u>

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

[Table of Contents](#)**USCB FINANCIAL HOLDINGS, INC.**
Notes to the Consolidated Financial Statements - Unaudited**1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES****Overview**

USCB Financial Holdings, Inc., a Florida corporation incorporated in 2021, is a bank holding company with one direct wholly owned subsidiary, U.S. Century Bank (the "Bank"), together referred to as "the Company". The Bank, established in 2002, is a Florida state-chartered, non-member financial institution providing financial services through its banking centers located in South Florida.

The Bank owns a subsidiary, Florida Peninsula Title LLC, that offers our clients title insurance policies for real estate transactions closed at the Bank. Licensed in the State of Florida and approved by the Department of Insurance Regulation, Florida Peninsula Title LLC began operations in 2021.

Basis of Presentation

The accompanying unaudited consolidated financial statements have been prepared in accordance with instructions to Form 10-Q and do not include all the information and footnotes required by U.S. generally accepted accounting principles ("U.S. GAAP") for complete financial statements. All adjustments consisting of normally recurring accruals that, in the opinion of management, are necessary for a fair presentation of the financial position and results of operations for the period presented have been included. These unaudited consolidated financial statements should be read in conjunction with the Company's consolidated financial statements and related notes appearing in the Company's Annual Report on Form 10-K/A for the year ended December 31, 2022.

Principles of Consolidation

The Company consolidates entities in which it has a controlling financial interest. Intercompany transactions balanced are eliminated in consolidation.

Use of Estimates

To prepare financial statements in conformity with U.S. GAAP, management makes estimates and assumptions based on available information. These estimates and assumptions affect the amounts reported in the financial statements. The most significant estimates impacting the Company's consolidated financial statements are the allowance for credit losses (ACL) and income taxes.

Reclassifications

Certain amounts in the consolidated financial statements have been reclassified to conform to the current presentation. Reclassifications had no impact on the net income or stockholders' equity of the Company.

Adoption of New Accounting Standards**Measurement of Credit Losses on Financial Instruments**

On January 1st, 2023, the Company adopted Accounting Standard Update ("ASU") 2016-13 Financial Instruments Credit Losses (Topic 326): Measurement of Credit Losses on Financial Instruments, as amended, which replaced the methodology with an expected loss methodology that is referred to as the current expected credit loss (CECL) methodology. The measurement of expected credit losses under the CECL methodology is applicable to financial assets at amortized cost, including loan receivables and held-to-maturity debt securities. It also applies to off-balance sheet credit exposures not accounted for as insurance (e.g., loan commitments, standby letters of credit, guarantees, and other similar instruments) and net investments in leases recognized by a lessor in accordance with Topic 842 on leases. In addition, ASC 326 amended the accounting for available-for-sale debt securities. One such change is to require credit losses to be presented as an allowance rather than as a write-down on available-for-sale debt securities that management does not intend to sell or believes that it is more likely than not they will not be required to sell.

Under CECL, the Company estimates the allowance for credit losses using relevant available information, from both internal and external sources, relating to past events, current conditions, and reasonable and supportable forecasts. Credit losses provide the basis for estimation of expected credit losses. Qualitative adjustments are applied to the

[Table of Contents](#)

USCB FINANCIAL HOLDINGS, INC.
Notes to the Consolidated Financial Statements - Unaudited

expected credit losses estimated for the loan portfolio in relation to potential limitations of the quantitative model. A ~~more detailed~~ aid management in the assessment of qualitative factor adjustments applied to expected credit losses.

The quantitative component of the estimate relies on the statistical relationship between the projected value ~~economic indicator~~ and the implied historical loss experience among a curated group of peers. The Company ~~utilized~~ regression analyses of peer data, in which the Company was included, and where observed credit losses and ~~several~~ factors were used to determine suitable loss drivers for modeling the lifetime rates of probability of default (PD). A loss given default rate (LGD) is assigned to each pool for each period based on these PD outcomes. The ~~fundamentally~~ utilizes an expected discounted cash flow (DCF) analysis for loan portfolio segments. The DCF analysis is run at the instrument-level and incorporates an array of loan-specific data points and segment-implied ~~determinants~~ lifetime expected loss attributable to each instrument. An implicit "hypothetical loss" is derived for each period of the DCF and helps establish the present value of future cash flows for each period. The reserve applied to a ~~segment~~ is the difference between the sum of the present value of future cash flows and the book balance of the loan at the measurement date.

Management elected the Remaining Life (WARM) methodology for five loan portfolio segments. For each of ~~segments~~ a long-term average loss rate is calculated and applied on a quarterly basis for the remaining life of the ~~adjustments~~ for economic expectations are made through qualitative assessments. For the remaining life ~~segment~~ implemented a software solution that uses an attrition-based calculation that performs quarterly, cohort-based attrition measurements based on the loan portfolio.

At adoption of CECL, 84% or \$1.3 billion of loan receivables were collectively evaluated under DCF method and 16% or \$251.0 million of loan receivables were collectively evaluated under the Remaining Life method. The remaining \$1.0 million of loan receivables of the total loan portfolio were individually evaluated.

Portfolio segments are the level at which loss assumptions are applied to a pool of loans based on the similarity of risk characteristics inherent in the included instruments, relying on collateral codes and FFIEC Call Report codes. The Company currently segments the portfolio based on collateral codes for purpose of establishing reserves. Each of these segments is paired to regression models (Loss Driver Analyses) based on peer data for loans of similar risk. ~~Company has established~~ relationships between internal segmentation and FFIEC Call Report codes for this purpose. The loss driver for each loan portfolio segment is derived from a readily available and reasonable economic forecast, including the Federal Reserve Bank projections of U.S. civilian unemployment rate and the year-over-year real GDP growth; for the residential loan segment the House Price index ("HPI") projections published by Fannie Mae's Economic and ~~Strategic~~ Group are utilized for the forecast. Forecasts are applied the first four quarters of the credit loss estimate ~~convert~~ on a straight-line basis to the lookback period's historical mean for the economic indicator over the expected life ~~of loans~~.

The model incorporates qualitative factor adjustments in order to calibrate the model for risk in each portfolio segment that may not be captured through quantitative analysis. Determinations regarding qualitative adjustments are reflective of management's expectation of loss conditions differing from those already captured in the quantitative component of ~~model~~.

The Company estimates a reserve for unfunded commitments, which is reported separately from the ~~credit losses~~ ~~and~~ other liabilities. The reserve is based upon the same quantitative and qualitative factors applied to the collectively evaluated loan portfolio.

The impact of adoption of the ASU 2016-13 was an increase to the allowance for credit losses (ACL) ~~receivable~~ of \$ 1.1 million and an increase to the reserve for unfunded commitments of \$ 259 thousand. This one-time net of tax cumulative adjustment resulted in a increase of \$ 1.0 million in accumulated deficit. See "Allowance for Credit Losses" section in Note 3 for more information on the ACL.

Trouble Debt Restructuring

In March 2022, the Financial Accounting Standards Board ("FASB") issued ASU 2022-02, Financial Instruments-Credit Losses (Topic 326): Troubled Debt Restructurings ("TDR") and Vintage Disclosures. The standard addresses the following: 1) eliminates the accounting guidance for TDRs, requires an entity to determine whether a modification results in a ~~new~~ or a continuation of an existing loan, 2) expands disclosures related to modifications, and 3) requires disclosure of current period gross write-offs of financing receivables within the vintage disclosures table (see Note 3). The Company

[Table of Contents](#)

USCB FINANCIAL HOLDINGS, INC.
Notes to the Consolidated Financial Statements - Unaudited

adopted ASU 2022-02 effective January 1, 2023 on a prospective basis. The adoption of ASU 2022-02 did not have a material impact on the Company's consolidated financial statements.

Issued and Not Yet Adopted

Reference Rate Reform

In March 2020, the FASB issued ASU 2020-04, Reference Rate Reform (Topic 848), Facilitation of the Reference Rate Reform on Financial Reporting. In January 2021, the FASB clarified the scope of this guidance with ASU 2021-01 which provides optional guidance for a limited period of time to ease the burden in accounting for (or recognizing the effects of) reference rate reform on financial reporting. This ASU is effective from March 12, 2020 through December 31, 2024. The Company is evaluating the impact of this ASU and has not yet determined whether LIBOR transition and ASU will have a material effect on our business operations and consolidated financial statements.

2. INVESTMENT SECURITIES

On January 1st, 2023, the Company adopted ASU 2016-13 Financial Instruments - Credit Losses (Topic 326) Measurement of Credit Losses on Financial Instruments, as amended, which replaces the incurred loss methodology with an expected loss methodology that is referred to as the current expected credit loss (CECL) methodology. The measurement of expected credit losses under the CECL methodology is applicable to financial assets measured at amortized cost including loan receivables and held-to-maturity debt securities. In addition, ASC 326 amended the accounting for available-for-sale debt securities. One such change is to require credit losses to be presented as an allowance rather than as a write-down on available-for-sale debt securities management does not intend to sell or believes that it is more likely than not they will be required to sell.

CECL requires a loss reserve for securities classified as Held-to-Maturity (HTM). The reserve should reflect historical credit performance as well as the impact of projected economic forecast. For U.S. Government bonds and U.S. Agency bonds in HTM the explicit guarantee of the US Government is sufficient to conclude that a credit loss reserve is not required. The reserve requirement is for three primary assets groups: municipal bonds, corporate bonds, and non-agency securitizations. The Company calculates quarterly the loss reserve utilizing Moody's ImpairmentStudio. The measurement for investment securities incorporates historical data, containing defaults and recoveries information, Moody's baseline economic forecast. The solution uses probability of default/loss given default ("PD/LGD") approach. PD represents the likelihood a borrower will default. Within the Moody's model, this is determined using historical default data, adjusted for the current economic environment. LGD projects the expected loss if a borrower were to default.

The Company monitors the credit quality of held to maturity securities through the use of credit ratings. Credit ratings are monitored by the Company on at least a quarterly basis. As of September 30, 2023 and December 31, 2022, all held-to-maturity securities held by the Company were rated investment grade.

At quarter end, HTM securities included \$187.9 million of U.S. Government and U.S. Agency issued bonds and mortgage-backed securities. Because of the explicit and/or implicit guarantee on these bonds, the Company no longer holds these on these holdings. The remaining portion of the HTM portfolio is made up of \$1.6 million in investment grade corporate bonds. The required reserve for these holdings is determined each quarter using the model described above. For the portion of the HTM exposed to non-government credit risk, the Company utilized the PD/LGD methodology to estimate a \$16 thousand ACL as of September 30, 2023. The book value for debt securities classified as HTM represents amortized cost less ACL.

The Company determined that an ACL on its debt securities available for sale as of September 30, 2023 and December 31, 2022 was not required.

[Table of Contents](#)

USCB FINANCIAL HOLDINGS, INC.
Notes to the Consolidated Financial Statements - Unaudited

The following tables present a summary of the amortized cost, unrealized or unrecognized gains and losses, and value of investment securities at the dates indicated (in thousands):

	September 30, 2023			
	Amortized Cost	Unrealized Gains	Unrealized Losses	Fair Value
Available-for-sale:				
U.S. Government Agency	\$ 9,913	\$ -	\$ (1,888)	\$ 8,025
Collateralized mortgage	105,547	-	(26,976)	78,571
Mortgage-backed securities - residential	66,024	-	(14,867)	51,157
Mortgage-backed securities -	48,010	62	(7,508)	40,564
Municipal securities	25,024	-	(6,908)	18,116
Bank subordinated debt	24,417	5	(2,246)	22,176
Corporate bonds	-	-	-	-
	<u>\$ 278,935</u>	<u>\$ 67</u>	<u>\$ (60,393)</u>	<u>\$ 218,609</u>
Held-to-maturity:				
U.S. Government Agency	\$ 44,087	\$ -	\$ (7,038)	\$ 37,049
U.S.	19,934	-	(28)	19,906
Collateralized mortgage	64,094	-	(10,308)	53,786
Mortgage-backed securities - residential	44,302	-	(6,088)	38,214
Mortgage-backed securities -	15,467	-	(1,583)	13,884
Commercial bonds	9,443	-	(988)	8,455
	<u>\$ 197,327</u>	<u>\$ -</u>	<u>\$ (26,033)</u>	<u>\$ 171,294</u>
Allowance for credit losses - securities held-to-maturity	<u>(16)</u>			
Securities held-to-maturity, net of allowance for credit losses	<u>\$ 197,311</u>			
	December 31, 2022			
	Amortized Cost	Unrealized Gains	Unrealized Losses	Fair Value
Available-for-sale:				
U.S. Government Agency	\$ 10,177	\$ -	\$ (1,522)	\$ 8,655
Collateralized mortgage	118,951	-	(23,410)	95,541
Mortgage-backed securities - residential	73,838	-	(12,959)	60,879
Mortgage-backed securities -	32,244	15	(4,305)	27,954
Municipal securities	25,084	-	(6,601)	18,483
Bank subordinated debt	15,964	5	(1,050)	14,919
Corporate bonds	4,037	-	(328)	3,709
	<u>\$ 280,295</u>	<u>\$ 20</u>	<u>\$ (50,175)</u>	<u>\$ 230,140</u>
Held-to-maturity:				
U.S. Government Agency	\$ 44,914	\$ 25	\$ (5,877)	\$ 39,062
U.S.	9,841	-	(13)	9,828
Collateralized mortgage	68,727	28	(7,830)	60,925
Mortgage-backed securities - residential	42,685	372	(4,574)	38,483
Mortgage-backed securities -	11,442	-	(665)	10,777
Commercial bonds	11,090	-	(1,077)	10,013
	<u>\$ 188,699</u>	<u>\$ 425</u>	<u>\$ (20,036)</u>	<u>\$ 169,088</u>

During the year ended December 31, 2022, a total of 26 investment securities with an amortized cost basis and fair value of \$4.4 million and \$3.8 million, respectively, were transferred from AFS to HTM. These securities had a unrealized loss of \$0.6 million at the date of transfer. The net unrealized loss that was retained in accumulated comprehensive income ("ACCI") is being amortized over the remaining life of the securities. For the three and nine months ended September 30, 2023, total amortization out of ACCI for net unrealized losses on securities transferred from AFS to HTM was \$64 thousand and \$184 thousand, respectively. The unamortized net unrealized loss on September 30, 2023, was \$9.6 million. There were no securities transferred from AFS to HTM during the nine months ended September 30, 2023.

[Table of Contents](#)

USCB FINANCIAL HOLDINGS, INC.

Notes to the Consolidated Financial Statements - Unaudited

Gains and losses on the sale of securities are recorded on the trade date and are determined on the ~~identifiable~~ specific basis. The following table presents the proceeds, realized gross gains and realized gross losses on sales and calls of AFS debt securities for the three and nine months ended September 30, 2023 and 2022 (in thousands):

Available-for-sale:	Three Months Ended September 30,		Nine Months Ended September 30,	
	2023	2022	2023	2022
Proceeds from sale and call of securities	\$ 6,792	\$ 13,809	\$ 15,409	\$ 45,647
Gross gains	\$ -	\$ 2	\$ 3	\$ 218
Gross losses	(955)	(560)	(979)	(758)
Net realized (loss) gain	\$ (955)	\$ (558)	\$ (976)	\$ (540)

The amortized cost and fair value of investment securities, by contractual maturity, are shown below as of the indicated (in thousands). Actual maturities may differ from contractual maturities because borrowers may have the right to call or prepay obligations with or without call or prepayment penalties. Securities not due at a single maturity date are shown separately.

September 30, 2023:	Available-for-sale		Held-to-maturity	
	Amortized Cost	Fair Value	Amortized Cost	Fair Value
Due within one year	\$ -	\$ -	\$ 19,934	\$ 19,906
After one year through five years	6,000	5,977	9,443	8,455
After five years through ten years	22,059	18,919	-	-
After ten years	21,382	15,396	-	-
Government Agency	9,913	8,025	44,087	37,049
Collateralized mortgage obligations	105,547	78,571	64,094	53,786
Mortgage-backed securities - residential	66,024	51,157	44,302	38,214
Mortgage-backed securities - commercial	48,010	40,564	15,467	13,884
	<u>\$ 278,935</u>	<u>\$ 218,609</u>	<u>\$ 197,327</u>	<u>\$ 171,294</u>

At September 30, 2023, there were no securities held in the portfolio from any one issuer in an amount greater than 10% of total stockholders' equity other than the United States Government and Government Agency securities. All collateralized mortgage obligations and mortgage-backed securities are issued by United States sponsored entities as of September 30, 2023 and December 31, 2022.

Information pertaining to investment securities with gross unrealized losses, aggregated by investment category length of time that those individual securities have been in a continuous loss position, are presented as of the following (thousands):

	September 30, 2023					
	Less than 12 months		12 months or more		Total	
	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses	Fair Value	
U.S. Government Agency	\$ -	-	45,075	(10,184)	\$ 45,075	\$ (10,184)
U.S.	19,906	(28)	-	-	19,906	(28)
Collateralized mortgage obligations	-	-	132,357	(41,869)	132,357	(41,869)
Mortgage-backed securities - residential	5,362	(237)	84,009	(23,353)	89,371	(23,590)
Mortgage-backed securities - commercial	20,006	(917)	32,923	(9,656)	52,929	(10,573)
Bank subordinated debt	9,611	(304)	11,560	(1,941)	21,171	(2,245)
Corporate bonds	-	-	8,454	(631)	8,454	(631)
	<u>\$ 54,885</u>	<u>\$ (1,486)</u>	<u>\$ 332,494</u>	<u>\$ (94,542)</u>	<u>\$ 387,379</u>	<u>\$ (96,028)</u>

[Table of Contents](#)

USCB FINANCIAL HOLDINGS, INC.
Notes to the Consolidated Financial Statements - Unaudited

	December 31, 2022					
	Less than 12 months		12 months or more		Total	
	<u>Fair Value</u>	<u>Unrealized Losses</u>	<u>Fair Value</u>	<u>Unrealized Losses</u>	<u>Fair Value</u>	<u>Unrealized Losses</u>
U.S. Government Agency	\$ 11,407	(1,093)	36,310	(7,616)	47,717	\$ (8,709)
U.S.	9,828	(13)	-	-	9,828	(13)
Collateralized mortgage	16,500	(963)	139,965	(34,962)	156,465	(35,925)
Mortgage-backed securities - residential	5,059	(564)	91,742	(19,348)	96,801	(19,912)
Mortgage-backed securities -	10,052	(1,173)	26,823	(5,300)	36,875	(6,473)
Municipal securities	-	-	18,483	(6,601)	18,483	(6,601)
Bank subordinated debt	11,295	(670)	2,619	(381)	13,914	(1,051)
Corporate bonds	13,723	(926)	-	-	13,723	(926)
	<u>\$ 77,864</u>	<u>\$ (5,402)</u>	<u>\$ 315,942</u>	<u>\$ (74,208)</u>	<u>\$ 393,806</u>	<u>\$ (79,610)</u>

As of September 30, 2023, the unrealized losses associated with \$8.5 million of investment securities transferred from the AFS portfolio to the HTM portfolio represent unrealized losses since the date of purchase, independent of changes in the cost basis of the securities upon transfer between portfolios.

