

Hamilton Bancorp, Inc.  
Form 10-K  
June 29, 2018

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**UNITED STATES**

**SECURITIES AND EXCHANGE COMMISSION**

**Washington, D.C. 20549**

**FORM 10-K**

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

**For the fiscal year ended March 31, 2018**

**OR**

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

**For the transition period from \_\_\_\_\_ to \_\_\_\_\_**

Commission File Number: **1-35693**

**HAMILTON BANCORP, INC.**

(Exact name of registrant as specified in its charter)

**MARYLAND**

**46-0543309**

(State or other jurisdiction of incorporation or organization) (I.R.S. Employer Identification No.)

**501 Fairmount Avenue, Suite 200, Towson, Maryland**      **21286**

(Address of principal executive offices)

(Zip Code)

**(410) 823-4510**

(Registrant's telephone number, including area code)

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

| <u>Title of each class</u>               | <u>Name of each exchange on which registered</u> |
|--|--|
| Common Stock, par value \$0.01 per share | Nasdaq Capital Market                            |

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

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

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

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

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§ 232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes [ X ] No [ ]

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



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Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, smaller reporting company, or an emerging growth company. See the definitions of “large accelerated filer,” “accelerated filer,” “smaller reporting company,” and “emerging growth company” in Rule 12b-2 of the Exchange Act.

Large accelerated filer [  ]

Accelerated filer [  ]

Non-accelerated filer [  ]

Smaller reporting company [  ]

(Do not check if a smaller reporting company)

Emerging growth company [  ]

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

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

The aggregate market value of the voting and non-voting common equity held by non-affiliates as of September 30, 2017 was \$47,974,641

The number of shares outstanding of the registrant’s common stock as of June 29, 2018 was 3,407,613.

**DOCUMENTS INCORPORATED BY REFERENCE:**

Proxy Statement for the Registrant’s Annual Meeting of Stockholders (Part III)

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*This report contains certain “forward-looking statements” within the meaning of the federal securities laws. These statements are not historical facts; rather, they are statements based on Hamilton Bancorp, Inc.’s current expectations regarding its business strategies, intended results and future performance. Forward-looking statements are preceded by terms such as “expects,” “believes,” “anticipates,” “intends” and similar expressions.*

*Management’s ability to predict results or the effect of future plans or strategies is inherently uncertain. Factors which could affect actual results include changes in interest rates, national and regional economic conditions, legislative and regulatory changes, monetary and fiscal policies of the U.S. government, including policies of the U.S. Treasury and the Federal Reserve Board, the credit quality and composition of the loan and investment portfolios, valuation of assets acquired, deposit flows, competition, demand for loan products and for financial services in Hamilton Bancorp, Inc.’s market area, changes in real estate market values in Hamilton Bancorp, Inc.’s market area, changes in relevant accounting principles and guidelines and the inability of third party service providers to perform as required. For further discussion of factors that may affect the results, see “Item 1A. Risk Factors” in this Annual Report on Form 10-K (“Annual Report”). These factors should be considered in evaluating the forward-looking statements and undue reliance should not be placed on such statements. Except as required by law, we disclaim any intention or obligation to update or revise any forward-looking statements after the date of this Annual Report, whether as a result of new information, future events or otherwise.*

*In this Annual Report, the terms “we,” “our,” and “us” refer to Hamilton Bancorp, Inc. and Hamilton Bank, unless the context indicates another meaning. In addition, we sometimes refer to Hamilton Bancorp, Inc. as “Hamilton Bancorp,” and to Hamilton Bank as the “Bank.”*

**PART I**

**Item 1. BUSINESS**

**General**

Hamilton Bancorp, Inc. (the “Company”) is a Maryland chartered corporation incorporated on June 7, 2012 to serve as the stock holding company for Hamilton Bank (the “Bank”), a state chartered commercial bank. On October 10, 2012, in accordance with a Plan of Conversion adopted by its Board of Directors and approved by its members, the Bank converted from a mutual savings bank to a stock savings bank and became the wholly owned subsidiary of the Company. In connection with the conversion, the Company sold 3,703,000 shares of common stock at a price of \$10.00 per share, through which the Company received net proceeds of approximately \$35,580,000. On December 21, 2017, the Bank converted its charter from a federal savings bank to a Maryland state-chartered commercial bank and now operates under the laws of the State of Maryland. In conjunction with the Bank’s charter conversion, Hamilton

Bancorp converted from a savings and loan holding company to a bank holding company. Hamilton Bancorp's principal business activity is the ownership of the Bank's capital stock and the management of the offering proceeds it retained in connection with the Bank's conversion. Hamilton Bancorp does not own or lease any property but instead uses the premises, equipment and other property of the Bank with the payment of appropriate rental fees, as required by applicable law and regulations, under the terms of an expense allocation agreement. In the future, Hamilton Bancorp may acquire or organize other operating subsidiaries.