ASC Topic 326 amended the existing other-than-temporary-impairment guidance for AFS securities, requiring losses to be recorded as an allowance rather than through a permanent write-down. When evaluating AFS debt securities under ASC Topic 326, the Company has evaluated whether the decline in fair value is attributed to credit losses or factors like interest rate risk, using both quantitative and qualitative analyses, including company performance analysis of credit ratings, remaining payment terms, prepayment speeds and analysis of macro-economic conditions. Each investment is expected to recover its price depreciation over its holding period as it moves to maturity and the Company's intent and ability to hold these securities to maturity if necessary. As a result of this evaluation, the Company concluded that no allowance was required on AFS securities.

At September 30, 2023, the Company had \$73 million of unrealized losses on mortgage-backed securities collateralized mortgage obligations of government sponsored entities having a fair value \$66.8 million that were attributable to a combination of factors, including relative changes in interest rates since the time of purchase.

At December 31, 2022, the Company had \$37 million of unrealized losses on mortgage backed securities collateralized mortgage obligations of government sponsored entities having a fair value \$66.6 million that were attributable to a combination of factors, including relative changes in interest rates since the time of purchase.

The contractual cash flows for these securities are guaranteed by U.S. government agencies and U.S. sponsored entities. The municipal bonds are of high credit quality and the declines in fair value are not due to credit quality. Based on the assessment of these mitigating factors, management believed that the unrealized losses on these holdings are a function of changes in investment spreads and interest rate movements and not changes in credit quality. Management expects to recover the entire amortized cost basis of these securities.

At September 30, 2023, the Company does not intend to sell debt securities that are in an unrealized loss position and it is not more than likely that the Company will be required to sell these securities before recovery of the amortized cost basis. Therefore, management does not consider any investment to be other than temporarily impaired at September 30, 2023.

Pledged Securities

The Company maintains a master repurchase agreement with a public banking institution for up to \$0.0 million fully guaranteed with investment securities upon withdrawal. Any amounts borrowed would be at a variable interest rate based on prevailing rates at the time funding is requested. As of September 30, 2023, the Company did not have any securities pledged under this agreement.

The Bank is a Qualified Public Depository ("QPD") with the State of Florida. As a QPD, the Bank has the legal authority to maintain public deposits from cities, municipalities, and the State of Florida. These public deposits are securities pledged to the State of Florida at a ratio of 25% of the outstanding uninsured deposits. The Bank must maintain a minimum amount of pledged securities to be in the public funds program.

[Table of Contents](#)**USCB FINANCIAL HOLDINGS, INC.**

Notes to the Consolidated Financial Statements - Unaudited

As of September 30, 2023, the Bank had a total ~~202.8~~ million in deposits under the public funds program pledged to the State of Florida for these public funds were twenty-seven bonds with an aggregate fair value of \$82.6 million.

As of December 31, 2022, the Bank had a total of \$804.2 million in deposits under the public funds program and pledged to the State of Florida for these public funds were eighteen corporate bonds with an aggregate fair value of \$ 49.0 million.

The Board of Governors of the Federal Reserve System, on March 12, 2023, announced the creation of a new Term Funding Program (BTFP). The BTFP offers loans of up to one year in length to banks, savings associations, credit unions, and other eligible depository institutions pledging U.S. Treasuries, U.S. agency debt and mortgage-backed securities, and other qualifying assets as collateral. These assets will be valued at par.

The Company had no borrowing under the BTFP program as of September 30, 2023, and had pledged \$134.4 million in securities measured at par to the Federal Reserve Bank of Atlanta for the BTFP program.

3. LOANS

On January 1, 2023, the Company adopted FASB ASC Topic 326 using the modified retrospective accounting methodology the amendments of FASB ASU 2016-13. Through the adoption of CECL, the Company developed a credit losses ("ACL") methodology that replaces its previous allowance for loan losses methodology. See the ACL section in this note for further information regarding the Company's ACL. Prior periods balance for ACL are presented under legacy GAAP and may not be comparable to current period presentation.

The following table is a summary of the distribution of loans held for investment by type (in thousands):

	September 30, 2023		December 31, 2022	
	Total	Percent of Total	Total	Percent of Total
Residential Real Estate	\$ 188,880	11.3 %	\$ 185,636	12.3 %
Commercial Real Estate	1,005,280	60.0 %	970,410	64.4 %
Commercial and Industrial	212,975	12.7 %	126,984	8.4 %
Foreign	94,640	5.7 %	93,769	6.2 %
Banker and Other	173,096	10.3 %	130,429	8.7 %
Total gross loans	1,674,871	100.0 %	1,507,228	100.0 %
Plus: Deferred fees (cost)	1,649		110	
Total loans net of deferred fees (cost)	1,676,520		1,507,338	
Less: Allowance for credit losses	19,493		17,487	
Net loans	\$ 1,657,027		\$ 1,489,851	

At September 30, 2023 and December 31, 2022, the Company had \$556.1 million and \$338.1 million, respectively, of commercial real estate and residential mortgage loans pledged as collateral for lines of credit with the FHLB and the Federal Reserve Bank of Atlanta.

The Company was a participant in the Small Business Administration's ("SBA") Paycheck Protection Program ("PPP") loans. These loans were designed to provide a direct incentive for small businesses to keep their workers on payroll funds had to be used towards payroll cost, mortgage interest, rent, utilities and other costs related to COVID-19. These loans are forgivable under specific criteria as determined by the SBA. The Company had PPP loans totaling \$ 295 thousand at September 30, 2023 and \$ 1.3 million at December 31, 2022, which are categorized as commercial and industrial loans.

The Company recognized \$6 thousand and \$ 1.6 million in PPP loan fees and interest income during the nine months ended September 30, 2023 and 2022, respectively, which is reported under loans, including fees, within the Consolidated Statements of Operations.

Allowance for Credit Losses

In general, the Company utilizes the Discounted Cash Flow (DCF) method or the Remaining Life (WARM) methodology to estimate the quantitative portion of the ACL for loan pools. The DCF uses a loss driver analysis (LDA) and ~~deloitte~~ analyses. Management engaged advisors and consultants with expertise in CECL model development to assist

[Table of Contents](#)

USCB FINANCIAL HOLDINGS, INC.

Notes to the Consolidated Financial Statements - Unaudited

in development of a loss driver analysis based on regression models and supportable forecast. Peer group data obtained from FFIEC Call Report filings is used to inform regression analyses to quantify the impact of reasonable and supportable forecasts in projective models. Economic forecasts applied to regression models to estimate probability of default for loan receivables use at least one of the following economic indicators: civilian unemployment rate (national), real gross domestic product growth (national GDP) and/or the HPI. For each of the segments in which the WARM methodology is used, the long-term average loss rate is calculated and applied on a quarterly basis for the remaining life of the pool. Adjustments for economic expectations are made through qualitative factors.

Qualitative factors ("Q-Factors") used in the ACL methodology include:

- Changes in lending policies, procedures, and strategy
- Changes in international, national, regional, and local conditions
- Changes in nature and volume of portfolio
- Changes in the volume and severity of past due loans and other similar conditions
- Concentration risk
- Changes in the value of underlying collateral
- Effect of other external factors: e.g., competition, legal, and regulatory requirements
- Changes in lending management, among others

ACL for the three and nine months ended September 30, 2023, was estimated under the CECL methodology, and for all periods in 2022, it was estimated under the incurred loss model.

Changes in the allowance for credit losses for the three and nine months ended September 30, 2023 and 2022 were as follows (in thousands):

	Residential Real Estate	Commercial Real Estate	Commercial and Industrial	Foreign Banks	Consumer and Other	Total
Three Months Ended September 30, 2023						
Beginning balance	\$ 2,673	\$ 10,183	\$ 2,500	\$ 677	\$ 2,782	\$ 18,815
Provision for credit ⁽¹⁾	(162)	(84)	738	73	108	673
Recoveries	-	-	8	-	-	8
Charge-offs	-	-	-	-	(3)	(3)
Ending Balance	<u>\$ 2,511</u>	<u>\$ 10,099</u>	<u>\$ 3,246</u>	<u>\$ 750</u>	<u>\$ 2,887</u>	<u>\$ 19,493</u>
Nine Months Ended September 30, 2023						
Beginning balance	\$ 1,352	\$ 10,143	\$ 4,163	\$ 720	\$ 1,109	\$ 17,487
Cumulative effect of adoption of ⁽²⁾	1,238	1,105	(2,158)	23	858	1,066
Provision for credit ⁽³⁾	(89)	(1,149)	1,181	7	965	915
Recoveries	10	-	60	-	3	73
Charge-offs	-	-	-	-	(48)	(48)
Ending Balance	<u>\$ 2,511</u>	<u>\$ 10,099</u>	<u>\$ 3,246</u>	<u>\$ 750</u>	<u>\$ 2,887</u>	<u>\$ 19,493</u>

(1) Provision for credit losses excludes 17 thousand release due to unfunded commitments included in other liabilities and 3 thousand release due to investment securities held to maturity.

(2) Impact of CECL adoption on January 1, 2023.

(3) Provision for credit losses excludes 39 thousand release due to unfunded commitments included in other liabilities and 16 thousand expense due to investment securities held to maturity.

[Table of Contents](#)

USCB FINANCIAL HOLDINGS, INC.

Notes to the Consolidated Financial Statements - Unaudited

	Residential Real Estate	Commercial Real Estate	Commercial and Industrial	Foreign Banks	Consumer and Other	Total
Three Months Ended September 30, 2022						
Beginning balance	\$ 2,366	\$ 9,290	\$ 2,671	\$ 651	\$ 808	\$ 15,786
Provision for credit	(1,009)	695	1,126	74	24	910
Recoveries	1	-	-	-	-	1
Charge-offs	-	-	(88)	-	(5)	(93)
Ending	<u>\$ 1,358</u>	<u>\$ 9,985</u>	<u>\$ 3,709</u>	<u>\$ 725</u>	<u>\$ 827</u>	<u>\$ 16,604</u>
Balance						
Nine Months Ended September 30, 2022						
Beginning balance	\$ 2,498	\$ 8,758	\$ 2,775	\$ 457	\$ 569	\$ 15,057
Provision for credit	(1,157)	1,227	1,011	268	266	1,615
Recoveries	33	-	11	-	3	47
Charge-offs	(16)	-	(88)	-	(11)	(115)
Ending	<u>\$ 1,358</u>	<u>\$ 9,985</u>	<u>\$ 3,709</u>	<u>\$ 725</u>	<u>\$ 827</u>	<u>\$ 16,604</u>
Balance						

At September 30, 2023 the ACL, under the CECL methodology, was \$5.5 million compared to \$7.5 million at December 31, 2022, under the incurred loss methodology. The increase of \$20 million was composed of a \$1.1 million impact of adoption of the ASU 2016-13 on loan receivables, a \$ 915 thousand increase in the ACL for loan receivables due to loan growth and to net charge-offs.

The Company had charge offs totaling \$3 thousand for the quarter ended September 30, 2023 related to originated in 2023. The Company had charge offs totaling \$8 thousand for the nine months ended September 30, 2023 related to loans. \$27 thousand was related to loans originated in 2023 and \$ 21 thousand of charge offs was related to loans originated in 2015.

The Company had charge offs totaling \$15.0 thousand for the nine months ended September 30, 2022, on \$15.6 thousand and \$87.7 thousand of charge offs related to loans that were originated in 2004 and 2019, \$10.9 thousand of charge offs related to loans that were originated in 2022.

The Federal Open Market Committee ("FOMC") economic forecasts as of September 30, 2023, showed improvements in unemployment and a slower real GDP growth. Fannie Mae HPI forecast reflected important improvement in national housing prices over the next four quarters. The Company continued to adjust the HPI index effect on 1-4 Family loan portfolio with a qualitative factor because Florida housing prices are performing better than national levels. Q-Factors were reviewed and updated; maximum loss calculations are based on refreshed stress test and risk statuses were updated based on portfolio and external developments during the third quarter.

[Table of Contents](#)

USCB FINANCIAL HOLDINGS, INC.
Notes to the Consolidated Financial Statements - Unaudited

The ACL and the outstanding balances in the specified loan categories as of September 30, 2023 and December 31, 2022 are as follows (in thousands):

	<u>Residential Real Estate</u>	<u>Commercial Real Estate</u>	<u>Commercial and Industrial</u>	<u>Foreign Banks</u>	<u>Consumer and Other</u>	<u>Total</u>
September 30, 2023:						
Allowance for credit losses:						
Individually evaluated for	\$ 146	\$ -	\$ 135	\$ -	\$ -	\$ 281
Collectively evaluated for	<u>2,365</u>	<u>10,099</u>	<u>3,111</u>	<u>750</u>	<u>2,887</u>	<u>19,212</u>
Balance end of period	<u><u>2,511</u></u>	<u><u>\$ 10,099</u></u>	<u><u>3,246</u></u>	<u><u>\$ 750</u></u>	<u><u>2,887</u></u>	<u><u>\$ 19,493</u></u>
Loans:						
Individually evaluated for	\$ 6,749	\$ -	\$ 869	\$ -	\$ -	\$ 7,618
Collectively evaluated for	<u>182,131</u>	<u>1,005,280</u>	<u>212,106</u>	<u>94,640</u>	<u>173,096</u>	<u>1,667,253</u>
Balance end of period	<u><u>188,880</u></u>	<u><u>\$ 1,005,280</u></u>	<u><u>212,975</u></u>	<u><u>\$ 94,640</u></u>	<u><u>\$ 173,096</u></u>	<u><u>\$ 1,674,871</u></u>
December 31, 2022:						
Allowance for credit losses:						
Individually evaluated for	\$ 155	\$ -	\$ 41	\$ -	\$ 98	\$ 294
Collectively evaluated for	<u>1,197</u>	<u>10,143</u>	<u>4,122</u>	<u>720</u>	<u>1,011</u>	<u>17,193</u>
Balance end of period	<u><u>1,352</u></u>	<u><u>\$ 10,143</u></u>	<u><u>4,163</u></u>	<u><u>\$ 720</u></u>	<u><u>\$ 1,109</u></u>	<u><u>\$ 17,487</u></u>
Loans:						
Individually evaluated for	\$ 7,206	\$ 393	\$ 82	\$ -	\$ 196	\$ 7,877
Collectively evaluated for	<u>178,430</u>	<u>970,017</u>	<u>126,902</u>	<u>93,769</u>	<u>130,233</u>	<u>1,499,351</u>
Balance end of period	<u><u>185,636</u></u>	<u><u>\$ 970,410</u></u>	<u><u>\$ 126,984</u></u>	<u><u>\$ 93,769</u></u>	<u><u>\$ 130,429</u></u>	<u><u>\$ 1,507,228</u></u>

Credit Quality Indicators

The Company grades loans based on the estimated capability of the borrower to repay the contractual obligation of the loan agreement based on relevant information which may include: current financial information on the borrower, historical payment experience, credit documentation and other current economic trends. Internal credit risk grades are **preauthorized**.

The Company's internally assigned credit risk grades are as follows:

Pass – Loans indicate different levels of satisfactory financial condition and performance.

Special Mention – Loans classified as special mention have a potential weakness that deserves management's close attention. If left uncorrected, these potential weaknesses may result in deterioration of the repayment prospects for the loan or of the institution's credit position at some future date.

Substandard – Loans classified as substandard are inadequately protected by the current net worth and paying capacity of the obligator or of the collateral pledged, if any. Loans so classified have a well-defined weakness or weaknesses that jeopardize the liquidation of the debt. They are characterized by the distinct possibility that the institution will sustain some loss if the deficiencies are not corrected.

Doubtful – Loans classified as doubtful have all the weaknesses inherent in those classified at substandard, with the added characteristic that the weaknesses make collection or liquidation in full on the basis of currently existing facts, conditions, and values, highly questionable and improbable.

Loss – Loans classified as loss are considered uncollectible.

[Table of Contents](#)

USCB FINANCIAL HOLDINGS, INC.
Notes to the Consolidated Financial Statements - Unaudited

Loan credit exposures by internally assigned grades are presented below for the periods indicated (in thousands):

	As of September 30, 2023							
	Term Loans by Origination							Revolving Loans
	Year		2023		2022		2021	
	2023	2022	2021	2020	2019	Prior	Revolving Loans	Total
Residential real estate								
Pass	\$ 17,760	\$ 36,828	\$ 26,315	\$ 6,527	\$ 9,749	\$ 83,244	\$ 8,457	\$ 188,880
Total	17,760	36,828	26,315	6,527	9,749	83,244	8,457	188,880
Commercial real estate								
Pass	78,285	340,524	210,028	104,816	79,129	186,669	3,314	1,002,765
Substandard	-	-	1,818	697	-	-	-	2,515
Total	78,285	340,524	211,846	105,513	79,129	186,669	3,314	1,005,280
Commercial and industrial								
Pass	92,156	38,012	34,581	7,141	14,001	3,483	21,617	210,991
Substandard	-	-	340	-	1,344	-	300	1,984
Total	92,156	38,012	34,921	7,141	15,345	3,483	21,917	212,975
Foreign banks								
Pass	93,515	1,125	-	-	-	-	-	94,640
Total	93,515	1,125	-	-	-	-	-	94,640
Consumer and others								
Pass	50,027	74,961	44,249	717	529	1,396	1,217	173,096
Substandard	-	-	-	-	-	-	-	-
Total	50,027	74,961	44,249	717	529	1,396	1,217	173,096
Total Loans								
Pass	331,743	491,450	315,173	119,201	103,408	274,792	34,605	1,670,372
Special Mention	-	-	-	-	-	-	-	-
Substandard	-	-	2,158	697	1,344	-	300	4,499
Doubtful	-	-	-	-	-	-	-	-
Total	\$ 331,743	\$ 491,450	\$ 317,331	\$ 119,898	\$ 104,752	\$ 274,792	\$ 34,905	\$ 1,674,871

[Table of Contents](#)**USCB FINANCIAL HOLDINGS, INC.**
Notes to the Consolidated Financial Statements - Unaudited

	As of December 31, 2022					
	Pass	Special Mention	Substandard	Doubtful	Total Loans	
Residential real estate:						
Home equity line of credit and Multi-family	\$ 623	\$ -	\$ -	\$ -	\$ 623	
Condo	132,178	-	-	-	132,178	
Commercial residential	52,835	-	-	-	52,835	
	185,636	-	-	-	185,636	
Commercial real estate:						
Land and construction	38,687	-	-	-	38,687	
Multi-family residential	176,820	-	-	-	176,820	
Condo	49,601	-	393	-	49,994	
Commercial property	702,357	-	2,552	-	704,909	
	967,465	-	2,945	-	970,410	
Commercial and Industrial	120,873	-	807	-	121,680	
Unsecured	5,304	-	-	-	5,304	
	126,177	-	807	-	126,984	
Foreign banks	93,769	-	-	-	93,769	
Consumer and other loans	130,233	-	196	-	130,429	
Total	\$ 1,503,280	\$ -	\$ 3,948	\$ -	\$ 1,507,228	