Founded in 1915 and celebrating over 100 years of service, the Bank is a community-oriented financial institution, dedicated to serving the financial needs of consumers and businesses within its market area. Our lending market area is considered greater Maryland, southern Pennsylvania, Washington D.C., and northern Virginia. We offer a variety of deposit and loan products in our market area. Our real estate loans consist primarily of one-to- four family mortgage loans (including owner-occupied and non-owner-occupied investor loans), as well as commercial real estate loans, and home equity loans and lines of credit. We also offer commercial term, leases and line of credit loans along with consumer loans consisting primarily of automobile loans, recreational vehicles and loans secured by deposits. We currently operate out of our corporate headquarters in Towson, Maryland and our seven full-service branch offices located in Baltimore City, Cockeysville, Towson, Rosedale, Ellicott City and Pasadena, Maryland. Our market area for deposits is primarily the local counties surrounding our offices. Our primary source of income is loans to small and middle-market businesses and middle-income individuals.

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We also invest in securities, which consist primarily of U.S. government agency, municipal and corporate bond obligations, mortgage-backed securities and collateralized mortgage obligations issued or guaranteed by U.S. government-sponsored enterprises, and to a much lesser extent, equity securities of government-sponsored enterprises.

We offer a variety of deposit accounts, including certificate of deposit accounts, money market accounts, savings accounts, checking accounts and individual retirement accounts. Over the past three years we have borrowed funds from the Federal Home Loan Bank (FHLB) to meet growing loan demand and to facilitate several purchases of loan pools since March 2017. We have also acquired FHLB advances through our acquisitions of Fraternity Community Bancorp, Inc. and Fairmount Bancorp, Inc. completed in May 2016 and September 2015, respectively. We are committed to offering alternative banking delivery systems, including ATMs, online and mobile banking and remote deposit capture.

## **Recent Acquisitions**

On May 13, 2016, the Company completed its acquisition of Fraternity Community Bancorp, Inc. (“Fraternity”) through the merger of Fraternity, the parent company of Fraternity Federal Savings & Loan, with and into the Company pursuant to the Agreement and Plan of Merger dated October 12, 2015, by and between the Company and Fraternity. As a result of the merger, each shareholder of Fraternity received a cash payment equal to nineteen dollars and twenty-five cents (\$19.25) for each share of Fraternity common stock, or an aggregate of approximately \$25.7 million. Immediately following the merger of Fraternity into the Company, Fraternity Federal Savings & Loan was merged with and into the Bank, with the Bank the surviving entity.

On September 11, 2015, the Company completed its acquisition of Fairmount Bancorp, Inc. (“Fairmount”) through the merger of Fairmount, the parent company of Fairmount Bank, with and into the Company pursuant to the Agreement and Plan of Merger dated as of April 15, 2015, by and between the Company and Fairmount. As a result of the merger, each shareholder of Fairmount received a cash payment equal to thirty dollars (\$30.00) for each share of Fairmount common stock, or an aggregate of approximately \$15.4 million. Immediately following the merger of Fairmount, Fairmount Bank was merged with and into the Bank, with the Bank the surviving entity.

As a result of the acquisitions, we have added three branches to our branch structure in the Baltimore area. (See Note 3 – “*Acquisition*” of the consolidated financial statements for additional discussion concerning the more recent acquisition of Fraternity).

## **Available Information**

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The Bank's website address is [www.hamilton-bank.com](http://www.hamilton-bank.com). Available through the Investor Relations area of our website are annual reports on Form 10-K, quarterly reports on Form 10-Q, news releases on Form 8-K, and any amendments to those reports filed or furnished pursuant to Section 13(a) or 15(d) of the Exchange Act. In general, we intend that these reports be available as soon as practicable after they are filed with or furnished to the Securities and Exchange Commission ("SEC"). Information on the Bank's website should not be considered a part of this Annual Report.

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**Market Area**

We conduct our operations from our seven full-service banking offices in Maryland. Our primary deposit market includes the areas surrounding our banking offices in Cockeysville, Pasadena, Towson, Rosedale, Ellicott City and two locations in Baltimore City. In July 2017, we re-located our Ellicott City branch in Howard County a short distance away from the former location so as to still serve our existing customer base and surrounding area. The landlord, whom the property was leased from, is converting the former branch property into other commercial space. In March 2018 we also re-located our Pigtown branch, located in Baltimore City, just a few doors down from our former branch. The new branch locations are both smaller in size, offering cost savings, and allowed us to redesign our branches so the needs of our customers can be better served. In the new locations we did away with the conventional teller line and created a more open space with the use of a cash recycler. Our employees can now interact and provide greater assistance to our customers in a friendlier and inviting environment.

The Bank considers greater Maryland, southern Pennsylvania, Washington D.C., and northern Virginia its primary lending area for its various consumer, commercial and mortgage lending services. It is the policy of the Bank to focus on lending to customers within its primary lending area, and/or to collateralize secured loans with real property located within the primary lending area. However, we occasionally purchase or make loans secured by collateral located outside of our primary lending market, especially to borrowers with whom we have an existing relationship or who have a significant presence within our primary market. Our primary lending market contains a diverse cross section of employment sectors, with a mix of services, manufacturing, wholesale/retail trade, federal and local government, health care facilities and finance related employment. The city of Baltimore is now considered a major center for both the financial and health service industries.

Our branch network includes Baltimore City and the Maryland counties of Anne Arundel, Howard, and Baltimore. Maryland continues to rank first in the nation with respect to median household income, as reflected in 2016, with median household income of nearly \$79,000 compared to a national average of \$58,000. Both Howard and Anne Arundel county rank amongst the top counties in the state with respect to household income and report lower unemployment. Baltimore City, Baltimore County, Howard, and Anne Arundel County reported preliminary unemployment rates of 6.1%, 4.3%, 3.1% and 3.6%, respectively, for December 2017, compared to the statewide and national unemployment rates of 4.3% and 3.9%, respectively.

**Competition**

We face significant competition within our market both in making loans and attracting deposits. Our market area has a high concentration of financial institutions including large money center and regional banks, community banks and credit unions. Some of our competitors offer products and services that we currently do not offer, such as trust services and private banking. Our competition for loans and deposits comes principally from commercial banks, savings institutions, internet banks, mortgage banking firms, consumer finance companies, credit unions, and

non-bank lenders. We face additional competition for deposits from short-term money market funds, brokerage firms, mutual funds and insurance companies. Our primary focus is to build and develop profitable customer relationships across all lines of business while maintaining our position as a community bank.

As of June 30, 2017 (the latest date for which information is available), our market share was 0.38% of total deposits in Baltimore City, making us the 12th largest out of 27 financial institutions in Baltimore City. In addition, as of June 30, 2017, our deposit market share was 1.25%, 0.41% and 0.65% of total deposits in Baltimore County, Anne Arundel, and Howard County, respectively, making us the 12th largest out of 32 financial institutions in Baltimore County, the 20th largest out of 28 financial institutions in Anne Arundel County and 16<sup>th</sup> largest out of 20 financial institutions in Howard County.

### **Lending Activities**

**General.** Historically, our principal lending activity has been the origination of mortgage loans collateralized by one-to-four family residential real estate located within our primary market area. In recent years we have reduced our emphasis on the origination of one-to-four family mortgage lending to become less reliant on the origination of such loans for growth and to emphasize the origination of commercial business and commercial real estate lending. This will allow the Bank to develop a more diversified loan portfolio, generate loan growth from different resources, and provide our customers with more products and services that fit their needs. In connection with this strategy, we have hired several commercial real estate and commercial business loan officers over the past couple of years with strong experience in these lending areas. In addition, back office commercial loan personnel have also been hired to assist with the processing, underwriting, and monitoring of our commercial loan portfolio. Our commercial loan underwriting analysis is maintained in-house and allows us to be more efficient in originating loans and enhancing the customer experience. We sold a majority of our newly originated one-to-four family mortgage loans with terms over 10 years into the secondary market. However, towards the end of fiscal 2017 and throughout fiscal 2018, we did retain in our portfolio the fixed-rate residential mortgages we originated due to the amount of run-off we were experiencing within the portfolio. In addition to commercial business loans and leases, commercial real estate loans and residential mortgage loans, we also offer home equity loans and lines of credit, residential and commercial construction loans, and, to a much lesser extent, other consumer loans.

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Our portfolio of one-to four-family residential loans have increased in amount during fiscal 2018 and 2017 due to the purchase of several pools of loans in fiscal 2018 and our acquisition of Fraternity in fiscal 2017. The percentage of one-to four-family loans to total loans, however, has declined from 44% at March 31, 2017 to 40% at March 31, 2018.

**Loan Portfolio Composition.** Set forth below is selected information concerning the composition of our loan portfolio in dollar amounts and in percentages as of the dates indicated. Amounts shown do not include loans held for sale equal to \$-0-, \$-0-, \$259,000, \$581,000 and \$-0- at March 31, 2018, 2017, 2016, 2015 and 2014, respectively.