[Table of Contents](#)

USCB FINANCIAL HOLDINGS, INC.
Notes to the Consolidated Financial Statements - Unaudited

Loan Aging

The Company also considers the performance of loans in grading and in evaluating the credit quality of the loan. The Company analyzes credit quality and loan grades based on payment performance and the aging status of the loans. The following tables include an aging analysis of accruing loans and total non-accruing loans as of September 30, 2023 (December 31, 2022) (in thousands):

As of September 30, 2023	Accruing						Total Loans	
	Current	Past Due 30-89 Days	Past Due 90 Days or > and Still Accruing		Total Accruing	Non-Accrual		
			Accruing	Non-Accrual				
Residential real estate:								
Home equity line of credit and other family	\$ 491	\$ -	\$ -	\$ 491	\$ -	\$ 491		
Condominiums	138,069	-	-	138,069	-	138,069		
Single family residential	49,949	371	-	50,320	-	50,320		
	188,509	371	-	188,880	-	188,880		
Commercial real estate:								
Land and construction	30,717	-	-	30,717	-	30,717		
Multi-family residential	177,573	-	-	177,573	-	177,573		
Condo	58,100	-	-	58,100	-	58,100		
Commercial property	738,849	-	-	738,849	-	738,849		
Leasehold improvements	41	-	-	41	-	41		
	1,005,280	-	-	1,005,280	-	1,005,280		
Commercial and injected								
Unsecured	194,119	-	-	194,119	479	194,598		
	18,377	-	-	18,377	-	18,377		
	212,496	-	-	212,496	479	212,975		
Foreign banks	94,640	-	-	94,640	-	94,640		
Consumer and other	173,096	-	-	173,096	-	173,096		
Total	\$ 1,674,021	\$ 371	\$ -	\$ 1,674,392	\$ 479	\$ 1,674,871		

[Table of Contents](#)

USCB FINANCIAL HOLDINGS, INC.
Notes to the Consolidated Financial Statements - Unaudited

As of December 31, 2023	Accruing						Total Loans	
	Current	Past Due 30-89 Days	Past Due 90 Days or > and Still Accruing	Total Accruing		Non-Accrual		
				Accruing	Non-Accrual			
Dental real estate:								
Home equity line of credit and other family	\$ 623	\$ -	\$ -	\$ 623	\$ -	\$ 623	\$ 623	
Condominium	131,120	1,058	-	132,178	-	132,178		
Commercial residential	50,310	2,525	-	52,835	-	52,835		
	182,053	3,583	-	185,636	-	185,636		
Commercial real estate:								
Land and construction	38,687	-	-	38,687	-	38,687		
Multi-family residential	176,820	-	-	176,820	-	176,820		
Condo	49,994	-	-	49,994	-	49,994		
Commercial property	704,884	25	-	704,909	-	704,909		
Leasehold improvements	-	-	-	-	-	-	970,410	
Commercial and industrial	121,649	31	-	121,680	-	121,680		
Unsecured	4,332	972	-	5,304	-	5,304		
	125,981	1,003	-	126,984	-	126,984		
Foreign banks	93,769	-	-	93,769	-	93,769		
Consumer and other	130,169	260	-	130,429	-	130,429		
Total	<u>\$ 1,502,357</u>	<u>\$ 4,871</u>	<u>\$ -</u>	<u>\$ 1,507,228</u>	<u>\$ -</u>	<u>\$ 1,507,228</u>		

Non-accrual Status

The following table includes the amortized cost basis of loans on non-accrual status and loans past due over 90 days and still accruing as of September 30, 2023 (in thousands):

	September 30, 2023				
	Nonaccrual Loans With No Related Allowance	Nonaccrual Loans With Related Allowance	Total Nonaccruals	Loans Past Over Days and Still Accruing	
				Days	Over
Residential real estate	\$ -	\$ -	\$ -	\$ -	\$ -
Commercial real estate	-	-	-	-	-
Commercial and industrial	-	479	479	-	-
Consumer and other	\$ -	\$ 479	\$ 479	\$ -	\$ -

The Company did not have loans in nonaccrual status as of December 31, 2022.

Accrued interest receivable is excluded from the estimate of credit losses. There was no interest income recognized attributable to non-accrual loans outstanding during the three months ended September 30, 2023 and 2022. Interest income on these loans for the three months ended September 30, 2023 and 2022, would have been approximately \$12 thousand and \$0 thousand, respectively, had these loans performed in accordance with their original terms. Interest income on these loans for the nine months ended September 30, 2023 and 2022, would have been approximately \$28 thousand and \$0 thousand, respectively, had these loans performed in accordance with their original terms.

[Table of Contents](#)

USCB FINANCIAL HOLDINGS, INC.
Notes to the Consolidated Financial Statements - Unaudited

Collateral-Dependent Loans

A loan is collateral dependent when the borrower is experiencing financial difficulty and repayment of the ~~expected to~~ is provided substantially through the sale or operation of the collateral. There ~~were~~ were collateral dependent loans as of September 30, 2023, or as of December 31, 2022.

Impaired Loans

The following table includes the unpaid principal balances for impaired loans with the associated allowance amount, if applicable, on the basis of impairment methodology as of December 31, 2022 (in thousands):

	December 31, 2022		
	Unpaid Principal Balance	Net Investment Balance	Valuation Allowance
Impaired Loans with No Specific Allowance			
Residential real estate	\$ 3,551	\$ 3,544	-
Commercial real estate	393	393	-
	<u>3,944</u>	<u>3,937</u>	-
Impaired Loans with Specific Allowance			
Residential real estate	3,655	3,626	155
Commercial and industrial	82	82	41
Consumer and other	196	196	98
	<u>3,933</u>	<u>3,904</u>	<u>294</u>
Total	<u><u>\$ 7,877</u></u>	<u><u>\$ 7,841</u></u>	<u><u>\$ 294</u></u>

Net investment balance is the unpaid principal balance of the loan adjusted for the remaining net deferred loan fees.

The following table presents the average recorded investment balance on impaired loans for the periods indicated (in thousands):

	Three Months Ended September 30, 2022	Nine Months Ended September 30, 2022
Residential real estate	\$ 7,282	\$ 7,732
Commercial real estate	590	619
Commercial and industrial	95	116
Consumer and other	207	214
Total	<u>\$ 8,174</u>	<u>\$ 8,681</u>

Interest income recognized on impaired loans for the three months ended September 30, 2022 was \$ 90 thousand and for the nine months ended September 30, 2022 was \$ 271 thousand.

Loan Modifications to Borrowers Experiencing Financial Difficulties

The following table presents newly restructured loans, by type of modification, which occurred during the nine months ended September 30, 2023 (in thousands):

	Recorded Investment Prior to Modification			Recorded Investment After Modification		
	Number of Loans	Combination Modifications	Total Modifications	Number of Loans	Combination Modifications	Total Modifications
Residential real estate	- \$	- \$	-	- \$	- \$	-
Commercial real estate	-	-	-	-	-	-
Commercial and industrial	1	350	350	1	350	350
Consumer and other	-	-	-	-	-	-
	<u>1</u>	<u>\$ 350</u>	<u>\$ 350</u>	<u>1</u>	<u>\$ 350</u>	<u>\$ 350</u>

[Table of Contents](#)**USCB FINANCIAL HOLDINGS, INC.**
Notes to the Consolidated Financial Statements - Unaudited

The Company had no new modifications and one new modifications to borrowers experiencing financial difficulties for the three and nine months ended September 30, 2023, respectively. There were existing loan modifications that subsequently defaulted during the three and nine months ended September 30, 2023.

4. INCOME TAXES

The Company's provision for income taxes is presented in the following table for the dates indicated (in thousands):

	Nine Months Ended September 30,	
	2023	2022
Current:		
Federal	\$ -	\$ -
State	-	-
Total current	-	-
Deferred:		
Federal	3,510	4,342
State	954	1,187
Total deferred	4,464	5,529
Total tax expense	\$ 4,464	\$ 5,529

The actual income tax expense for the nine months ended September 30, 2023 and 2022 differs from the statutory tax expense for the period (computed by applying the U.S. federal corporate tax rate 21% for 2023 and 2022 to income before provision for income taxes) as follows (in thousands):

	Nine Months Ended September 30,	
	2023	2022
Federal taxes at statutory rate	\$ 3,840	\$ 4,460
State income taxes, net of federal tax benefit	795	923
Bank owned life	(171)	(202)
Deferred	-	348
Total tax expense	\$ 4,464	\$ 5,529

The Company's deferred tax assets and deferred tax liabilities as of the dates indicated were (in thousands):

	September 30, 2023	December 31, 2022
Deferred tax assets:		
Operating	\$ 17,588	\$ 21,720
Allowance for credit losses	4,670	4,432
Unrealized losses on available for sale	3,084	3,648
Debt payable	17,723	15,193
Equity compensation	192	158
Accruals	554	373
CECL	411	723
Adoption	336	-
Deferred tax assets:	44,558	46,247
Deferred tax liabilities:		
Advised loan cost	(418)	(28)
Lease right of use	(3,084)	(3,648)
Deferred expense	(189)	(175)
Other, net	(332)	-
Deferred tax liability	(105)	(36)
Deferred tax assets	(4,128)	(3,887)
Net deferred tax assets	\$ 40,430	\$ 42,360

[Table of Contents](#)**USCB FINANCIAL HOLDINGS, INC.**
Notes to the Consolidated Financial Statements - Unaudited

The Company has approximately \$5.5 million of federal and \$8.2 million of state net operating loss carryforwards expiring in various amounts between 2031 and 2036 and which are limited to offset, to the extent permitted, future taxable earnings of the Company.

In assessing the realizability of deferred tax assets, management considers whether it is more likely than not that some portion or all of the deferred tax assets will not be realized. The ultimate realization of deferred tax assets is dependent upon generation of future taxable income during the periods in which those temporary differences become deductible. Management considers the scheduled reversal of deferred tax liabilities, projected future taxable income, and tax planning strategies in making this assessment.

The major tax jurisdictions where the Company files income tax returns are the U.S. federal jurisdiction and the State of Florida. With few exceptions, the Company is no longer subject to U.S. federal and state income tax examinations by tax authorities for years before 2019.

For the three and nine months ended September 30, 2023 and 2022, the Company did not have any unrecognized tax benefits as a result of tax positions taken during a prior period or during the current period. Additional interest or penalties were recorded as a result of tax uncertainties.

5. OFF-BALANCE SHEET ARRANGEMENTS

The Company is a party to financial instruments with off-balance-sheet risk in the normal course of business in order to meet the financial needs of its customers and to reduce its own exposure to fluctuations in interest rates. These financial instruments include unfunded commitments under lines of credit, commitments to extend credit, standby and commercial letters of credit. Those instruments involve, to varying degrees, elements of credit and interest rate risk in excess of that recognized in the Company's Consolidated Balance Sheets. The Company uses the same credit policies in making commitments and conditional obligations as it does for on-balance sheet instruments.

The Company's exposure to credit loss in the event of nonperformance by the other party to the financial instruments for unused lines of credit, and standby letters of credit is represented by the contractual amount of these commitments.

A summary of the amounts of the Company's financial instruments with off-balance sheet risk are shown September 30, 2023 and December 31, 2022 (in thousands):

	September 30, 2023	December 31, 2022
Commitments to grant loans and unfunded lines of credit	\$ 100,661	\$ 95,461
Standby and commercial letters of credit	6,490	4,320
	\$ 107,151	\$ 99,781

Commitments to extend credit are agreements to lend to a customer as long as there is no violation of any established in the contract. Commitments generally have fixed expiration dates or other termination clauses.

Unfunded lines of credit and revolving credit lines are commitments for possible future extensions of credit to existing customers. These lines of credit are uncollateralized and usually do not contain a specified maturity date and ultimately may not be drawn upon to the total extent to which the Company committed.

Standby and commercial letters of credit are conditional commitments issued by the Company to guarantee of the customer to a third party. Those letters of credit are primarily issued to support public and private borrowing arrangements. Essentially all letters of credit have fixed maturity dates and since many of them expire without being drawn upon, they do not generally present a significant liquidity risk to the Company.

6. DERIVATIVES

The Company utilizes interest rate swap agreements as part of its asset-liability management strategy to help manage its interest rate risk exposure. The notional amount of the interest rate swaps does not represent actual amounts exchanged by the parties. The amounts exchanged are determined by reference to the notional amount and the other terms of the individual interest rate swap agreements.

Interest Rate Swaps Designated as a Cash Flow Hedge

[Table of Contents](#)**USCB FINANCIAL HOLDINGS, INC.**
Notes to the Consolidated Financial Statements - Unaudited

As of September 30, 2023, the Company had two interest rate swap agreements with a notional aggregate amount of \$50 million that were designated as cash flow hedges of certificates of deposit. The interest rate swap agreements have an average maturity of 2.63 years, the weighted average fixed rate paid is 3.59%, with the weighted average 3-month compound SOFR being received. The Company had no cash flow hedges outstanding on December 31, 2022.

The changes in fair value on these interest rate swaps are recorded in other assets or other liabilities corresponding recognition in other comprehensive income (loss) and subsequently reclassified to earnings when gains or losses are realized.

Interest Rate Swaps Designated as Fair Value Hedge

As of September 30, 2023, the Company had four interest rate swap agreements with a notional aggregate amount of \$200 million that were designated as fair value hedges on loans. The interest rate swap agreements have an average 4.8 years, the weighted average fixed rate paid is 4.74%, with the weighted average 3-month compound SOFR being received.

Interest Rate Swaps

The Company enters into interest rate swaps with its loan customers. The Company had 20 and 15 interest rate swaps with loan customers with an aggregate notional amount \$46.5 million and \$3.9 million at September 30, 2023 and December 31, 2022, respectively. These interest rate swaps mature between 2025 and 2051. The Company entered into responding and offsetting derivatives with third parties. The fair value of liability on these derivatives Company to provide the counterparty with funds to be held as collateral which the Company reports as other assets under the Consolidated Balance Sheets. While these derivatives represent economic hedges, they do not qualify as hedges for accounting purposes.

The following table reflects the Company's interest rate swaps at the dates indicated (in thousands):

	Notional Amount	Collateral Amount	Balance Sheet Location	Fair Value	
				Asset	Liability
September 30, 2023:					
Derivatives designated as hedging interest rate swaps	\$ 250,000	-	Other assets	\$ 1,450	\$ 294
Derivatives not designated as hedging interest rate swaps related to customer loans	\$ 46,717	\$ 1,297	Other assets/Other liabilities	\$ 5,623	\$ 5,623
December 31, 2022:					
Derivatives not designated as hedging interest rate swaps related to customer loans	\$ 33,893	\$ 1,278	Other assets/Other liabilities	\$ 5,011	\$ 5,011

7. FAIR VALUE MEASUREMENTS**Determination of Fair Value**

The Company uses fair value measurements to record fair-value adjustments to certain assets and liabilities and determine fair value disclosures. In accordance with the fair value measurements accounting guidance, the fair value of a financial instrument is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. Fair value is best determined based upon quoted market prices; however, in many instances, there are no quoted market prices for the Company's various financial instruments. In cases where quoted market prices are not available, fair values are based on estimates using present value or other techniques. Those techniques are significantly affected by the assumptions used, including the discount rate and estimates of future cash flows. Accordingly, the fair value estimates may not be realized in an immediate settlement of the instrument.

The fair value guidance provides a consistent definition of fair value, which focuses on exit price in an orderly transaction (that is, not a forced liquidation or distressed sale) between market participants at the measurement date under current

[Table of Contents](#)**USCB FINANCIAL HOLDINGS, INC.**

Notes to the Consolidated Financial Statements - Unaudited

market conditions. If there has been a significant decrease in the volume and level of activity for the asset or liability, change in valuation technique or the use of multiple valuation techniques may be appropriate. In such instances, determining the price at which willing market participants would transact at the measurement date under current market ~~depends on~~ the facts and circumstances and requires the use of significant judgment. The fair value is a reasonable point within the range that is most representative of fair value under current market conditions.

Fair Value Hierarchy

In accordance with this guidance, the Company groups its financial assets and financial liabilities generally measured at fair value in three levels, based on the markets in which the assets and liabilities are traded, and the reliability of assumptions used to determine fair value.

Level 1 - Valuation is based on quoted prices in active markets for identical assets or liabilities that the entity ~~has the ability~~ to access at the measurement date. Level 1 assets and liabilities generally include debt ~~and~~ securities that are traded in an active exchange market. Valuations are obtained from readily available pricing sources for market transactions involving identical assets or liabilities.

Level 2 - Valuation is based on inputs other than quoted prices included within Level 1 that are observable for the asset or liability, either directly or indirectly. The valuation may be based on quoted prices for similar ~~assets~~ or quoted prices in markets that are not active; or other inputs that are observable or can be ~~by observation~~ obtained from observable market data for substantially the full term of the asset or liability.

Level 3 - Valuation is based on 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~~ is determined using pricing models, discounted cash flow methodologies, or similar techniques, as well as instruments for which determination of fair value requires significant management judgment or estimation.

A financial instrument's categorization within the valuation hierarchy is based upon the lowest level of input ~~significantly to~~ the fair value measurement.

Items Measured at Fair Value on a Recurring Basis

AFS investment securities: When instruments are traded in secondary markets and quoted market prices do not exist for such securities, management generally relies on prices obtained from independent vendors or third-party broker-dealers. Management reviews pricing methodologies provided by the vendors and third-party broker-dealers in order to determine if observable market information is being utilized. Securities measured with pricing provided by independent vendors or third-party broker-dealers are classified within Level 2 of the hierarchy and often involve using quoted market prices for similar securities, pricing models or discounted cash flow analyses utilizing inputs observable in the market where available.

Derivatives: The fair value of derivatives are measured with pricing provided by third-party participants classified within ~~Level 2 and~~ the hierarchy.

[Table of Contents](#)

USCB FINANCIAL HOLDINGS, INC.