|  | At March 31,<br>2018   |         | 2017        |         | 2016       |         |   |
|--|------------------------|---------|-------------|---------|------------|---------|---|
|  | Amount                 | Percent | Amount      | Percent | Amount     | Percent |   |
|  | (Dollars in thousands) |         |             |         |            |         |   |
| Real estate loans:                           |                        |         |             |         |            |         |   |
| Residential mortgage loans:                  |                        |         |             |         |            |         |   |
| One- to four-family residential              | \$163,448              | 42.0    | % \$157,446 | 46.4    | % \$69,300 | 31.1    | % |
| One- to four-family investor                 | 26,736                 | 6.9     | 25,522      | 7.5     | 27,860     | 12.5    |   |
| Commercial construction                      | 7,116                  | 1.8     | 3,190       | 0.9     | 8,527      | 3.8     |   |
| Commercial                                   | 112,166                | 28.8    | 107,564     | 31.7    | 78,115     | 35.1    |   |
| Total real estate loans                      | 309,466                | 79.5    | 293,722     | 86.6    | 183,802    | 82.5    |   |
| Commercial business loans                    | 40,144                 | 10.3    | 21,537      | 6.4     | 20,395     | 9.2     |   |
| Consumer:                                    |                        |         |             |         |            |         |   |
| Home equity loans and lines of credit        | 19,996                 | 5.1     | 20,544      | 6.1     | 14,391     | 6.4     |   |
| Other consumer                               | 19,615                 | 5.0     | 3,197       | 0.9     | 4,179      | 1.9     |   |
| Total consumer loans                         | 39,611                 | 10.2    | 23,741      | 7.0     | 18,570     | 8.3     |   |
| Total loans receivable                       | 389,221                | 100.0   | % 339,000   | 100.0   | % 222,767  | 100.0   | % |
| Premium (discount) on loans acquired         | 1,412                  |         | 76          |         | (769       | )       |   |
| Net deferred loan origination fees and costs | (212                   | )       | (143        | )       | (139       | )       |   |
| Allowance for loan losses                    | (2,822                 | )       | (2,195      | )       | (1,702     | )       |   |
| Total loans receivable, net                  | \$387,599              |         | \$336,738   |         | \$220,157  |         |   |

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|  | At March 31,<br>2015 |         | 2014      |         |
|--|----------------------|---------|-----------|---------|
|  | Amount               | Percent | Amount    | Percent |
| (Dollars in thousands)                       |                      |         |           |         |
| Real estate loans:                           |                      |         |           |         |
| Residential mortgage loans:                  |                      |         |           |         |
| One- to four-family residential              | \$49,865             | 31.1 %  | \$57,674  | 39.8 %  |
| One- to four-family investor                 | 12,971               | 8.1     | 14,000    | 9.7     |
| Commercial construction                      | 6,362                | 4.0     | 3,268     | 2.3     |
| Commercial                                   | 59,273               | 36.9    | 41,406    | 28.6    |
| Total real estate loans                      | 128,471              | 80.1    | 116,348   | 80.4    |
| Commercial business loans                    | 18,490               | 11.5    | 15,657    | 10.8    |
| Consumer:                                    |                      |         |           |         |
| Home equity loans and lines of credit        | 12,261               | 7.6     | 11,660    | 8.0     |
| Other consumer                               | 1,166                | 0.8     | 1,154     | 0.8     |
| Total consumer loans                         | 13,427               | 8.4     | 12,814    | 8.8     |
| Total loans receivable                       | 160,388              | 100.0 % | 144,819   | 100.0 % |
| Premium (discount) on loans acquired         | -                    |         | -         |         |
| Net deferred loan origination fees and costs | (103 )               |         | (119 )    |         |
| Allowance for loan losses                    | (1,690 )             |         | (1,786 )  |         |
| Total loans receivable, net                  | \$158,595            |         | \$142,914 |         |

**Loan Portfolio Maturities and Yields.** The following table summarizes the scheduled repayments of our loan portfolio at March 31, 2018. Demand loans, loans having no stated repayment schedule or maturity, and overdraft loans are reported as being due in one year or less.

| Due During the Years Ending<br>March 31, | One- to<br>Four-Family<br>Residential Real<br>Estate |                             | One- to<br>Four-Family<br>Investor Real<br>Estate |                             | Commercial<br>Construction<br>Real Estate |                             | Commercial Real<br>Estate |                             |
|--|--|-----------------------------|---|-----------------------------|---|-----------------------------|---------------------------|-----------------------------|
|  | Amount   | Weighted<br>Average<br>Rate | Amount  | Weighted<br>Average<br>Rate | Amount                                    | Weighted<br>Average<br>Rate | Amount                    | Weighted<br>Average<br>Rate |
| (Dollars in thousands)                   |  |                             |   |                             |   |                             |                           |                             |
| 2019                                     | \$5,740  | 4.43 %                      | \$2,935   | 7.38 %                      | \$2,441                                   | 5.10 %                      | \$12,696                  | 3.95 %                      |
| 2020                                     | 541  | 4.84                        | 1,142   | 6.26                        | 401                                       | 6.00                        | 8,357                     | 4.14                        |
| 2021                                     | 1,195  | 4.52                        | 692   | 6.76                        | -   | -                           | 2,636                     | 4.66                        |
| 2022 to 2023                             | 1,965  | 3.35                        | 4,424   | 5.78                        | -   | -                           | 19,746                    | 4.74                        |
| 2024 to 2028                             | 6,164  | 3.83                        | 8,874   | 5.69                        | 3,829                                     | 5.11                        | 56,238                    | 4.30                        |
| 2029 to 2033                             | 13,826   | 3.62                        | 2,260   | 5.29                        | 139                                       | 6.62                        | 6,034                     | 4.52                        |



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|                 |           |        |          |        |         |        |           |        |
|-----------------|-----------|--------|----------|--------|---------|--------|-----------|--------|
| 2034 and beyond | 134,017   | 4.14   | 6,409    | 5.79   | 306     | 5.25   | 6,459     | 5.31   |
| Total           | \$163,448 | 4.09 % | \$26,736 | 5.93 % | \$7,116 | 5.19 % | \$112,166 | 4.40 % |

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|                                       | Commercial Business |                       | Home Equity Loans and Lines of Credit |                       | Other Consumer |                       | Total       |                       |   |
|---------------------------------------|---------------------|-----------------------|---------------------------------------|-----------------------|----------------|-----------------------|-------------|-----------------------|---|
|                                       | Amount              | Weighted Average Rate | Amount                                | Weighted Average Rate | Amount         | Weighted Average Rate | Amount      | Weighted Average Rate |   |
| (Dollars in thousands)                |                     |                       |                                       |                       |                |                       |             |                       |   |
| Due During the Years Ending March 31, |                     |                       |                                       |                       |                |                       |             |                       |   |
| 2019                                  | \$9,569             | 4.96                  | % \$110                               | 7.26                  | % \$1,151      | 2.78                  | % \$34,642  | 4.65                  | % |
| 2020                                  | 2,065               | 4.05                  | 152                                   | 4.70                  | 212            | 4.96                  | 12,870      | 4.42                  |   |
| 2021                                  | 3,964               | 5.15                  | 192                                   | 6.02                  | 365            | 4.85                  | 9,044       | 5.05                  |   |
| 2022 to 2023                          | 15,510              | 4.65                  | 428                                   | 5.65                  | 249            | 5.06                  | 42,322      | 4.76                  |   |
| 2024 to 2028                          | 7,355               | 4.65                  | 2,928                                 | 4.70                  | 3,531          | 5.52                  | 88,919      | 4.53                  |   |
| 2029 to 2033                          | 374                 | 4.50                  | 4,467                                 | 4.75                  | 11,715         | 4.60                  | 38,815      | 4.30                  |   |
| 2034 and beyond                       | 1,307               | 4.62                  | 11,719                                | 4.68                  | 2,392          | 4.21                  | 162,609     | 4.30                  |   |
| Total                                 | \$40,144            | 4.74                  | % \$19,996                            | 4.75                  | % \$19,615     | 4.63                  | % \$389,221 | 4.46                  | % |

**Fixed and Adjustable-Rate Loan Schedule.** The following table sets forth at March 31, 2018, the dollar amount of all fixed-rate and adjustable-rate loans due after March 31, 2019.

|                                       | Due after March 31, 2019 |            |           |
|---------------------------------------|--------------------------|------------|-----------|
|                                       | Fixed                    | Adjustable | Total     |
| (In thousands)                        |                          |            |           |
| Real estate loans:                    |                          |            |           |
| One- to four-family residential       | \$132,291                | \$25,417   | \$157,708 |
| One- to four-family investor          | 19,827                   | 3,974      | 23,801    |
| Commercial construction               | 2,297                    | 2,378      | 4,675     |
| Commercial                            | 87,740                   | 11,730     | 99,470    |
| Commercial business loans             | 26,762                   | 3,813      | 30,575    |
| Consumer loans:                       |                          |            |           |
| Home equity loans and lines of credit | 4,171                    | 15,715     | 19,886    |
| Other consumer                        | 18,464                   | -          | 18,464    |
| Total loans                           | \$291,552                | \$63,027   | \$354,579 |

**Residential Mortgage Loans.** Hamilton Bank originates mortgage loans secured by owner occupied one-to-four family residential properties. To a lesser extent, we have also acquired, participated and made loans to investors for the purchase of one-to-four family residential properties that are not owner-occupied. As of March 31, 2018, we had a total of \$190.2 million of residential mortgage loans secured by one-to-four family properties, of which \$163.4 million, or 85.9%, were secured by properties serving as the primary residence of the owner. The remaining \$26.7

million, or 14.1%, of such loans were secured by non-owner-occupied residential properties. The majority of our residential mortgage loans are secured by properties within our primary lending area of greater Maryland, southern Pennsylvania, Washington D.C., and northern Virginia, however, during fiscal 2018 we did purchase several residential mortgage loan pools totaling \$19.3 million in areas outside of our market.