Notes to the Consolidated Financial Statements - Unaudited

The following table represents the Company's assets and liabilities measured at fair value on a recurring basis at September 30, 2023 and December 31, 2022 for each of the fair value hierarchy levels (in thousands):

	September 30, 2023				December 31, 2022			
	Level 1	Level 2	Level 3	Total	Level 1	Level 2	Level 3	Total
Investment securities available for sale								
U.S. Government Agency	\$ -	\$ 8,025	\$ -	\$ 8,025	\$ -	\$ 8,655	\$ -	\$ 8,655
Collateralized mortgage obligations	-	78,571	-	78,571	-	95,541	-	95,541
Mortgage-backed securities - residential	-	51,157	-	51,157	-	60,879	-	60,879
Mortgage-backed securities - nonresidential	-	40,564	-	40,564	-	27,954	-	27,954
Municipal securities	-	18,116	-	18,116	-	18,483	-	18,483
Bank subordinated debt	-	22,176	-	22,176	-	14,919	-	14,919
Corporate bonds	-	-	-	-	-	3,709	-	3,709
Total	-	218,609	-	218,609	-	230,140	-	230,140
Derivative assets	-	7,073	-	7,073	-	5,011	-	5,011
Total assets at fair value	\$ -	\$ 225,682	\$ -	\$ 225,682	\$ -	\$ 235,151	\$ -	\$ 235,151
Derivative liabilities	\$ -	\$ 5,917	\$ -	\$ 5,917	\$ -	\$ 5,011	\$ -	\$ 5,011
Total liabilities at fair value	\$ -	\$ 5,917	\$ -	\$ 5,917	\$ -	\$ 5,011	\$ -	\$ 5,011

Items Measured at Fair Value on a Non-recurring Basis

Individually Evaluated Loans and Impaired Loans: ASC 326 eliminates the current accounting model for impaired loans effective as of January 1, 2023. At December 31, 2022, in accordance with provisions of the loan modification individual loans with a carrying amount of approximately \$93 million were written down to their fair value approximately \$3.6 million, resulting in an impairment charge of \$94 thousand, which was included in the allowance for credit losses at December 31, 2022. Loans subject to write-downs, or impaired loans, are estimated using the present value of expected cash flows or the appraised value of the underlying collateral discounted as necessary due to management's estimates of changes in economic conditions and are considered a Level 3 valuation.

Other Real Estate: Other real estate owned is valued at the lesser of the third-party appraisals less estimate of the costs to sell or the carrying cost of the other real estate owned. Appraisals generally use the market approach valuation technique and use market observable data to formulate an opinion of the fair value of the properties. The appraiser uses professional judgment in determining the fair value of the property and the Company may also adjust the value for changes in market conditions subsequent to the valuation date when current appraisals are not available. As a consequence of the carrying cost or the third-party appraisal and adjustments therein, the fair values of the properties are considered a Level 3 valuation.

The following table represents the Company's assets measured at fair value on a non-recurring basis at September 30, 2023 and December 31, 2022 for each of the fair value hierarchy levels (in thousands):

	Level 1	Level 2	Level 3	Total
September 30, 2023:				
Individually evaluated loans	\$ -	\$ -	\$ -	\$ -
December 31, 2022:				
Impaired loans	\$ -	\$ -	\$ 3,639	\$ 3,639

The following table presents quantified information about Level 3 fair value measurements for assets measured at fair value on a non-recurring basis at December 31, 2022 (in thousands):

	Fair Value	Valuation Technique(s)	Unobservable Input(s)
December 31, 2022:			
Residential real estate	\$ 3,500	Sales comparison approach	Adj. for differences between comparable
Commercial and industrial	41	Discounted cash flow	Adj. for differences in net operating income
Consumer and other	98	Discounted cash flow	Adj. for differences in net operating income
Total impaired loans	\$ 3,639		expectations

[Table of Contents](#)**USCB FINANCIAL HOLDINGS, INC.**
Notes to the Consolidated Financial Statements - Unaudited

There were no financial liabilities measured at fair value on a non-recurring basis at September 30, 2023 December 31, 2022, and

Items Not Measured at Fair Value

The following table presents the carrying amounts and estimated fair values of financial instruments not carried at fair value as of September 30, 2023 and December 31, 2022 (in thousands):

	Carrying Amount	Fair Value Hierarchy			Fair Value Amount		
		Level 1	Level 2	Level 3			
September 30, 2023:							
Financial							
Accounts and due from banks	\$ 5,074	\$ 5,074	\$ -	\$ -	\$ 5,074		
Interest-bearing deposits in	\$ 28,361	\$ 28,361	\$ -	\$ -	\$ 28,361		
Investment securities held to maturity, net	\$ 197,311	\$ -	\$ 171,294	\$ -	\$ 171,294		
Loans held for investment,	\$ 1,657,027	\$ -	\$ -	\$ 1,606,440	\$ 1,606,440		
Accrued interest	\$ 8,920	\$ -	\$ 1,476	\$ 7,444	\$ 8,920		
Financial Liabilities:							
Demand deposits	\$ 573,546	\$ 573,546	\$ -	\$ -	\$ 573,546		
Money market and savings accounts	\$ 1,016,564	\$ 1,016,564	\$ -	\$ -	\$ 1,016,564		
Interest-bearing checking	\$ 46,537	\$ 46,537	\$ -	\$ -	\$ 46,537		
Time deposits	\$ 284,275	\$ -	\$ -	\$ 282,062	\$ 282,062		
FHLB	\$ 102,000	\$ -	\$ 98,718	\$ -	\$ 98,718		
Advances interest payable	\$ 1,206	\$ -	\$ 469	\$ 737	\$ 1,206		
December 31, 2022:							
Financial							
Accounts and due from banks	\$ 6,605	\$ 6,605	\$ -	\$ -	\$ 6,605		
Interest-bearing deposits in	\$ 47,563	\$ 47,563	\$ -	\$ -	\$ 47,563		
Investment securities held to maturity	\$ 188,699	\$ -	\$ 169,088	\$ -	\$ 169,088		
Loans held for investment,	\$ 1,489,851	\$ -	\$ -	\$ 1,436,877	\$ 1,436,877		
Accrued interest	\$ 7,546	\$ -	\$ 1,183	\$ 6,363	\$ 7,546		
Financial Liabilities:							
Demand deposits	\$ 629,776	\$ 629,776	\$ -	\$ -	\$ 629,776		
Money market and savings accounts	\$ 915,853	\$ 915,853	\$ -	\$ -	\$ 915,853		
Interest-bearing checking	\$ 66,675	\$ 66,675	\$ -	\$ -	\$ 66,675		
Time deposits	\$ 216,977	\$ -	\$ -	\$ 211,406	\$ 211,406		
FHLB	\$ 46,000	\$ -	\$ 44,547	\$ -	\$ 44,547		
Advances interest payable	\$ 229	\$ -	\$ 92	\$ 137	\$ 229		

8. STOCKHOLDERS' EQUITY**Common Stock**

In July 2021, the Bank completed the initial public offering of its Class A common stock, in which it issued and 4,606,000 shares of Class A common stock at a price of \$10.00 per share. The Bank received total net proceeds of \$40.0 million after deducting underwriting discounts and expenses.

In December 2021, the Company acquired all the issued and outstanding shares of the Class A common stock of the Bank, which at the time were the only issued and outstanding shares of the Bank's capital stock, in a share exchange (the "Reorganization") effected under the Florida Business Corporation Act. Each outstanding share of the Bank's ~~Common~~ stock, par value \$1.00 per share, formerly held by its Shareholders was converted into and exchanged for one newly issued share of the Company's Class A common stock, par value \$1.00 per share, and the Bank became the Company's wholly owned subsidiary.

[Table of Contents](#)**USCB FINANCIAL HOLDINGS, INC.**

Notes to the Consolidated Financial Statements - Unaudited

In the Reorganization, each shareholder of the Bank received securities of the same class, having substantially the same designations, rights, powers, preferences, qualifications, limitations and restrictions, as those that the shareholders of the Bank, and the Company's then current shareholders owned the same percentages of the Company's common stock as they previously owned of the Bank's common stock.

In March 2023, the Company issued 121,627 shares of Class A common stock to employees and directors as restricted stock awards pursuant to the Company's 2015 equity incentive plan. There were no stock awards issued during the quarter ended September 30, 2023 nor during the three and nine months ended September 30, 2022.

During the nine months ended September 30, 2023 the Company repurchased 577,603 shares of Class A common stock at a weighted average price per share of \$7.6 million, including transaction costs. These repurchases were made through open market pursuant to the Company's publicly announced repurchase program. No shares were repurchased during the three months ended September 30, 2023. As of September 30, 2023, 2,397 shares remained authorized for repurchase under this program.

Shares of the Company's Class A common stock issued and outstanding as of September 30, 2023 and December 31, 2022 were 19,542,290 and 20,000,753, respectively.

Dividends

Declaration of dividends by the Board is required before dividend payments are made. No dividends were approved by the Board for the common stock classes for the three months ended September 30, 2023 and 2022. Additionally, there were no dividends declared and unpaid as of September 30, 2023 and 2022.

The Company and the Bank exceeded all regulatory capital requirements and remained above "well-capitalized" as of September 30, 2023 and December 31, 2022. At September 30, 2023, the total risk-based capital ratios for the Company and the Bank were 13.10% and 13.06%, respectively.

9. EARNINGS PER SHARE

Earnings per share ("EPS") for common stock is calculated using the two-class method required for participating EPS is calculated by dividing net income (loss) available to common shareholders by the weighted-average number of common shares outstanding for the period, without consideration for common stock equivalents. Diluted EPS is computed by dividing net income (loss) available to common shareholders by the weighted-average number of shares outstanding for the period and the weighted-average number of dilutive common stock equivalents outstanding for the period determined using the treasury-stock method. For purposes of this calculation, common stock equivalents include common stock options and are only included in the calculation of diluted EPS when their effect is dilutive.

The following table reflects the calculation of net income available to common shareholders for the three months ended September 30, 2023 and 2022 (in thousands):

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2023	2022	2023	2022
Net income available to common shareholders	\$ 3,819	\$ 5,558	\$ 13,824	\$ 15,707
	<u>\$ 3,819</u>	<u>\$ 5,558</u>	<u>\$ 13,824</u>	<u>\$ 15,707</u>

[Table of Contents](#)

USCB FINANCIAL HOLDINGS, INC.
Notes to the Consolidated Financial Statements - Unaudited

The following table reflects the calculation of basic and diluted earnings per common share class for the three and nine months ended September 30, 2023 and 2022 (in thousands, except per share amounts):

	<u>Three Months Ended September 30,</u>	
	<u>2023</u>	<u>2022</u>
	<u>Class A</u>	<u>Class A</u>
Basic EPS		
Numerator:		
Net income available to common shares	\$ 3,819	\$ 5,558
Denominator:		
Weighted average shares	19,542,723	20,000,753
Earnings per share, basic	<u>\$ 0.20</u>	<u>\$ 0.28</u>
Diluted EPS		
Numerator:		
Net income available to common	\$ 3,819	\$ 5,558
Denominator:		
Weighted average shares outstanding for basic	19,542,723	20,000,753
ADS Dilutive effects of assumed exercises of stock options	69,174	147,455
Weighted avg. shares including dilutive potential common shares	19,611,897	20,148,208
Earnings per share, diluted	<u>\$ 0.19</u>	<u>\$ 0.28</u>
Anti-dilutive stock options excluded from diluted EPS	720,500	15,000

Net income has not been allocated to unvested restricted stock awards that are participating securities because the amounts that would be allocated are not material to net income per share of common stock. Unvested restricted stock awards that are participating securities represent less than one percent of all of the outstanding shares of common stock for each of the periods presented.

	<u>Nine Months Ended September 30,</u>	
	<u>2023</u>	<u>2022</u>
	<u>Class A</u>	<u>Class A</u>
Basic EPS		
Numerator:		
Net income available to common	\$ 13,824	\$ 15,707
Denominator:		
Weighted average shares	19,661,685	19,998,841
Earnings per share, basic	<u>\$ 0.70</u>	<u>\$ 0.79</u>
Diluted EPS		
Numerator:		
Net income available to common	\$ 13,824	\$ 15,707
Denominator:		
Weighted average shares outstanding for basic	19,661,685	19,998,841
ADS Dilutive effects of assumed exercises of stock options	67,496	179,248
Weighted avg. shares including dilutive potential common shares	19,729,181	20,178,089
Earnings per share, diluted	<u>\$ 0.70</u>	<u>\$ 0.78</u>
Anti-dilutive stock options excluded from diluted EPS	720,500	15,000

Net income has not been allocated to unvested restricted stock awards that are participating securities because the amounts that would be allocated are not material to net income per share of common stock. Unvested restricted stock awards that are participating securities represent less than one percent of the outstanding shares of common stock for each of the periods presented.

[Table of Contents](#)

USCB FINANCIAL HOLDINGS, INC.
Notes to the Consolidated Financial Statements - Unaudited

10. LOSS CONTINGENCIES

Loss contingencies, including claims and legal actions may arise in the ordinary course of business. In the opinion management, none of these actions, either individually or in the aggregate, is expected to have a material adverse effect on the Company's Consolidated Financial Statements.

As previously disclosed, on July 13, 2023, three individual shareholders ("The Plaintiffs") filed a complaint against six board members serving in July 2021, without naming the Bank as a party, alleging the named directors did not have the authority to approve the exchange of preferred stock in July 2021 as part of the Bank's initial public offering and that further, such action breached their fiduciary duties. The Plaintiffs claim this exchange was not permitted by the Bank's Articles of Incorporation. The Company believes that the allegations in the lawsuit are legally and factually without merit, ~~and~~ Company intends to vigorously defend against the allegations in the lawsuit. Despite the Company's belief the lawsuit lacks merit, if the plaintiffs were successful, the Court could award substantial compensatory damages.

[Table of Contents](#)

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

The following discussion and analysis is designed to provide a better understanding of the consolidated financial condition and results of operations of the Company and the Bank, its wholly owned subsidiary, for the quarter and nine months ended September 30, 2023. This discussion and analysis is best read in conjunction with the unaudited consolidated financial statements and related footnotes included in this Quarterly Report on Form 10-Q ("Form 10-Q") and the audited consolidated financial statements and related footnotes included in the Annual Report on Form 10-K/A ("2022 Form 10-K/A") filed with the Securities and Exchange Commission ("SEC") for the year ended December 31, 2022.

This discussion contains forward-looking statements that involve risks, uncertainties and assumptions that could cause actual results to differ materially from management's expectations. Factors that could cause such differences are discussed in the sections entitled "Forward-Looking Statements" and Item 1A "Risk Factors" below and in the 2022 Form 10-K/A filed with the SEC which is available at the SEC's website www.sec.gov.

Throughout this document, references to "we," "us," "our," and "the Company" generally refer to USCB Financial Holdings, Inc.

Forward-Looking Statements

This Form 10-Q contains statements that are not historical in nature and are intended to be, and are hereby identified as, forward-looking statements for purposes of the safe harbor provided by Section 21E of the Securities Exchange Act of 1934, as amended (Exchange Act). The words "may," "will," "anticipate," "should," "would," "believe," "contemplate," "expect," "aim," "plan," "estimate," "continue," and "intend," as well as other similar words and expressions of the future, are intended to identify forward-looking statements. These forward-looking statements include, but are not limited to, statements related to our projected growth, anticipated future financial performance, and management's long-term performance goals, as well as statements relating to the anticipated effects on results of operations and financial condition from expected developments or events, or business and growth strategies, including anticipated internal growth and balance sheet restructuring.

These forward-looking statements involve significant risks and uncertainties that could cause our actual results to differ materially from those anticipated in such statements. Potential risks and uncertainties include, but are not limited to:

- the strength of the United States economy in general and the strength of the local economies in which we conduct operations to successfully manage interest rate risk, credit risk, liquidity risk, and other risks inherent to our business;
- the accuracy of our financial statement estimates and assumptions, including the estimates used for our credit loss reserve and deferred tax asset valuation allowance;
- the efficiency and effectiveness of our internal control procedures and processes to comply with the extensive laws and regulations to which we are subject, including the laws for each jurisdiction we operate in;
- changes or conditions in capital and financial markets, including actual or potential stresses in the banking industry, deposit attrition and the level of our uninsured deposits;
- the effects of legislative or regulatory changes and changes in accounting principles, policies, practices or guidelines, including the on-going effects of the implementation of the Current Expected Credit Losses ("CECL");
- the standard of a significantly diversified loan portfolio and the concentration in the South Florida market, including the risks of geographic, depositor, and industry concentrations, including our concentration in loans secured by real estate, in particular real estate;
- the effects of climate change;
- the concentration of ownership of our common stock;
- fluctuations in the price of our common stock;
- our ability to fund or access the capital markets at attractive rates and terms and manage our growth, both organic growth as well as growth through other means, such as future acquisitions;
- interest rate, unemployment rate, market and monetary fluctuations;
- the effects of international hostilities and geopolitical events;
- increased competition and its effect on the pricing of our products and services as well as our interest rate spread and net interest margin;
- the loss of key employees;
- the effectiveness of our risk management strategies, including operational risks, including, but not limited to, client, employee and third-party fraud and security breaches;
- other risks described in this Form 10-Q, the 2022 Form 10-K/A and other filings we make with the Securities and Exchange Commission ("SEC").

All forward-looking statements are necessarily only estimates of future results, and there can be no assurance that results will not differ materially from expectations. Therefore, you are cautioned not to place undue reliance on any

[Table of Contents](#)

forward-looking statements. Further, forward-looking statements included in this Form 10-Q are made only as of the date hereof, and we undertake no obligation to update or revise any forward-looking statement to reflect events or circumstances after the date on which the statements are made or to reflect the occurrence of unanticipated events, unless required to do so under the federal securities laws. You should also review the risk factors described in the reports the Company has filed or will file with the SEC.

Overview

The Company reported net income of \$3.8 million or \$0.19 per diluted share of common stock for the three months ended September 30, 2023 compared to \$5.6 million or \$0.28 per diluted share of common stock for the three months ended September 30, 2022. Net income for the nine months ended September 30, 2023 was \$13.8 million or \$0.70 per diluted share of common stock compared to \$15.7 million or \$0.78 per diluted share of common stock for the same period in 2022.

No shares were repurchased during the third quarter 2023. Year-to-date, the Company has repurchased 577,603 of Class A common stock shares at a weighted average price per share of \$9.77. These repurchases were made through open market purchases pursuant to the Company's publicly announced repurchase program. As of September 30, 2023, 172,397 shares remained authorized for repurchase under this program.

In evaluating our financial performance, the Company considers the level of and trends in net interest income, the net interest margin, the cost of deposits, levels and composition of non-interest income and non-interest expense, performance ratios, asset quality ratios, regulatory capital ratios, and any significant event or transaction.

Unless otherwise stated, all period comparisons in the bullet points below are calculated for the quarter ended September 30, 2023 compared to the quarter ended September 30, 2022 and to December 31, 2022, and annualized where appropriate:

- Net interest income for the three months ended September 30, 2023 decreased \$2.8 million or 16.4% to \$14.0 million from \$16.8 million for the quarter ended September 30, 2022. Net interest income for the nine months ended September 30, 2023 decreased \$2.6 million or 5.6% to \$44.2 million compared to the same period ended September 30, 2022.
- Net interest margin ("NIM") was 2.60% for the three months ended September 30, 2023 compared to 3.47% for the three months ended September 30, 2022. NIM was 2.84% for the nine months ended in September 30, 2023 compared to 3.36% for the period in 2022.
- Total assets were \$2.2 billion at September 30, 2023, representing an increase of \$207.1 million or 10.2% from September 30, 2022 and an increase of \$158.8 million or 10.2% annualized from December 31, 2022.
- Total loans were \$1.7 billion at September 30, 2023, representing an increase of \$245.0 million or 17.1% from September 30, 2022 and an increase of \$169.2 million or 15.0% annualized from December 31, 2022.
- Total deposits were \$1.9 billion at September 30, 2023, representing an increase of \$124.3 million or 6.9% from September 30, 2022 and an increase of \$91.6 million or 6.7% annualized from December 31, 2022.
- Annualized return on average assets for the quarter ended September 30, 2023 was 0.67% compared to 1.09% for the quarter ended September 30, 2022.
- Annualized return on average stockholders' equity for the quarter ended September 30, 2023 was 8.19% compared to 11.90% for the quarter ended September 30, 2022.
- The ACL to total loans was 1.16% at both September 30, 2023 and December 31, 2022. ACL was calculated under the CEO methodology for three and nine months ended September 30, 2023 and the incurred loss methodology for all periods in 2022.
- Non-performing loans to total loans was 0.03% at September 30, 2023 compared to 0.00% at December 31, 2022.
- At September 30, 2023, the total risk-based capital ratios for the Company and the Bank were 13.10% and 13.06%, respectively.
- Tangible book value per common share (a non-GAAP financial measurement) of \$9.36 as of September 30, 2023 was negatively affected by \$2.62 due to accumulated comprehensive loss of \$51.2 million at September 30, 2023. At September 30, 2022, tangible book value of \$8.87 per common share was negatively affected by \$2.26 due to \$45.2 million accumulated other comprehensive loss. See "Reconciliation and Management Explanation for Non-GAAP Financial Measures" for a reconciliation of this non-GAAP financial measure.

[Table of Contents](#)

Critical Accounting Policies and Estimates

The consolidated financial statements are prepared based on the application of U.S. GAAP, the most significant which are described in Note 1 "Summary of Significant Accounting Policies" in the Company's 2022 Form 10-K/A. To prepare financial statements in conformity with US GAAP, management makes estimates, assumptions, and judgments based on available information. These estimates, assumptions, and judgments affect the amounts reported in the financial statements and accompanying notes. These estimates, assumptions, and judgments are based on information available as of the date of the financial statements and, as this information changes, actual results could differ from the estimates, assumptions and judgments reflected in the financial statements. In particular, management has identified accounting policies that, due to the estimates, assumptions and judgments inherent in those policies, are critical in understanding our financial statements. Management has presented the application of these policies to the Audit and Risk Committee of our Board of Directors.

Allowance for Credit Losses

On January 1, 2023, the Company adopted ASU 2016-13 Financial Instruments - Credit Losses (Topic 326) on January 1, 2023, the Company adopted ASU 2016-13 Financial Instruments - Credit Losses (Topic 326) on Financial Instruments, as amended, which replaces the incurred loss methodology with an expected loss methodology that is referred to as the current expected credit loss (CECL) methodology. See Note 1 "Summary of Significant Accounting Policies" in Item 1 of Part I of this Form 10-Q for more information on the adoption ASC 326 and the allowance for credit losses.

Our ACL included residential loans. To assess the potential impact of changes in qualitative factors related to these loans, management performed a sensitivity analysis. The Company evaluated the impact of the HPI used in calculating expected losses on the residential loan segment. As of September 30, 2023, for every 100 basis points increase in the HPI index, the forecast reduces reserves by approximately \$21.7 thousand and about 1 basis point to the reserve coverage ratio, everything else being constant. This sensitivity analysis provides a hypothetical result to assess the sensitivity of the ACL and does not represent a change in management's judgement.

Income Taxes

Deferred tax assets and liabilities are recognized for the future tax consequences attributable to differences between the financial statement carrying amounts of existing assets and liabilities and their respective tax bases and operating loss and tax credit carryforwards. Deferred tax assets and liabilities are measured using enacted tax rates expected to apply to taxable income in the years in which those temporary differences are expected to be recovered or settled. The effect on deferred tax assets and liabilities of a change in tax rates is recognized in income in the period that includes the enactment date.

Management is required to assess whether a valuation allowance should be established on the net deferred tax assets based on the consideration of all available evidence using a more likely than not standard. In its evaluation, management considers taxable loss carry-back availability, expectation of sufficient taxable income, trends in earnings, the future reversal of temporary differences, and available tax planning strategies.

The Company recognizes positions taken or expected to be taken in a tax return in accordance with existing accounting guidance on income taxes which prescribes a recognition threshold and measurement process. Interest and penalties on tax liabilities, if any, would be recorded in interest expense and other operating non-interest expense, respectively.

Non-GAAP Financial Measures

This Form 10-Q includes financial information determined by methods other than in accordance with generally accepted accounting principles ("GAAP"). This financial information includes certain operating performance measures. Management has included these non-GAAP measures because it believes these measures may provide useful supplemental information for evaluating the Company's underlying performance trends. Further, management uses these measures in managing and evaluating the Company's business and intends to refer to them in discussions about our operations and ~~operating~~ performance measures should be viewed in addition to, and not as an alternative to or substitute for, measures determined in accordance with GAAP, and are not necessarily comparable to non-GAAP measures that may be presented by other companies. To the extent applicable, reconciliations of these non-GAAP measures to the most directly comparable GAAP measures can be found in the section "Reconciliation and Management Explanation of Non-GAAP Financial Measures" included in this Form 10-Q.

[Table of Contents](#)**Segment Reporting**

Management monitors the revenue streams for all its various products and services. The identifiable segments are not material and operations are managed and financial performance is evaluated on an overall Company-wide basis. Accordingly, all the financial service operations are considered by management to be aggregated in one reportable operating segment.

Results of Operations**General**

The following tables present selected balance sheet, income statement, and profitability ratios for the dates indicated (in thousands, except ratios):

	<u>September 30, 2023</u>	<u>December 31, 2022</u>
Consolidated Balance Sheets:		
Assets:	\$ 2,244,602	\$ 2,085,834
Total loans ⁽¹⁾	\$ 1,676,520	\$ 1,507,338
Total deposits	\$ 1,920,922	\$ 1,829,281
Total stockholders' equity	\$ 182,884	\$ 182,428

(1) Loan amounts include deferred fees/costs.

	<u>Three Months Ended September 30,</u>		<u>Nine Months Ended September 30,</u>	
	<u>2023</u>	<u>2022</u>	<u>2023</u>	<u>2022</u>
Consolidated Statements of Operations:				
Income before provision for credit	\$ 14,022	\$ 16,774	\$ 44,192	\$ 46,795
Non-interest income	\$ 2,161	\$ 1,789	\$ 6,077	\$ 5,351
Total non-interest	\$ 10,461	\$ 10,132	\$ 31,089	\$ 29,295
Net income	\$ 3,819	\$ 5,558	\$ 13,824	\$ 15,707
Profitability:				
Efficiency	64.64%	54.58%	61.85%	56.18%
Net interest margin	2.60%	3.47%	2.84%	3.36%

The Company's results of operations depend substantially on net interest income and non-interest income. Other factors contributing to the results of operations include our provision for credit losses, the level of non-interest expense, and the provision for income taxes.

Three months ended September 30, 2023 compared to the three months ended September 30, 2022

Net income decreased to \$3.8 million for the three months ended September 30, 2023 from \$5.6 million for the same period in 2022 mainly due to higher weighted average deposit costs.

Nine months ended September 30, 2023 compared to nine months ended September 30, 2022

Net income decreased to \$13.8 million for the nine months ended September 30, 2023 from \$15.7 million for the same period in 2022. The main drivers of the variance of net income was a \$25.1 million increase in interest expense mainly due to increases in the cost of deposits partially offset by a \$22.5 million increase in interest income generated from higher loan yields and a larger loan portfolio.

Net Interest Income

Net interest income is the difference between interest earned on interest-earning assets and interest paid on interest-bearing liabilities and is the primary driver of core earnings. Interest income is generated from interest and dividends on interest-earning assets, including loans, investment securities and other short-term investments. Interest expense is incurred from interest paid on interest-bearing liabilities, including interest-bearing deposits, FHLB advances and other borrowings.

To evaluate net interest income, we measure and monitor (i) yields on loans and other interest-earning assets, (ii) the costs of deposits and other funding sources, (iii) net interest spread, and (iv) net interest margin. Net interest spread is equal to the difference between yields earned on interest-earning assets and rates paid on interest-bearing liabilities. Net interest

[Table of Contents](#)

margin is equal to the annualized net interest income divided by average interest-earning assets. Because non-interest-bearing sources of funds, such as non-interest-bearing deposits and stockholders' equity, also fund interest-earning assets, net interest margin includes the indirect benefit of these non-interest-bearing funding sources.

Changes in market interest rates and interest rates we earn on interest-earning assets or pay on interest-bearing liabilities, as well as the volume and types of interest-earning assets and interest-bearing and non-interest-bearing liabilities, are usually the largest drivers of periodic changes in net interest spread, net interest margin and net interest income. Our asset liability committee (ALCO) has in place asset-liability management techniques to manage major factors that affect net interest income and net interest margin.

[Table of Contents](#)

The following table contains information related to average balances, average yields earned on assets, and average costs of liabilities for the periods indicated (dollars in thousands):

	Three Months Ended September 30,					
	2023			2022		
	Average ⁽¹⁾ Balance	Interest	Yield/Rate ⁽²⁾	Average ⁽¹⁾ Balance	Interest	Yield/Rate ⁽²⁾
Assets						
Interest-earning assets:						
Loans ⁽³⁾	\$ 1,610,864	\$ 22,523	5.55%	\$ 1,398,761	\$ 15,954	4.53%
Investment securities ⁽⁴⁾	445,828	2,833	2.52%	450,514	2,201	1.94%
Other interest-earning assets	<u>83,479</u>	<u>1,026</u>	<u>4.88%</u>	<u>70,540</u>	<u>322</u>	<u>1.81%</u>
Total interest-earning assets	<u>2,140,171</u>	<u>26,382</u>	<u>4.89%</u>	<u>1,919,815</u>	<u>18,477</u>	<u>3.82%</u>
Non-interest-earning assets	<u>110,087</u>			<u>106,976</u>		
Total assets	<u><u>\$ 2,250,258</u></u>			<u><u>\$ 2,026,791</u></u>		
Liabilities and stockholders' equity						
Interest-bearing liabilities:						
Interest-bearing checking	\$ 52,080	331	2.52%	\$ 66,585	19	0.11%
Saving and money market deposits	1,011,164	8,779	3.44%	823,521	1,141	0.55%
Time deposits	<u>290,272</u>	<u>2,565</u>	<u>3.51%</u>	<u>217,023</u>	<u>363</u>	<u>0.66%</u>
Total interest-bearing deposits	<u>1,353,516</u>	<u>11,675</u>	<u>3.42%</u>	<u>1,107,129</u>	<u>1,523</u>	<u>0.55%</u>
FHLB advances and other borrowings	<u>85,326</u>	<u>685</u>	<u>3.19%</u>	<u>43,935</u>	<u>180</u>	<u>1.63%</u>
Total interest-bearing liabilities	<u>1,438,842</u>	<u>12,360</u>	<u>3.41%</u>	<u>1,151,064</u>	<u>1,703</u>	<u>0.59%</u>
Non-interest-bearing demand deposits	<u>587,917</u>			<u>655,853</u>		
Other non-interest-bearing liabilities	<u>38,598</u>			<u>34,586</u>		
Total liabilities	<u><u>\$ 2,065,357</u></u>			<u><u>\$ 1,841,503</u></u>		
Stockholders' equity	<u>184,901</u>			<u>185,288</u>		
Total liabilities and stockholders' equity	<u><u>\$ 2,250,258</u></u>			<u><u>\$ 2,026,791</u></u>		
Net interest income		\$ 14,022			\$ 16,774	
Net interest spread ⁽⁵⁾			1.48%			3.23%
Net interest margin ⁽⁶⁾			2.60%			3.47%

(1) Average balances - Daily average balances are used to calculate yields/rates.

(2) Annualized.

(3) Average loan balances include non-accrual loans. Interest income on loans includes accretion of deferred loan fees, net of deferred loan costs.

(4) At fair value except for securities held to maturity. This amount includes FHLB stock.

(5) Net interest spread is the weighted average yield on total interest-earning assets minus the weighted average rate on total interest-bearing liabilities.

(6) Net interest margin is the ratio of net interest income to average total interest-earning assets.

[Table of Contents](#)

Nine Months Ended September 30.							
	2023			2022			
	Average Balance ⁽¹⁾	Interest	Yield/Rate ⁽²⁾	Average Balance ⁽¹⁾	Interest	Yield/Rate ⁽²⁾	
Assets							
Interest-earning assets:							
Loans ⁽³⁾	\$ 1,576,074	\$ 63,081	5.35 %	\$ 1,302,909	\$ 42,989	4.41 %	
Investment securities ⁽⁴⁾	430,118	7,501	2.33 %	484,489	7,040	1.94 %	
Other interest-earnings assets	71,514	2,459	4.60 %	76,655	474	0.83 %	
Total interest-earning assets	2,077,706	73,041	4.70 %	1,864,053	50,503	3.62 %	
Non-interest earning assets	107,443			105,914			
Total assets	<u>\$ 2,185,149</u>			<u>\$ 1,969,967</u>			
Liabilities and stockholders' equity							
Interest-bearing liabilities:							
Interest-bearing checking	\$ 54,554	574	1.41 %	\$ 65,798	52	0.11 %	
Money market and savings accounts	949,858	20,532	2.89 %	780,564	2,307	0.40 %	
Time deposits	264,241	5,767	2.92 %	221,504	893	0.54 %	
Total interest-bearing deposits	1,268,653	26,873	2.83 %	1,067,866	3,252	0.30 %	
Borrowings and repurchase agreements	80,087	1,976	3.30 %	38,788	456	1.57 %	
Total interest-bearing liabilities	1,348,740	28,849	2.87 %	1,106,654	3,708	0.45 %	
Non-interest bearing demand deposits	617,741			642,396			
Other non-interest-bearing liabilities	34,492			29,608			
Total liabilities	2,000,973			1,778,658			
Stockholders' equity	<u>184,176</u>			<u>191,309</u>			
Total liabilities and stockholders' equity	<u>\$ 2,185,149</u>			<u>\$ 1,969,967</u>			
Net interest income		<u>\$ 44,192</u>			<u>\$ 46,795</u>		
Net interest spread ⁽⁵⁾			1.83 %			3.17 %	
Net interest margin ⁽⁶⁾			2.84 %			3.36 %	

(1) Average balances - Daily average balances are used to calculate yields/rates.

(2) Annualized.

(3) Average loan balances include non-accrual loans. Interest income on loans includes accretion of deferred loan fees, net of deferred loan costs.

(4) At fair value except for securities held to maturity. Includes FHLB stock.

(5) Net interest spread is the weighted average yield on total interest-earning assets minus the weighted average rate on total interest-bearing liabilities.

(6) Net interest margin is the ratio of net interest income to average total interest-earning assets.

Three months ended September 30, 2023 compared to the three months ended September 30, 2022

Net interest income before the provision for credit losses was \$14.0 million for the three months ended September 30, 2023, a decrease of \$2.8 million or 16.4%, from \$16.8 million for the same period in 2022. The decrease was primarily attributable to the \$10.7 million increase in interest expense, which was a result to the prevailing market interest conditions which offset the increase in interest income.

Net interest margin was 2.60% for the quarter ended September 30, 2023 and 3.47% for the same period in 2022. The increase in loan yields as well as yields on other interest-earning assets was offset by higher deposit and borrowing costs.

Nine months ended September 30, 2023 compared to nine months ended September 30, 2022

Net interest income before the provision for credit losses was \$44.2 million for the nine months ended September 30, 2023, a decrease of \$2.6 million or 5.6%, from \$46.8 million for the same period in 2022. The decrease was attributable to the \$25.1 million increase in interest expense, which was a result to the prevailing market interest conditions which partially offset by the increase in interest income.

Net interest margin decreased to 2.84% for the nine months ended September 30, 2023 from 3.36% for the same period in 2022. Overall interest-bearing asset yields grew but were outpaced by the increase in the cost of funds.

Provision for Credit Losses

The provision for credit losses represents a charge to earnings necessary to maintain an allowance for credit losses that, in management's evaluation, is adequate to provide coverage for all expected credit losses. The provision for credit

Table of Contents

losses is impacted by variations in the size and composition of our loan and debt securities portfolio, recent historical and projected future economic conditions, our internal assessment of the credit quality of the loan and debt securities portfolios and net charge-offs.

Three months ended September 30, 2023 compared to the three months ended September 30, 2022

The provision for credit loss was \$653 thousand for the three months ended September 30, 2023 compared to \$910 thousand for the same period in 2022. Growth in the loan portfolio was the primary driver of the provision expense during the three months ended September 30, 2023 period. The decrease in provision for credit losses in the 2023 period compared to the September 30, 2022 quarter was due to greater loan growth in third quarter 2022.

Nine months ended September 30, 2023 compared to nine months ended September 30, 2022

The provision for credit loss was \$892 thousand for the nine months ended September 30, 2023 compared to \$1.6 million for the same period in 2022. Decrease of \$723 thousand due to higher loan growth in the nine months ended September 30, 2022. The ACL as a percentage of total loans was 1.16% at September 30, 2023 and at September 30, 2022.

ACL for the three and nine months ended September 30, 2023, was estimated under the CECL methodology, and for all periods in 2022, it was estimated under the incurred loss model. See "Allowance for Credit Losses" below for further discussion on how the ACL is calculated.

Non-Interest Income

Our services and products generate service charges and fees, mainly from our depository accounts. We also generate income from gain on sale of loans through our swap and SBA programs. In addition, we own and are beneficiaries of the life insurance policies on some of our employees and generate income from the increase in the cash surrender value of these policies.

The following table presents the components of non-interest income for the dates indicated (in thousands):

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2023	2022	2023	2022
Service fees	\$ 1,329	\$ 934	\$ 3,707	\$ 2,917
Gain (loss) on sale of securities available for sale,	(955)	(558)	(976)	(540)
Gain on sale of loans held for sale,	255	330	696	686
Other	-	-	-	161
Settlement interest income	1,532	1,083	2,650	2,127
Total non-interest income	\$ 2,161	\$ 1,789	\$ 6,077	\$ 5,351

Three months ended September 30, 2023 compared to the three months ended September 30, 2022

Non-interest income for the three months ended September 30, 2023 increased \$372 thousand or 20.8%, compared to the same period in 2022. This increase was primarily driven by growth in service fees from a larger deposit portfolio and an increase in wire and treasury management fees. A strategic restructuring of bank owned life insurance increased other income by \$982 thousand. However, there was a \$955 thousand securities loss experienced during the period. The Company sold \$7.7 million in lower-yielding securities to reinvest the funds in higher-return investments.

Nine months ended September 30, 2023 compared to the nine months ended September 30, 2022

Non-interest income for the nine months ended September 30, 2023 increased \$726 thousand or 13.6%, compared to the same period in 2022. This increase was primarily driven by an increase in service fees from a larger deposit portfolio and an increase in wire and treasury management fees. A strategic restructuring of bank owned life insurance increased other income by \$982 thousand experienced during the period. However, there was a \$976 thousand securities loss. The Company sold \$16.4 million in lower-yielding securities to reinvest the funds in higher-return investments. For the period ended September 30, 2022, the Company recognized \$161 thousand interest recovery from a prior lending customer of the Bank. This payment reflected the final payment and settlement of lien judgements against the customer.