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Historically, the terms of our one-to-four family mortgage loans retained in our portfolio ranged from 10 to 30 years. In order to lower our interest rate risk in a rising rate environment though, we have been selling to the secondary market the majority of our one-to-four family fixed rate loans that have been originated with terms exceeding 10 years. However, towards the end of fiscal 2017 and throughout fiscal 2018, we did portfolio the fixed-rate residential mortgages we originated due to the amount of run-off we were experiencing within the portfolio. In fiscal 2019, we plan to sell these loans into the secondary market. During fiscal 2017 and 2016, we sold \$2.2 million, or 23.5%, and \$4.4 million, or 68.0%, of one-to-four family mortgage loans that we originated with terms exceeding 10 years, respectively. Our residential mortgage portfolio is almost entirely comprised of fixed-rate loans, with 83.9% of residential mortgage loans due after March 31, 2019 having fixed rates at March 31, 2018. During the year ended March 31, 2018, we originated \$1.5 million in residential mortgage loans with adjustable-rates.

We generally do not make new one-to-four family mortgage loans on owner-occupied properties with loan-to-value ratios exceeding 95% at the time the loan is originated, and all loans with loan-to-value ratios in excess of 80% require private mortgage insurance. Loan to value ratios on refinances may not exceed 80%, and loan-to-value ratios for non-owner-occupied properties may not exceed 85%. In addition, borrower debt may generally not exceed 43% of the borrower's monthly cash flow. With respect to borrower debt on loans secured by non-owner-occupied properties, we look to the investor's aggregate debt and cash flows from all investment properties the investor operates. We require all properties securing residential mortgage loans to be appraised by a board-approved independent appraiser.

Loans secured by non-owner-occupied properties typically have five to ten year terms and amortize over a 25 to 30 year period. Because of the increased risk associated with non-owner-occupied properties, interest rates on such loans are higher than owner-occupied properties; averaging 5.9% during the year ended March 31, 2018. We have generally only originated loans secured by non-owner-occupied properties to investors that reside in our market area.

In an effort to provide financing for first-time home buyers, we offer 30-year fixed-rate one-to-four family mortgage loans with loan-to-value ratios up to 95%, which cannot be readily sold to the secondary market and are held in portfolio.

We also make "jumbo loans" (loans above \$424,100, the current maximum conforming loan amount as established by the Federal Housing Finance Agency) that we may sell into the secondary market or retain in the Bank's portfolio depending upon the residential mortgage run-off at the time. Jumbo loans that we originate and sell, typically have 30-year terms and maximum loan-to-value ratios of 80%. At March 31, 2018, our largest outstanding portfolio jumbo residential mortgage loan was for \$2.3 million at origination, with a current book balance of \$1.9 million. This loan is performing in accordance with its original terms.

From 2009 through part of fiscal 2017, applications for loans that we intended to sell were processed through Mortgage Department Services, LLC ("MDS"), a company in which we had a minority interest. In fiscal 2017 we brought this process in-house using various software programs. Each application and loan is reviewed to ensure that

the loan meets the standards for sale to the secondary market and the Bank's portfolio (See "—Loan Originations, Participations, Purchases and Sales"). When we sell loans in the secondary market, we typically sell the loans at a premium and record the income immediately as a gain on sale of loans. All such loans are sold with servicing released and in most cases, with recourse that we provide to the purchaser in the case of (i) delinquency within the first 90 days of sale or (ii) breaches of customary representations and warranties to the buyers.

All residential mortgage loans that we originate include "due-on-sale" clauses, which give us the right to declare a loan immediately due and payable in the event that, among other things, the borrower sells or otherwise disposes of the real property subject to the mortgage and the loan is not repaid. All borrowers are required to obtain title insurance for the benefit of Hamilton Bank. We also require homeowner's insurance and fire and casualty insurance and, where circumstances warrant, flood insurance.

***Commercial Real Estate Loans.*** We originate commercial real estate loans within our primary lending area, with an emphasis on the Greater Baltimore region, that are secured by properties used for business purposes such as small office buildings or retail facilities. We have increased our origination of commercial real estate loans over the last several years. At March 31, 2018, commercial real estate loans amounted to 28.8% of total loans or \$112.2 million, including \$11.8 million acquired in the Fraternity acquisition, compared to approximately \$41.4 million, or 28.6% of total loans, at March 31, 2014.

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Our commercial real estate loans are underwritten based on our loan underwriting policies. Our policies provide that such loans may be made in amounts of up to 85% of the appraised value of the property, provided that the property is more than 50% owner-occupied or 75% of the appraised value of the property if it is not owner-occupied. Our commercial real estate loans typically have terms of 5 to 10 years and amortize for a period of up to 25 years. In the past year we have originated an increased amount of commercial real estate loans with terms of 7 to 10 years based upon the strength of the property cash flow and loan to value ratio. Interest rates may be fixed or adjustable. If adjustable, then they are generally based on the Prime rate of interest, LIBOR, or U.S. Treasuries Constant Maturity.

The regulatory loan-to-one borrower limit is 15% of a bank's unimpaired capital plus unimpaired surplus, or approximately \$6.3 million at March 31, 2018. We have adopted an internal limit equal to 75% of the Bank's loan-to-one borrower limit. The internal limit at March 31, 2018 is \$4.7 million. We generally target commercial real estate loans with balances of \$250,000 to \$4.0 million. At March 31, 2018, our commercial real estate loans had an average balance of \$807,000. At that same date, our largest commercial real estate relationship consisted of one loan totaling \$4.7 million. This loan is secured by a shopping center, and was performing in accordance with their original terms at March 31, 2018.

Commercial real estate lending involves additional risks compared to one-to-four family residential lending because payments on loans secured by commercial real estate properties are often dependent on the successful operation or management of the properties, and/or the collateral value of the commercial real estate securing the loan. Repayment of such loans may be subject, to a greater extent than residential loans, to adverse conditions in the real estate market or the economy. Also, commercial real estate loans typically involve larger loan balances in relation to single borrowers or groups of related borrowers. Commercial real estate loans generally have a higher rate of interest and shorter term than residential mortgage loans because of increased risks associated with this type of lending. We seek to minimize these risks through our underwriting standards. We have experienced a decrease over the past several years in the number of delinquencies and non-performing loans in our commercial real estate loan portfolio. See "Risk Factors—Our increase in commercial real estate loans has increased our credit risk."

**Commercial Business Loans.** We originate commercial business loans and lines of credit secured by non-real estate business assets. These loans are generally originated to small and middle market businesses in our primary market area, although in fiscal 2018 we purchased a \$15.5 million pool of commercial equipment lease loans that are considered out of our market area. Our commercial business loans are generally used for working capital purposes or for acquiring equipment, inventory or furniture, and are primarily secured by business assets other than real estate, such as business equipment, inventory and accounts receivable. We have increased our origination of commercial business loans over the last few years and intend to continue to grow this portfolio at a moderate pace. At March 31, 2018, commercial business loans and lines of credit outstanding totaled \$40.1 million, including the \$15.5 million pool of commercial equipment lease loans. This loan segment amounted to 10.3% of total loans, compared to approximately \$15.7 million, or 10.8% of total loans, at March 31, 2014. At March 31, 2018, we also had \$9.2 million of available and unfunded commercial business lines of credit.

Our commercial business loans have terms up to five years at both fixed and adjustable rates of interest, although, adjustable rates of interest are preferred and obtained when possible. Our commercial business loans are underwritten based on our commercial business loan underwriting policies. We typically avoid making commercial business loans to purchase highly specialized, custom made equipment which may be difficult to dispose of in the event of default. When making commercial business loans, we consider the financial statements, lending history and debt service capabilities of the borrower (generally requiring a minimum debt service coverage ratio of 1.20:1.00), the projected cash flows of the business, and the value of the collateral, if any. The majority all commercial business loans are guaranteed by the principals of the borrower.

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Hamilton Bank is also qualified to make Small Business Administration (“SBA”) loans. The SBA program is an economic development program which finances the expansion of small businesses. Under the SBA program, we originate and fund loans under the SBA 7(a) Loan Program which qualify for guarantees up to 85% for loans less than or equal to \$150,000 and 75% for loans greater than \$150,000. We also originate loans under the SBA’s CDC/504 Loan Program in which we generally provide 50% of the financing, taking a first lien on the real property as collateral. We do not treat the SBA guarantee as a substitute for a borrower meeting our credit standards, and, except for minimum capital levels or maximum loan terms, the borrower must meet our other credit standards as applicable to loans outside the SBA process. During fiscal 2018 and fiscal 2017, we did not originate any loans under the SBA 7(a) Loan Program.

We focus on the origination of commercial business loans in amounts between \$250,000 and \$4.0 million. At March 31, 2018, our commercial business loans had an average outstanding balance of \$180,000. At that same date, our largest commercial business loan was a commercial line of credit with a commitment balance of \$5.0 million, of which \$2.5 million has been advanced. The loan is secured by the business assets of the company and is performing in accordance with its original terms at March 31, 2018.

Commercial business loans generally have a greater credit risk than one-to-four family residential mortgage loans and real estate backed commercial loans. Unlike residential and commercial mortgage loans, which generally are made on the basis of the borrower’s ability to make repayment from his or her employment and other income, and which are secured by real property whose value tends to be more easily ascertainable, commercial business loans are of higher risk and typically are made on the basis of the borrower’s ability to make repayment from the cash flow of the borrower’s business. As a result, the availability of funds for the repayment of commercial business loans may be substantially dependent on the success of the business itself. Further, the collateral securing the loans may depreciate over time, may be difficult to appraise and may fluctuate in value based on the success of the business. We seek to minimize these risks through our underwriting standards. See “Risk Factors - Our entry into commercial real estate and commercial business lending may result in higher losses on our loans.”

***Home Equity Loans and Lines of Credit.*** We offer home equity loans and lines of credit that are secured by the borrower’s primary or secondary residence. At March 31, 2018, we had \$20.0 million, or 5.1% of our total loan portfolio in home equity loans and lines of credit. At that date we also had \$22.6 million of undisbursed funds related to home equity lines of credit.