[Table of Contents](#)

Non-Interest Expense

The following table presents the components of non-interest expense for the dates indicated (in thousands):

	<u>Three Months Ended September 30,</u>		<u>Nine Months Ended September 30,</u>	
	<u>2023</u>	<u>2022</u>	<u>2023</u>	<u>2022</u>
Salaries and employee benefits	\$ 6,066	\$ 6,075	\$ 18,325	\$ 17,863
Occupancy	1,350	1,281	3,968	3,802
Regulatory assessment and fees	365	269	1,041	708
Consulting and legal	513	604	1,257	1,519
Network and information technology	481	488	1,464	1,323
Other operating	1,686	1,415	5,034	4,080
Total non-interest expense	\$ 10,461	\$ 10,132	\$ 31,089	\$ 29,295

Three months ended September 30, 2023 compared to the three months ended September 30, 2022

Non-interest expense for the three months ended September 30, 2023 increased \$329 thousand or 3.2%, compared to the same period in 2022. The increase was primarily driven by an increase in the audit and tax services, legal expenses, FDIC deposit insurance assessment, and was partially offset by a decrease in the professional fees.

Nine months ended September 30, 2023 compared to the nine months ended September 30, 2022

Non-interest expense for the nine months ended September 30, 2023 increased \$1.8 million or 6.1%, compared to the same period in 2022. The increase was primarily driven by higher salaries and employee benefits expense due to new hires, increased salary compensation and seasonal payroll taxes as well as increases in the FDIC deposit insurance assessment rate, and audit and tax services expense.

Provision for Income Tax

Fluctuations in the effective tax rate reflect the effect of the differences in the inclusion or deductibility of certain income and expenses for income tax purposes. Therefore, future decisions on the investments we choose will affect our effective tax rate. The cash surrender value of bank-owned life insurance policies covering key employees, purchasing municipal bonds, and overall levels of taxable income will be important elements in determining our effective tax rate.

Three months ended September 30, 2023 compared to the three months ended September 30, 2022

Income tax expense for the quarter ended September 30, 2023 was \$1.3 million as compared to \$2.0 million for the same period in 2022. The effective tax rate for the three months ended September 30, 2023 was 24.7% compared to 26.1% for the same period in 2022.

Nine months ended September 30, 2023 compared to the nine months ended September 30, 2022

Income tax expense for the nine months ended September 30, 2023 decreased to \$4.5 million from \$5.5 million for the same period in 2022. The Company's effective tax rate was 24.4% for the 2023 period compared to 26.0% for the same period in 2022.

For a further discussion of income taxes, see Note 4 "Income Taxes" to the unaudited Consolidated Statements Item 1 of Part I of this Form 10-Q.

Analysis of Financial Condition

Total assets at September 30, 2023 were \$2.2 billion, an increase of \$158.8 million, or 10.2% annualized, over total assets of \$2.1 billion at December 31, 2022. Total loans, net of unearned fees/cost, increased \$169.2 million, or 15.0% annualized, to \$1.7 billion at September 30, 2023 compared to \$1.5 billion at December 31, 2022. Total deposits increased by \$91.6 million, or 6.7% annualized, to \$1.9 billion at September 30, 2023 compared to December 31, 2022.

Investment Securities

The investment portfolio is used and managed to provide liquidity through cash flows, marketability and, if necessary, collateral for borrowings. The investment portfolio is also used as a tool to manage interest rate risk and the Company's capital market risk exposure. The philosophy of the portfolio is to maximize the Company's profitability taking into

[Table of Contents](#)

consideration the Company's risk appetite and tolerance, manage the asset composition and diversification, and maintain adequate risk-based capital ratios.

The investment portfolio is managed in accordance with the Board approved Asset and Liability Management ("ALM") policy, which includes investment guidelines. Such policy is reviewed at least annually or more frequently if deemed necessary, depending on market conditions and/or unexpected events. The investment portfolio composition is subject to change depending on the funding and liquidity needs of the Company, and the interest risk management objective directed by the Asset-Liability Committee ("ALCO"). The portfolio of investments also can be used to modify the duration of the balance sheet. The allocation of cash into securities takes into consideration anticipated future cash flows (uses and sources) and all available sources of credit.

Our investment portfolio consists primarily of securities issued by U.S. government-sponsored agencies, U.S. agency mortgage-backed securities, collateralized mortgage obligation securities, municipal securities, and other debt securities, all with varying contractual maturities and coupons. Due to the optionality embedded in these securities, the final maturities do not necessarily represent the expected life of the portfolio. Some of these securities will be called or paid down prior to maturity depending on capital market conditions and expectations. The investment portfolio is regularly reviewed by the Chief Financial Officer, Treasurer, and the ALCO of the Company to ensure an appropriate risk and return profile as well as for adherence to the investment policy.

ASC Topic 326 amended the existing other-than-temporary-impairment guidance for AFS securities, requiring credit losses to be recorded as an allowance rather than through a permanent write-down. When evaluating AFS debt securities under ASC Topic 326, the Company has evaluated whether the decline in fair value is attributable to credit losses or other factors like interest rate risk, using both quantitative and qualitative analyses, including company performance analysis, review of credit ratings, remaining payment terms, prepayment speeds and analysis of macro-economic conditions. Each investment is expected to recover its price depreciations over its holding period as it moves to maturity and the Company has the intent and ability to hold these securities to maturity if necessary. As a result of this evaluation, the ~~Company~~ that no allowance was required on AFS securities.

AFS and HTM investment securities decreased \$2.9 million, or 0.9% annualized, to \$415.9 million at September 30, 2023 from \$418.8 million at December 31, 2022. Investment securities increased due to reinvestment of payments received and investment of excess in cash balances into high credit quality investments to increase the Company's profitability and modify the Company's balance sheet duration according to the ALM policy. As of September 30, 2023, investment securities with a market value of \$107.7 million were pledged to secure public deposits and the BTFP. The investment portfolio does not have any tax-exempt securities.

[Table of Contents](#)

The following table presents the amortized cost and fair value of investment securities for the dates indicated (in thousands):

	September 30, 2023		December 31, 2022	
	Amortized Cost	Fair Value	Amortized Cost	Fair Value
Available-for-sale:				
U.S. Government Agency	\$ 9,913	\$ 8,025	\$ 10,177	\$ 8,655
Collateralized mortgage obligations	105,547	78,571	118,951	95,541
Mortgage-backed securities - residential	66,024	51,157	73,838	60,879
Mortgage-backed securities - commercial	48,010	40,564	32,244	27,954
Corporate securities	25,024	18,116	25,084	18,483
Bank subordinated debt	24,417	22,176	15,964	14,919
Corporate bonds	-	-	4,037	3,709
	\$ 278,935	\$ 218,609	\$ 280,295	\$ 230,140
Held-to-maturity:				
U.S. Government Agency	\$ 44,087	\$ 37,049	\$ 44,914	\$ 39,062
U.S. Treasury	19,934	19,906	9,841	9,828
Collateralized mortgage obligations	64,094	53,786	68,727	60,925
Mortgage-backed securities - residential	44,302	38,214	42,685	38,483
Mortgage-backed securities - commercial	15,467	13,884	11,442	10,777
Corporate bonds	9,443	8,455	11,090	10,013
	\$ 197,327	\$ 171,294	\$ 188,699	\$ 169,088
Allowance for credit losses - securities held-to-maturity	(16)			
Securities held-to-maturity, net of allowance for credit losses	\$ 197,311			

The following table shows the weighted average yields, categorized by contractual maturity, for investment securities as of September 30, 2023 (in thousands, except ratios):

	Within 1 year		After 1 year through 5 years		After 5 years through 10 years		After 10 years		Total	
	Amortized Cost	Yield	Amortized Cost	Yield	Amortized Cost	Yield	Amortized Cost	Yield	Amortized Cost	Yield
Available-for-sale:										
U.S. Government	\$ -	0.00%	\$ -	0.00%	\$ 1,983	3.17%	\$ 6,042	1.53%	\$ 8,025	1.93%
Collateralized mortgage obligations	-	0.00%	-	0.00%	-	0.00%	78,571	1.39%	78,571	1.39%
MBS - residential	-	0.00%	-	0.00%	-	0.00%	51,157	1.62%	51,157	1.62%
MBS - commercial	-	0.00%	-	0.00%	-	0.00%	40,564	2.58%	40,564	2.58%
Municipal securities	-	0.00%	-	0.00%	2,720	1.69%	15,396	1.75%	18,116	1.74%
Bank subordinated debt securities	-	0.00%	5,977	5.75%	16,199	4.88%	-	0.00%	22,176	5.12%
Corporate bonds	-	0.00%	-	0.00%	-	0.00%	-	0.00%	-	0.00%
	\$ -	\$ 5,977	\$ 20,902		\$ 191,730		\$ 218,609		\$ 218,609	2.09%
Held-to-maturity:										
U.S. Government	\$ -	0.00%	\$ 7,921	1.02%	\$ 20,141	1.38%	\$ 16,025	2.01%	\$ 44,087	1.54%
U.S. Treasury	19,934	5.20%	-	0.00%	-	0.00%	-	0.00%	19,934	5.20%
Collateralized mortgage obligations	-	0.00%	-	0.00%	-	0.00%	64,094	1.66%	64,094	1.66%
MBS - residential	-	0.00%	4,468	1.85%	5,925	1.75%	33,909	2.40%	44,302	2.26%
MBS - commercial	-	0.00%	-	0.00%	3,076	1.62%	12,391	2.60%	15,467	2.40%
Corporate bonds	-	0.00%	9,443	2.80%	-	0.00%	-	0.00%	9,443	2.80%
	\$ 19,934	\$ 21,832	\$ 29,142		\$ 126,419		\$ 197,327		\$ 197,327	2.24%

Loans

Loans are the largest category of interest-earning assets on the unaudited Consolidated Balance Sheets, and usually provide higher yields than the remainder of the interest-earning assets. Higher yields typically carry inherent credit and liquidity risks in comparison to lower yield assets. The Company manages and mitigates such risks in accordance with the credit and ALM policies, risk tolerance and balance sheet composition.

[Table of Contents](#)

The following table shows the loan portfolio composition as of the dates indicated (in thousands):

	September 30, 2023		December 31, 2022	
	Total	Percent of Total	Total	Percent of Total
Residential Real Estate	\$ 188,880	11.3 %	\$ 185,636	12.3 %
Commercial Real Estate	1,005,280	60.0 %	970,410	64.4 %
Commercial and Industrial	212,975	12.7 %	126,984	8.4 %
Foreign	94,640	5.7 %	93,769	6.2 %
Bank Consumer and Other	173,096	10.3 %	130,429	8.7 %
Total gross loans	1,674,871	100.0 %	1,507,228	100.0 %
Plus: Deferred fees (cost)	1,649		110	
Total loans net of deferred fees (cost)	1,676,520		1,507,338	
Less: Allowance for credit	19,493		17,487	
Loans net loans	\$ 1,657,027		\$ 1,489,851	

Total loans, net of unearned fees/cost, increased by \$169.2 million, or 15.0% annualized to \$1.7 billion, September 30, 2023 compared to December 31, 2022. The commercial and industrial, and to a lesser extent, consumer and other and commercial real estate loan segments had the most significant growth.

Our loan portfolio continues to grow, with commercial real estate lending as the primary focus which approximates 60.0% of the total gross loan portfolio as of September 30, 2023. Our loan growth strategy since inception has been reflective of the market in which we operate and of our strategic plan as approved by the Board.

Most of the commercial real estate exposure represents loans to commercial businesses secured by owner-occupied real estate. The growth experienced in recent years is primarily due to implementation of our relationship-based banking model and the success of our relationship managers in competing for new business in a highly competitive metropolitan area. Many of our larger loan clients have long-term relationships with members of our senior management team or our relationship managers that date back to former institutions.

From a liquidity perspective, our loan portfolio provides us with additional liquidity due to repayments or unexpected prepayments. The following table shows maturities and sensitivity to interest rate changes for the loan portfolio at September 30, 2023 (in thousands):

	Due in 1 year or less	Due in 1 to 5 years	Due after 5 to 15 years	Due after 15 years	Total
Residential Real Estate	\$ 9,513	\$ 23,902	\$ 81,777	\$ 73,688	\$ 188,880
Commercial Real Estate	85,013	164,387	747,779	8,101	1,005,280
Commercial and Industrial	5,348	53,234	114,106	40,287	212,975
Foreign	94,640	-	-	-	94,640
Bank Consumer and Other	1,634	3,080	10,223	158,159	173,096
Total gross loans	\$ 196,148	\$ 244,603	\$ 953,885	\$ 280,235	\$ 1,674,871
Interest rate sensitivity:					
Fixed interest	\$ 174,725	\$ 144,198	\$ 193,366	\$ 170,370	\$ 682,659
Flloating or adjustable rates	21,423	100,405	760,519	109,865	992,212
Total gross loans	\$ 196,148	\$ 244,603	\$ 953,885	\$ 280,235	\$ 1,674,871

The information presented in the table above is based upon the contractual maturities of the individual loans, which may be subject to renewal at their contractual maturity. Renewals will depend on approval by our credit department and balance sheet composition at the time of the analysis, as well as any modification of terms at the loan's maturity. Additionally, maturity concentrations, loan duration, prepayment speeds and other interest rate sensitivity measures are discussed, reviewed, and analyzed by the ALCO. Decisions on term /rate modifications are discussed as well.

As of September 30, 2023, approximately 59% of the loans have adjustable/variable rates and 41% of the loans have fixed rates. The adjustable/variable rate loans re-price to different benchmarks and tenors in different periods of time. By contractual characteristics, there are no material concentrations on anniversary repricing. Additionally, it is important to note that most of our loans have interest rate floors. This embedded option protects the Company from a decrease in interest rates below the floor and positions us to gain in the scenario of higher interest rates.

[Table of Contents](#)

Asset Quality

Our asset quality grading analysis estimates the capability of the borrower to repay the contractual obligation of the loan agreement as scheduled or at all. The Company's internal credit risk grading system is based on experiences with similarly graded loans. Internal credit risk grades are reviewed at least once a year, and more frequently as needed. Internal credit risk ratings may change based on management's assessment of the results from the annual review, portfolio monitoring, and other developments observed with borrowers.

The internal credit risk grades used by the Company to assess the credit worthiness of a loan are shown below:

Pass – Loans indicate different levels of satisfactory financial condition and performance.

Special Mention – Loans classified as special mention have a potential weakness that deserves management's close attention. If left uncorrected, these potential weaknesses may result in deterioration of the repayment prospects for the loan or of the institution's credit position at some future date.

Substandard – Loans classified as substandard are inadequately protected by the current net worth and paying capacity of the obligator or of the collateral pledged, if any. Loans so classified have a well-defined weakness or weaknesses that jeopardize the liquidation of the debt. They are characterized by the distinct possibility that the institution will sustain some loss if the deficiencies are not corrected.

Doubtful – Loans classified as doubtful have all the weaknesses inherent in those classified at substandard, with the added characteristic that the weaknesses make collection or liquidation in full on the basis of currently existing facts, conditions, and values, highly questionable and improbable.

Loss – Loans classified as loss are considered uncollectible.

Loan credit exposures by internally assigned grades are as follows for the dates indicated (in thousands):

	September 30, 2023				
	Pass	Special Mention	Substandard	Doubtful	Total
Residential Real Estate	\$ 188,880	\$ -	\$ -	\$ -	\$ 188,880
Commercial Real Estate	1,002,765	-	2,515	-	1,005,280
Commercial and Industrial	210,991	-	1,984	-	212,975
Foreign	94,640	-	-	-	94,640
Banksumer and Other	173,096	-	-	-	173,096
	<u>\$ 1,670,372</u>	<u>\$ -</u>	<u>\$ 4,499</u>	<u>\$ -</u>	<u>\$ 1,674,871</u>

	December 31, 2022				
	Pass	Special Mention	Substandard	Doubtful	Total
Residential Real Estate	\$ 185,636	\$ -	\$ -	\$ -	\$ 185,636
Commercial Real Estate	967,465	-	2,945	-	970,410
Commercial and Industrial	126,177	-	807	-	126,984
Foreign	93,769	-	-	-	93,769
Banksumer and Other	130,233	-	196	-	130,429
	<u>\$ 1,503,280</u>	<u>\$ -</u>	<u>\$ 3,948</u>	<u>\$ -</u>	<u>\$ 1,507,228</u>

[Table of Contents](#)

Non-Performing Assets

The following table presents non-performing assets as of the dates shown (in thousands, except ratios):

	<u>September 30, 2023</u>	<u>December 31, 2022</u>
Total non-performing loans	\$ 479	\$ -
Other real estate owned	-	-
Total non-performing assets	\$ 479	\$ -
Asset quality ratios: (1)		
Allowance for credit losses to total loans	1.16%	1.16%
Allowance for credit losses to non-performing loans	4070%	- %
Non-performing loans to total loans	0.03%	- %

⁽¹⁾ ACL was calculated under CECL methodology for 2023, and incurred loss methodology for 2022

Non-performing assets include all loans categorized as non-accrual or restructured, impaired securities, other real estate owned ("OREO") and other repossessed assets. Problem loans for which the collection or liquidation in full is reasonably uncertain are placed on a non-accrual status. This determination is based on current existing facts concerning collateral values and the paying capacity of the borrower. When the collection of the full contractual balance is unlikely, the loan is placed on non-accrual to avoid overstating the Company's income for a loan with increased credit risk.

If the principal or interest on a commercial loan becomes due and unpaid for 90 days or more, the loan is placed on non-accrual status as of the date it becomes 90 days past due and remains in non-accrual status until it meets the criteria for restoration to accrual status. Residential loans, on the other hand, are placed on non-accrual status when the principal or interest becomes due and unpaid for 120 days or more and remains in non-accrual status until it meets the criteria for restoration to accrual status. Restoring a loan to accrual status is possible when the borrower resumes payment of principal and interest payments for a period of six months and the Company has a documented expectation of repayment of the remaining contractual principal and interest or the loan becomes secured and in the process of collection.

The Company may grant a loan concession to a borrower experiencing financial difficulties. This determination is performed during the annual review process or whenever problems surface regarding the client's ability to repay in accordance with the original terms of the loan or line of credit. The concessions are given to the debtor in various forms, including interest rate reductions, principal forgiveness, extension of maturity date, waiver, or deferral of payments and other concessions intended to minimize potential losses.

For further discussion on non-performing loans and borrowers experiencing financial difficulties, see Note 3 "Loans" to the unaudited Consolidated Financial Statements in Item 1 of Part 1 of this Form 10-Q.

Allowance for Credit Losses

On January 1, 2023, the Company adopted FASB ASU 2016-13, which introduced the current expected credit losses (CECL) methodology and required us to estimate all expected credit losses over the remaining life of our loan portfolio. Accordingly, the ACL represents an amount that, in management's evaluation, is adequate to provide coverage for all expected future credit losses on outstanding loans. Additionally, qualitative adjustments are made to the ACL when, based on management's judgment, there are factors impacting the allowance estimate not considered by the quantitative calculations. See Note 3 "Loans" in Item 1 of Part 1 of this Form 10-Q for more information on the allowance for losses.

[Table of Contents](#)

The following table presents ACL and net charge-offs to average loans by type for the periods indicated (in thousands):

	Residential Real Estate	Commercial Real Estate	Commercial and Industrial	Foreign Banks	Consumer and Other	Total
Three Months Ended September 30, 2023						
Beginning balance	\$ 2,673	\$ 10,183	\$ 2,500	\$ 677	\$ 2,782	\$ 18,815
Provision for credit ⁽¹⁾	(162)	(84)	738	73	108	673
Reserves	-	-	8	-	-	8
Charge-offs	-	-	-	-	(3)	(3)
Ending Balance	<u>\$ 2,511</u>	<u>\$ 10,099</u>	<u>\$ 3,246</u>	<u>\$ 750</u>	<u>\$ 2,887</u>	<u>\$ 19,493</u>
Average loans	\$ 183,643	\$ 992,171	\$ 179,127	\$ 87,847	\$ 168,076	\$ 1,610,864
Net charge-offs to average loans	-	-	-0.02%	-	0.01%	0.00%
Nine Months Ended September 30, 2023						
Beginning balance	\$ 1,352	\$ 10,143	\$ 4,163	\$ 720	\$ 1,109	\$ 17,487
Cumulative effect of adoption of ⁽²⁾ CECL ⁽³⁾ CECL	1,238	1,105	(2,158)	23	858	1,066
Provision for credit ⁽³⁾	(89)	(1,149)	1,181	7	965	915
Reserves	10	-	60	-	3	73
Charge-offs	-	-	-	-	(48)	(48)
Ending Balance	<u>\$ 2,511</u>	<u>\$ 10,099</u>	<u>\$ 3,246</u>	<u>\$ 750</u>	<u>\$ 2,887</u>	<u>\$ 19,493</u>
Average loans	\$ 186,918	\$ 980,244	\$ 164,466	\$ 90,597	\$ 153,849	\$ 1,576,074
Net charge-offs to average loans	-0.01%	-	-0.05%	-	0.04%	0.00%

(1) Provision for credit losses excludes \$17 thousand release due to unfunded commitments included in other liabilities and \$8 thousand release due to investment securities held to maturity.

(2) Impact of CECL adoption on January 1, 2023.

(3) Provision for credit losses excludes \$39 thousand release due to unfunded commitments included in other liabilities and \$11 thousand expense due to investment securities held to maturity.

	Residential Real Estate	Commercial Real Estate	Commercial and Industrial	Foreign Banks	Consumer and Other	Total
Three Months Ended September 30, 2022						
Beginning balance	\$ 2,366	\$ 9,290	\$ 2,671	\$ 651	\$ 808	\$ 15,786
Provision for credit	(1,009)	695	1,126	74	24	910
Reserves	1	-	-	-	-	1
Charge-offs	-	-	(88)	-	(5)	(93)
Ending Balance	<u>\$ 1,358</u>	<u>\$ 9,985</u>	<u>\$ 3,709</u>	<u>\$ 725</u>	<u>\$ 827</u>	<u>\$ 16,604</u>
Average loans	\$ 190,757	\$ 887,000	\$ 119,993	\$ 94,628	\$ 106,382	\$ 1,398,761
Net charge-offs to average loans	-	-	0.29%	-	0.02%	0.03%
Nine Months Ended September 30, 2022						
Beginning balance	\$ 2,498	\$ 8,758	\$ 2,775	\$ 457	\$ 569	\$ 15,057
Provision for credit	(1,157)	1,227	1,011	268	266	1,615
Reserves	33	-	11	-	3	47
Charge-offs	(16)	-	(88)	-	(11)	(115)
Ending Balance	<u>\$ 1,358</u>	<u>\$ 9,985</u>	<u>\$ 3,709</u>	<u>\$ 725</u>	<u>\$ 827</u>	<u>\$ 16,604</u>
Average loans	\$ 195,863	\$ 809,411	\$ 128,625	\$ 77,237	\$ 91,773	\$ 1,302,909
Net charge-offs to average loans	-0.02%	0.00%	0.12%	0.00%	0.02%	0.01%

Bank-Owned Life Insurance

As of September 30, 2023, the combined cash surrender value of all bank-owned life insurance ("BOLI") policies was \$51.4 million. Changes in cash surrender value are recorded to non-interest income in the unaudited Consolidated Statements of Operations. The Company had BOLI policies with five insurance carriers. The Company is the beneficiary of these policies.

[Table of Contents](#)

During the third quarter of 2023, the Company restructured its BOLI, cancelling a \$7.1 million policy by surrendering \$4.2 million of the value and transferring the remaining \$2.9 million to a new BOLI policy. The new BOLI policy was funded with an additional \$11.1 million for a total of \$14.1 million. This new BOLI policy received a cash surrender enhancement from the new insurance carrier of \$981 thousand.

Deposits

Customer deposits are the primary funding source for the Bank's growth. Through our network of banking centers, we offer a competitive array of deposit accounts and treasury management services designed to meet our customers' business needs. Our primary deposit customers are small-to-medium sized businesses ("SMBs"), and the personal business of owners and operators of these SMBs, as well as the retail/consumer relationships of the employees of these businesses.

The following table presents the daily average balance and average rate paid on deposits by category for the periods presented (in thousands, except ratios):

	Three Months Ended September 30,			
	2023		2022	
	Average Balance	Average Rate Paid	Average Balance	Average Rate Paid
Non-interest-bearing	\$ 587,917	0.00%	\$ 655,853	0.00%
Checking	52,080	2.52%	66,585	0.11%
Money market and savings deposits	1,011,164	3.44%	823,521	0.55%
Time deposits	290,272	3.51%	217,023	0.66%
Total	\$ 1,941,433	2.39%	\$ 1,762,982	0.34%

The Company has a granular deposit portfolio with outstanding balances comprised of 49% in commercial deposits, 37% personal deposits, 11% public funds which are partially collateralized and 3% brokered deposits. During the months ended September 30, 2023, the Company acquired \$50 million in brokered deposits to boost liquidity. The Company has approximately 20 thousand deposit accounts with the majority in personal accounts, approximately 13 thousand or 63.8%. The estimated average account size of our deposit portfolio is approximately \$95 thousand as of September 30, 2023. The Company also offers Insured Cash Sweep ("ICS") and Certificate of Deposit Account Registry Service ("CDARS") deposit products to fully insure our clients.

The uninsured deposits are estimated based on the FDIC deposit insurance limit of \$250 thousand for all accounts at the Company per account holder. The total estimated amount of uninsured deposits is 53% at September 30, 2023.

The following table shows scheduled maturities of uninsured time deposits as of September 30, 2023 (in thousands):

	September 30, 2023
Three months or	\$ 18,563
Over three through six	32,457
Over six through twelve	28,769
Over twelve months	2,566
	\$ 82,355

Other Liabilities

The Company collects from commercial and residential loan customers funds which are held in escrow for future payment of real estate taxes and insurance. These escrow funds are disbursed by the Company directly to the insurance companies and taxing authority of the borrower. Escrow funds are recorded as other liabilities.

As of September 30, 2023 escrow balances totaled \$16.7 million compared to \$3.5 million at December 31, 2022.

[Table of Contents](#)

Borrowings

As a member of the FHLB, we are eligible to obtain advances with various terms and conditions. This accessibility of additional funding allows us to efficiently and timely meet both expected and unexpected outgoing cash flows and collateral needs without adversely affecting either daily operations or the financial condition of the Company.

As of September 30, 2023, we had \$102.0 million of fixed and variable rate advances outstanding from the FHLB with a weighted average rate of 3.66%. Maturity dates for the advances range between 2023 to 2028 detailed in the table below.

The following table presents the FHLB advances as of September 30, 2023 (in thousands):

Interest Rate	Type of Rate	Maturity Date	Amount
5.57%	Variable	December 22, 2023	\$ 20,000
1.04%	Fixed	July 30, 2024	5,000
2.05%	Fixed	March 27, 2025	10,000
1.07%	Fixed	July 18, 2025	6,000
3.76%	Fixed	January 24, 2028	11,000
3.77%	Fixed	April 25, 2028	50,000
			<hr/>
			\$ 102,000

We have also established Federal Funds lines of credit with our upstream correspondent banks, the BTFP, and the FRB Atlanta Discount Window to manage temporary fluctuations in our daily cash balances. As of September 30, 2023, there were no outstanding balances with any of these liquidity sources.

Off-Balance Sheet Arrangements

We engage in various financial transactions in our operations that, under GAAP, may not be included on the balance sheet. To meet the financing needs of our customers we may include commitments to extend credit and standby letters of credit. To a varying degree, such commitments involve elements of credit, market, and interest rate risk in excess of the amount recognized in the balance sheet. We use more conservative credit and collateral policies in making these credit commitments than we do for on-balance sheet items. We are not aware of any accounting loss to be incurred by funding these commitments; however, we maintain an allowance for off-balance sheet credit risk which is recorded under other liabilities on the unaudited Consolidated Balance Sheets.

Since commitments associated with letters of credit and commitments to extend credit may expire unused, the amounts shown do not necessarily reflect actual future cash funding requirements. The following table presents lending ~~related~~ commitments outstanding as of the dates indicated (in thousands):

	September 30, 2023	December 31, 2022
Commitments to grant loans and unfunded lines of credit	\$ 100,661	\$ 95,461
Standby and commercial letters of credit	6,490	4,320
	<hr/>	<hr/>
	\$ 107,151	\$ 99,781

Commitments to extend credit are agreements to lend funds to a client, as long as there is no violation of any condition established in the contract, for a specific purpose. Commitments generally have variable interest rates, fixed expiration dates or other termination clauses and may require payment of a fee. Since many of the commitments are expected to expire without being fully drawn, the total commitment amounts disclosed above do not necessarily represent future cash requirements.

Unfunded lines of credit represent unused portions of credit facilities to our current borrowers that represent no change in credit risk in our portfolio. Lines of credit generally have variable interest rates. The maximum potential amount of future payments we could be required to make is represented by the contractual amount of the commitment, less the amount of any advances made.

Letters of credit are conditional commitments issued by us to guarantee the performance of a client to a third party. In the event of nonperformance by the client in accordance with the terms of the agreement with the third party, we would be required to fund the commitment. If the commitment is funded, we would be entitled to seek recovery from the client from the underlying collateral, which can include commercial real estate, physical plant and property, inventory, receivables, cash or marketable securities.

Asset and Liability Management Committee

Members of senior management and our Board make up the asset and liability management committee, or ALCO. Senior management is responsible for ensuring that Board approved strategies and policies for managing and mitigating risks are appropriately executed within the designated lines of authority and responsibility in a timely manner.

ALCO oversees the establishment, approval, implementation, and review of interest rate risk, management, and mitigation strategies, ALM related policies, ALCO procedures and risk tolerances and appetite.

While some degree of IRR ("Interest Rate Risk") is inherent to the banking business, we believe our ALCO implemented sound risk management practices to identify, quantify, monitor, and limit IRR exposures.

When assessing the scope of IRR exposure and impact on the consolidated balance sheet, cash flows and income statement, management considers both earnings and economic impacts. Asset price variations, deposit volatility and reduced earnings or outright losses could adversely affect the Company's liquidity, performance, and capital adequacy.

Income simulations are used to assess the impact of changing rates on earnings under different rates scenarios and time horizons. These simulations utilize both instantaneous and parallel changes in the level of interest rates, as well as non-parallel changes such as changing slopes (flat and steepening) and twists of the yield curve. Static simulation models are based on current exposures and assume a constant balance sheet with no new growth. Dynamic simulation analysis is also utilized to have a more comprehensive assessment on IRR. This simulation relies on detailed assumptions outlined in our budget and strategic plan, and in assumptions regarding changes in existing lines of business, new ~~business~~ strategies and client expected behavior.

To have a more complete picture of IRR, the Company also evaluates the economic value of equity ("EVE"). ~~assessment~~ allows us to measure the degree to which the economic values will change under different interest scenarios (parallel and non-parallel). The economic value approach focuses on a longer-term time horizon and captures all future cash flows expected from existing assets and liabilities. The economic value model utilizes a static approach in that the analysis does not incorporate new business; rather, the analysis shows a snapshot in time of the risk inherent in the balance sheet.

Market and Interest Rate Risk Management

According to our ALCO model, as of September 30, 2023, we had an asset sensitive balance sheet both for year one and two modeling, using the static modeling. Asset sensitivity indicates that our assets generally reprice faster than our liabilities, which results in a favorable impact to net interest income when market interest rates increase. Liability sensitivity indicates that our liabilities generally reprice faster than our assets, which results in a favorable impact to net interest income when market interest rates decrease. Many assumptions are used to calculate the impact of interest rate variations on our net interest income, such as asset prepayment speeds, non-maturity deposit price sensitivity, pricing correlations, deposit truncations and decay rates, and key interest rate drivers.

Because of the inherent use of these estimates and assumptions in the model, our actual results may, and most likely will, differ from static measures results. In addition, static measures like EVE do not include actions that management may undertake to manage the risks in response to anticipated changes in interest rates or client deposit behavior. As part of our ALM strategy and policy, management has the ability to modify the balance sheet to either increase asset duration and decrease liability duration to reduce asset sensitivity, or to decrease asset duration and increase liability duration in order to increase asset sensitivity.

According to our model, as of September 30, 2023, our balance sheet is asset sensitive for both year one and two under interest static rate scenarios (an increase or decrease of 400 basis points). This means that if rates increase the NIM will increase and if rates decrease the NIM will decrease. Additionally, utilizing an EVE approach, we analyze the risk to capital from the effects of various interest rate scenarios through a long-term discounted cash flow model. This measures difference between the economic value of our assets and the economic value of our liabilities, which is a proxy for liquidation value. According to our balance sheet composition, and as expected, our model stipulates that an increase in interest rates will have a negative impact on the EVE and lower rates, a positive impact. Results and analysis are presented quarterly to the ALCO, and strategies are reviewed and refined.

[Table of Contents](#)

Liquidity

Liquidity is defined as a Company's capacity to meet its cash and collateral obligations at a reasonable cost. Maintaining an adequate level of liquidity depends on the Company's ability to efficiently meet both expected and unexpected cash flow and collateral needs without adversely affecting either daily operations or the financial condition of the Company.

Liquidity risk is the risk that we will be unable to meet our short-term and long-term obligations as they become due because of an inability to liquidate assets or obtain relatively adequate funding. The Company's obligations, and the funding sources used to meet them, depend significantly on our business mix, balance sheet structure and composition, ~~quality~~ of our assets and the cash flow profiles of our on- and off-balance sheet obligations.

In managing inflows and outflows, management regularly monitors situations that can give rise to increased liquidity risk. These include funding mismatches, market constraints on the ability to convert assets (particularly investments) into cash or in accessing sources of funds (i.e., market liquidity), and contingent liquidity events.

Changes in macroeconomic conditions, as well as exposure to credit, market, operational, legal and reputational risks, such as cybersecurity risk, could have an unexpected impact on the Company's liquidity risk profile and are factored into the assessment of liquidity and the ALM framework.

Management has established a comprehensive and holistic management process for identifying, measuring, monitoring and mitigating liquidity risk. Due to its critical importance to the viability of the Company, liquidity risk management is integrated into our risk management processes, Contingency Funding Plan and ALM policy.

Critical elements of our liquidity risk management include: effective corporate governance consisting of oversight by the Board and active involvement of senior management; appropriate strategies, policies, procedures, and limits used to identify and mitigate liquidity risk; comprehensive liquidity risk measurement and monitoring systems (including assessments of the current and prospective cash flows or sources and uses of funds) that are commensurate with the complexity and business activities of the Company; active management of intraday liquidity and collateral; an appropriately diverse mix of existing and potential future funding sources; adequate levels of highly liquid marketable securities free of legal, regulatory, operational impediments, that can be used to meet liquidity needs in stressful situations; comprehensive contingency funding plans that sufficiently address potential adverse liquidity events and emergency cash flow requirements; and internal controls and internal audit processes sufficient to determine the adequacy of the institution's liquidity risk management process.

We expect funds to be available from several basic banking activity sources, including the core deposit base, ~~repayment~~ and maturity of loans and investment security cash flows. Other potential funding sources include federal funds purchased, brokered certificates of deposit, listing services certificates of deposit, the Bank Term Funding Program, FRB Atlanta discount window, and borrowings from the FHLB. Accordingly, we believe our liquidity resources are adequate to fund loans and meet other cash needs as necessary.

[Table of Contents](#)**Capital Adequacy**

As of September 30, 2023, the Bank was well capitalized under the FDIC's prompt corrective action framework. We also follow the capital conservation buffer framework, and as of September 30, 2023, we exceeded the capital conservation buffer in all capital ratios, according to our actual ratios. The following table presents the capital ratios for the Bank at the dates indicated (in thousands, except ratios).

	Actual		Minimum Capital Requirements		To be Well Capitalized	
	Amount	Ratio	Amount	Ratio	Amendments	Ratio
September 30, 2023						
Total risk-based capital	\$ 230,801	13.06 %	\$ 141,327	8.00 %	\$ 176,659	10.00 %
Tier 1 risk-based capital	\$ 210,815	11.93 %	\$ 105,995	6.00 %	\$ 141,327	8.00 %
Common equity tier 1 capital	\$ 210,815	11.93 %	\$ 79,496	4.50 %	\$ 114,828	6.50 %
Leverage ratio	\$ 210,815	9.24 %	\$ 91,310	4.00 %	\$ 114,138	5.00 %
December 31, 2022:						
Total risk-based capital	\$ 216,693	13.58 %	\$ 127,616	8.00 %	\$ 159,520	10.00 %
Tier 1 risk-based capital	\$ 198,909	12.47 %	\$ 95,712	6.00 %	\$ 127,616	8.00 %
Common equity tier 1 capital	\$ 198,909	12.47 %	\$ 71,784	4.50 %	\$ 103,688	6.50 %
Leverage ratio	\$ 198,909	9.56 %	\$ 83,210	4.00 %	\$ 104,012	5.00 %

The Company is not subject to regulatory capital ratios imposed by Basel III on bank holding companies because the Company is deemed to be a small bank holding company.

Impact of Inflation

Our Consolidated Financial Statements and related notes have been prepared in accordance with U.S. GAAP, which require the measurement of financial position and operating results in terms of historical dollars, without considering the changes in the relative purchasing power of money over time due to inflation. The impact of inflation is reflected in the increased cost of operations. Unlike most industrial companies, nearly all our assets and liabilities are monetary in nature. As a result, interest rates have a greater impact on our performance than do the effects of general levels of inflation. Periods of high inflation are often accompanied by relatively higher interest rates, and periods of low inflation are accompanied by relatively lower interest rates. As market interest rates rise or fall in relation to the rates earned on loans and investments, the value of these assets decreases or increases respectively. Inflation can also impact core non-interest ~~expenses~~ expenses with delivering the Company's services.

Recently Issued Accounting Pronouncements

Recently issued accounting pronouncements are discussed in Note 1 "Summary of Significant Accounting Policies" to the unaudited Consolidated Financial Statements in this Form 10-Q.

[Table of Contents](#)

Reconciliation and Management Explanation of Non -GAAP Financial Measures

Management has included these non-GAAP measures because it believes these measures may provide useful supplemental information for evaluating the Company's underlying performance trends. Further, management uses these measures in managing and evaluating the Company's business and intends to refer to them in discussions about operations and performance. Operating performance measures should be viewed in addition to, and not as an alternative to or substitute for, measures determined in accordance with GAAP, and are not necessarily comparable to non-GAAP measures that may be presented by other companies. The following table reconciles the non-GAAP financial measurement of operating net income available to common stockholders for the periods presented (in thousands, except per share data):

[Table of Contents](#)

USCB FINANCIAL HOLDINGS, INC.
NON-GAAP FINANCIAL MEASURES (UNAUDITED)
(Dollars in thousands)

	As of or For the Three Months				
	9/30/2023	6/30/2023	3/31/2023	12/31/2022	9/30/2022
Pre-tax pre-provision ("PTPP") income⁽¹⁾					
Net income	\$ 3,819	\$ 4,196	\$ 5,809	\$ 4,434	\$ 5,558
Plus: Provision for income taxes	1,250	1,333	1,881	1,415	1,963
Plus: Provision for credit losses	653	38	201	880	910
PTPP income	\$ 5,722	\$ 5,567	\$ 7,891	\$ 6,729	\$ 8,431
PTPP return on average assets⁽¹⁾					
PTPP income	\$ 5,722	\$ 5,567	\$ 7,891	\$ 6,729	\$ 8,431
Average assets	\$ 2,250,258	\$ 2,183,542	\$ 2,120,218	\$ 2,051,867	\$ 2,026,791
PTPP return on average assets ⁽²⁾	1.01%	1.02%	1.51%	1.30%	1.65%
Operating net income⁽¹⁾					
Net income	\$ 3,819	\$ 4,196	\$ 5,809	\$ 4,434	\$ 5,558
Less: Net gains (losses) on sale of securities	(955)	-	(21)	(1,989)	(558)
Effect on sale of securities	242	-	5	504	141
Operating net income	\$ 4,532	\$ 4,196	\$ 5,825	\$ 5,919	\$ 5,975
Operating PTPP income⁽¹⁾					
PTPP income	\$ 5,722	\$ 5,567	\$ 7,891	\$ 6,729	\$ 8,431
Less: Net gains (losses) on sale of securities	(955)	-	(21)	(1,989)	(558)
Operating PTPP income	\$ 6,677	\$ 5,567	\$ 7,912	\$ 8,718	\$ 8,989
Operating PTPP return on average assets⁽¹⁾					
Operating PTPP income	\$ 6,677	\$ 5,567	\$ 7,912	\$ 8,718	\$ 8,989
Average assets	\$ 2,250,258	\$ 2,183,542	\$ 2,120,218	\$ 2,051,867	\$ 2,026,791
Operating PTPP return on average assets ⁽²⁾	1.18%	1.02%	1.51%	1.69%	1.76%
Operating return on average assets⁽¹⁾					
Operating net income	\$ 4,532	\$ 4,196	\$ 5,825	\$ 5,919	\$ 5,975
Average assets	\$ 2,250,258	\$ 2,183,542	\$ 2,120,218	\$ 2,051,867	\$ 2,026,791
Operating return on average assets ⁽²⁾	0.80%	0.77%	1.11%	1.14%	1.17%
Operating return on average equity⁽¹⁾					
Operating net income	\$ 4,532	\$ 4,196	\$ 5,825	\$ 5,919	\$ 5,975
Average equity	\$ 184,901	\$ 184,238	\$ 183,371	\$ 177,556	\$ 185,288
Operating return on average equity ⁽²⁾	9.72%	9.13%	12.88%	13.23%	12.79%
Operating Revenue⁽¹⁾					
Net interest income	\$ 14,022	\$ 14,173	\$ 15,997	\$ 16,866	\$ 16,774
Plus: Non-interest income	2,161	1,846	2,070	(123)	1,789
Less: Net gains (losses) on sale of securities	(955)	-	(21)	(1,989)	(558)
Operating revenue	\$ 17,138	\$ 16,019	\$ 18,088	\$ 18,732	\$ 19,121
Operating Efficiency Ratio⁽²⁾					
Total non-interest expense	\$ 10,461	\$ 10,452	\$ 10,176	\$ 10,014	\$ 10,132
Operating revenue	\$ 17,138	\$ 16,019	\$ 18,088	\$ 18,732	\$ 19,121
Operating efficiency ratio	61.04%	65.25%	56.26%	53.46%	52.99%

(1) The Company believes these non-GAAP measurements are key indicators of the ongoing earnings power of the Company.

(2) Annualized.

[Table of Contents](#)

USCB FINANCIAL HOLDINGS, INC.
NON-GAAP FINANCIAL MEASURES (UNAUDITED)
(Dollars in thousands, except per share
data)

	As of or For the Three Months				
	9/30/2023	6/30/2023	3/31/2023	12/31/2022	9/30/2022
Tangible book value per common share (at period-end):					
Total stockholders' equity	\$ 182,884	\$ 183,685	\$ 183,858	\$ 182,428	\$ 177,417
Less: Intangible assets	-	-	-	-	-
Tangible stockholders' equity	\$ 182,884	\$ 183,685	\$ 183,858	\$ 182,428	\$ 177,417
Total shares issued and outstanding (at period-end):					
Total common shares issued and outstanding	<u>19,544,777</u>	<u>19,622,380</u>	<u>19,622,380</u>	<u>20,000,753</u>	<u>20,000,753</u>
Tangible book value per common share	⁽²⁾ <u>\$ 9.36</u>	<u>\$ 9.40</u>	<u>\$ 9.37</u>	<u>\$ 9.12</u>	<u>\$ 8.87</u>
Operating diluted net income per common share: ⁽¹⁾					
Operating net income	\$ 4,532	\$ 4,196	\$ 5,825	\$ 5,919	\$ 5,975
Total weighted average diluted shares of common stock	<u>19,611,897</u>	<u>19,639,682</u>	<u>19,940,606</u>	<u>20,172,438</u>	<u>20,148,208</u>
Operating diluted net income per common share:	<u>\$ 0.23</u>	<u>\$ 0.21</u>	<u>\$ 0.29</u>	<u>\$ 0.29</u>	<u>\$ 0.30</u>
Tangible Common Equity/Tangible Assets:					
Tangible stockholders' equity	\$ 182,884	\$ 183,685	\$ 183,858	\$ 182,428	\$ 177,417
Tangible assets	\$ 2,244,602	\$ 2,225,914	\$ 2,163,821	\$ 2,085,834	\$ 2,037,453
Tangible Common Equity/Tangible Assets	8.15%	8.25%	8.50%	8.75%	8.71%

(1) The Company believes these non-GAAP measurements are key indicators of the ongoing earnings power of the Company.

(2) Excludes the dilutive effect, if any, of shares of common stock issuable upon exercise of outstanding stock options.

[Table of Contents](#)

Item 3. Quantitative and Qualitative Disclosures About Market Risk

As a smaller reporting company, we are not required to provide the information required by this item.

Item 4. Controls and Procedures

Evaluation of Disclosure Controls and Procedures

Under the supervision and with the participation of our management, including our President and Chief Executive Officer and our Chief Financial Officer, we evaluated the effectiveness of the design and operation of the Company's disclosure controls and procedures (as defined in Rules 13a-15(e) and 15d-15(e) under the Exchange Act) as of September 30, 2023. Based on that evaluation, management believes that the Company's disclosure controls and procedures were effective to collect, process, and disclose the information required to be disclosed in the reports filed or submitted under the Exchange Act within the required time periods as of the end of the period covered by this Form 10-Q.

Changes in Internal Control Over Financial Reporting

There has been no change in our internal control over financial reporting (as defined in Rules 13a-15(f) and 15d-15(f) under the Exchange Act) during the period covered by this Form 10-Q that has materially affected, or is reasonably likely to materially affect, our internal control over financial reporting.

Limitations on Effectiveness of Controls and Procedures

In designing and evaluating the disclosure controls and procedures, management recognizes that any controls and procedures, no matter how well designed and operated, can provide only reasonable, not absolute, assurance of achieving the desired control objectives. In addition, the design of disclosure controls and procedures must reflect the fact that there are resource constraints and that management is required to apply judgment in evaluating the benefits of possible controls and procedures relative to their costs.

[Table of Contents](#)

PART II

Item 1. Legal Proceedings

As previously disclosed, on July 13, 2023, three individuals who were shareholders of the Bank prior to its reorganization into the holding company form of organization (the "Plaintiffs") filed a lawsuit against six persons, all of whom were directors of the Bank at the relevant time (the "Defendants"), in the Circuit Court, Eleventh Judicial Circuit for Miami-Dade County (the "Court") (Benes et al. v. de la Aguilera et al.) alleging the Defendants (i) caused the Bank, as directors ~~engage in ultra vires conduct~~ by devising and approving the exchange transaction effected in July 2021 pursuant to which the Bank's then outstanding Class C and Class D preferred stock was exchanged (the "Exchange Transaction"), which action the Plaintiffs allege was not permitted by the Bank's Articles of Incorporation, and (ii) breached their fiduciary duty as directors of the Bank by approving and engaging in the Exchange Transaction. The Plaintiffs seek the Court to certify the action as a class action and to award damages in an amount to be proven at trial. Plaintiffs seek damages \$~~500,000~~ plus attorney's fees and costs as well as such other relief as the Court may determine. The Company believes that the allegations in the lawsuit are legally and factually without merit, and it intends to vigorously defend against ~~allegations~~ in the lawsuit, pursue any potential counterclaims against the plaintiffs as it deems appropriate, and seek coverage from its insurance carriers. However, there can be no assurance that this litigation will be resolved ~~favourably~~, there is also no assurance that we will be able to secure coverage from our insurance carriers for any expenses incurred by us in connection with this litigation. If the plaintiff shareholders are successful, the Court could award substantial compensatory damages.

In addition to the foregoing, we are from time to time subject to claims and litigation arising in the ordinary course of business. These claims and litigation may include, among other things, allegations of violation of banking and ~~applicable~~ regulations, competition law, labor laws and consumer protection laws, as well as claims or litigation relating to intellectual property, securities, breach of contract and tort. We intend to defend ourselves vigorously against any pending or future claims and litigation.

At this time, in the opinion of management, the likelihood is remote that the impact of such proceedings, individually or in the aggregate, would have a material adverse effect on our consolidated results of operations, financial condition or cash flows. However, one or more unfavorable outcomes in any claim or litigation against us, including the aforementioned litigation regarding the Exchange Transaction, could have a material adverse effect on the period in which such claims or litigation are resolved. In addition, regardless of their merits or their ultimate outcomes, such matters are costly, divert management's attention and may materially adversely affect our reputation, even if resolved in our favor.

Item 1A. Risk Factors

For detailed information about certain risk factors that could materially affect our business, financial condition, or future results, see "Part I, Item 1A – Risk Factors" of the 2022 Form 10-K/A and see "Part II, Item 1A – Risk Factors" of the March 31, 2023 Form 10-Q.

Item 2. Unregistered Sales of Equity Securities and Use of Proceeds

- (a) None.
- (b) Not applicable.
- (c) The Company's repurchases of equity securities for the quarter ended September 30, 2023 were as follows:

[Table of Contents](#)

Period	Total Number of Shares Purchased	Average Price Paid	Total Number of Shares Purchased Publicly Announced or Under Plans or Programs (1)	Maximum Number of Shares that May Be Purchased Under Plans or Programs (1)
July 1-31, 2023	-	\$ -	-	172,397
August 1-30, 2023	-	-	-	172,397
September 1-30, 2023	-	-	-	172,397

(1) On January 24, 2022 the Company announced its initial stock repurchase program to repurchase up to 750,000 shares of Class A common stock approximately 3.75% of the Company's then outstanding shares of common stock.

Item 3. Defaults Upon Senior Securities

- (a) Not applicable
- (b) Not applicable

Item 4. Mine Safety Disclosures

Not applicable.

Item 5. Other Information

- (a) Not applicable
- (b) Not applicable
- (c) Not applicable

[Table of Contents](#)

Item 6. Exhibits

Exhibit	Description of
No. 2.1	Exhibit and Plan of Share Exchange, dated December 27, 2021, by and between U.S. Century Bank and USCB Financial Holdings, Inc. (incorporated by reference to Exhibit 2.1 to the Registrant's Current Report on Form 8-K (File No. 001-41196) filed with the Securities and Exchange Commission on December 30,
3.1	Articles of Incorporation, as amended, of USCB Financial Holdings, Inc. (incorporated by reference to Exhibit 3.1 to the Registrant's Quarterly Report on Form 10-Q for the quarter ended June 30, 2023 (File No. 001-41196) filed with the Securities and Exchange Commission on August 11,
3.2	Amended and Restated Bylaws of USCB Financial Holdings, Inc. (incorporated by reference to Exhibit 3.1 to the Current Report on Form 8-K (File No. 001-41196) filed with the Securities and Exchange Commission on July 26,
4.1	2023 Letter Agreement, dated December 30, 2021, between USCB Financial Holdings, Inc., U.S. Century Bank, Priam Capital Fund II, L.P., Patriot Financial Partners II, L.P., and Patriot Financial Partners Parallel II, L.P. (incorporated by reference to Exhibit 4.1 to the Registrant's Current Report on Form 8-K (File No. 001-41196) filed with the Securities and Exchange Commission on December 30,
4.2	Registration Rights Agreement, dated March 17, 2015, between U.S. Century Bank, Priam Capital Fund II, L.P., Patriot Financial Partners II, L.P., Patriot Financial Partners Parallel II, L.P., and certain other shareholders of U.S. Century Bank (incorporated by reference to Exhibit 4.2 to the Registrant's Current Report on Form 8-K (File No. 001-41196) filed with the Securities and Exchange Commission on December 30,
4.3	Assignment and Assumption of Agreement, dated December 30, 2021, between U.S. Century Bank and USCB Financial, Inc. (incorporated by reference to Exhibit 4.3 to the Registrant's Current Report on Form 8-K (File No. 001-41196) filed with the Securities and Exchange Commission on December 30,
4.4	Description of USCB Financial Holdings, Inc.'s securities (incorporated by reference to Exhibit 4.4 to the Registrant's Report on Form 10-K (File No. 001-41196) filed with the Securities and Exchange Commission on March 24,
31.1	Certification of Chief Executive Officer pursuant to Rule 13a-14(a) of the Securities Exchange Act of 1934, as amended, filed with the Securities and Exchange Commission on December 30, 2023.
31.2	Certification of Chief Financial Officer pursuant to Rule 13a-14(a) of the Securities Exchange Act of 1934, as amended, filed with the Securities and Exchange Commission on December 30, 2023.
32.1	Certification of Chief Executive Officer pursuant to 18 U.S.C. Section 639A, filed with the Securities and Exchange Commission on December 30, 2023.
32.2	Certification of Chief Financial Officer pursuant to 18 U.S.C. Section 639A, filed with the Securities and Exchange Commission on December 30, 2023.
101	The following financial statements from the Company's Quarterly Report on Form 10-Q for the quarter ended September 2023 formatted in Inline XBRL: (i) Consolidated Balance Sheets (unaudited), (ii) Consolidated Statements of Operations, (iii) Consolidated Statements of Comprehensive Income (unaudited), (iv) Consolidated Statements of Changes in Stockholders' Equity (unaudited), (v) Consolidated Statements of Cash Flows (unaudited), (vi) Notes to Consolidated Statements (unaudited).
104	Cover Page Interactive Data File (formatted as Inline XBRL and contained in Exhibit 101)

* Filed herewith.
** Furnished
herby.

[Table of Contents](#)

SIGNATURES

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

USCB FINANCIAL HOLDINGS, INC.
(Registrant)

Signature	Title	Date
<u>/s/ Luis de la Aguilera</u> Luis de la Aguilera	Chairman, President and Chief Executive Officer (Principal Executive Officer)	November 9, 2023
<u>/s/ Robert Anderson</u> Robert Anderson	Chief Financial Officer (Principal Financial Officer and Principal Accounting Officer)	November 9, 2023

Exhibit 31.1

Certification of Chief Executive Officer
Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002

I, Luis de la Aguilera, certify that:

1. I have reviewed this Quarterly Report on Form 10-Q of USCB Financial Holdings, Inc.;
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state 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 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, 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) evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report.

Exhibit 31.2

Certification of Chief Financial Officer
Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002

I, Robert Anderson, certify that:

1. I have reviewed this Quarterly Report on Form 10-Q of USCB Financial Holdings, Inc.;
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state 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 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, 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) evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in our

Exhibit 32.1

**Certification of Chief Executive Officer Pursuant to 18 U.S.C. Section 1350
as Adopted Pursuant to Section 906 of the Sarbanes -Oxley Act of 2002**

In connection with the Quarterly Report of USCB Financial Holdings, Inc. (the "Company") on Form 10-Q quarter ended September 30, 2023, as filed with the Securities and Exchange Commission on the date hereof (the "Report"), I, Luis de la Aguilera, as President and Chief Executive Officer of the Company, certify, to the best of my knowledge pursuant to

18 U.S.C. §1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, that:

- 1) The Report fully complies with the requirements of Section 13(a) or 15(d), as applicable, Securities Exchange Act of 1934; and
- 2) The information contained in the Report fairly presents, in all material respects, the financial and results of operations of the Company.

/s/ Luis de la Aguilera

Luis de la Aguilera

Chairman, President and Chief Executive Officer

Date: November 9, 2023

Exhibit 32.2

**Certification of Chief Financial Officer Pursuant to 18 U.S.C. Section 1350
as Adopted Pursuant to Section 906 of the Sarbanes -Oxley Act of 2002**

In connection with the Quarterly Report of USCB Financial Holdings, Inc. (the "Company") on Form 10-Q for the quarter

ended September 30, 2023, as filed with the Securities and Exchange Commission on the date hereof (the "Report"), I,

Robert Anderson, as Chief Financial Officer of the Company, certify, to the best of my knowledge, pursuant to 18 U.S.C.

§1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, that:

- 1) The Report fully complies with the requirements of Section 13(a) or 15(d), as applicable, of the Securities Exchange Act of 1934; and
- 2) The information contained in the Report fairly presents, in all material respects, the financial results of operations of the Company.

/s/ Robert Anderson

Robert Anderson

Chief Financial Officer

Date: November 9, 2023