Home equity loans and lines of credit are generally underwritten using the same criteria that we use to underwrite one-to-four family residential mortgage loans. Home equity loans and lines of credit may be underwritten with a loan-to-value ratio of up to 80% when combined with the principal balance of the existing first mortgage loan. Our home equity loans are primarily originated with fixed rates of interest with terms of up to 20 years. Our home equity lines of credit are originated with adjustable-rates based on the prime rate of interest plus or minus an applicable margin and require interest paid monthly. Home equity loans and lines of credit are available in amounts of between \$10,000 and \$1.0 million.



Home equity loans and lines of credit secured by second mortgages have greater risk than one-to-four family residential mortgage loans secured by first mortgages. We face the risk that the collateral will be insufficient to compensate us for loan losses and costs of foreclosure. When customers default on their loans, we attempt to foreclose on the property and resell the property as soon as possible to minimize foreclosure and carrying costs. However, the value of the collateral may not be sufficient to compensate us for the amount of the unpaid loan and we may be unsuccessful in recovering the remaining balance from those customers. Particularly with respect to our home equity loans and lines of credit, decreases in real estate values could adversely affect the value of property securing the loan.

**Construction Loans.** We originate construction loans for both commercial and residential real estate. Construction loans we originate generally provide for the payment of interest only during the construction phase. At the end of the construction phase, the loan converts to a permanent mortgage loan at the same or a different rate of interest. The construction period on the residential homes is typically nine to twelve months, at which time Hamilton Bank is repaid through permanent financing by a third party with servicing released or the loan is converted under the loan documents to a permanent loan and is retained in the Bank's portfolio.

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Before making a commitment to fund a construction loan, Hamilton Bank requires detailed cost estimates to complete the project and an appraisal of the property by an independent licensed appraiser. Hamilton Bank also reviews and inspects each property before disbursement of funds during the term of the construction loan. Loan proceeds are disbursed after inspection based on the percentage of completion method. Construction loans for one-to-four family residential real estate may be underwritten with a loan-to-value ratio of up to 80% or 95% with private mortgage insurance. Commercial construction loans generally may not exceed a loan-to-value ratio of 75% to 80%.

Construction lending generally involves a greater degree of risk than other one-to-four family mortgage lending. The repayment of the construction loan is, to a great degree, dependent upon the successful and timely completion of construction. Various potential factors including construction delays or the financial viability of the builder may further impair the borrower's ability to repay the loan.

At March 31, 2018, total construction loans represented \$12.6 million, or 3.2%, of Hamilton Bank's total loans, of which \$5.5 million consisted of residential construction loans and \$7.1 million were commercial construction. At March 31, 2018, the commitment to fund or advance funds on total construction loans equaled \$13.2 million. At March 31, 2018, our largest construction loan was a commercial construction loan with a contractual principal and recorded investment balance of \$1.5 million. This loan is under the SBA CDC/504 loan program and we are waiting to be taken out by the SBA. The loan is secured by the commercial property being constructed and is performing in accordance with its original terms at March 31, 2018.

**Other Consumer Loans.** We make loans secured by deposit accounts up to 90% of the amount of the depositor's deposit account balance. On a more limited basis, we also originate automobile loans to our customers, along with boats, motorcycles, and recreational vehicles. During fiscal 2018 we purchased two loan pools consisting of recreational vehicles from the same seller that totaled \$19.8 million. These loans are located outside of what is considered our lending area. Other consumer loans at March 31, 2018 totaled \$19.6 million, or 5.0% of our total loan portfolio.

**Loan Originations, Participations, Purchases and Sales.** Most of our loan originations are generated by our loan personnel operating at our corporate headquarters and banking office locations. All loans we originate are underwritten pursuant to our policies and procedures. While we originate fixed-rate and adjustable-rate loans, our ability to generate each type of loan depends upon relative borrower demand and the pricing levels as set in the local marketplace by competing banks, thrifts, credit unions, and mortgage banking companies. Our volume of real estate loan originations is influenced significantly by market interest rates. As a result, the volume of our real estate loan originations can vary from period to period.

Consistent with our interest rate risk strategy, in the low interest rate environment that has existed in recent years, we have sold on a servicing-released basis the majority of our one-to-four family residential mortgage loans with maturities over 10 years that we have originated. All loan applications originated from 2009 through the first part of

2017, that we had the intention of selling, were processed through a third party. That third party has since dissolved and we started directly underwriting and selling loans in the secondary market ourselves in 2017. Through the Fraternity acquisition, we obtained the necessary software and personnel to be able to process loans we intend to sell in-house. We receive a premium for each loan that is delivered or sold to the secondary market. When a loan is sold, it is sold with servicing released and in most cases, with recourse that we provide to the purchaser in the event of (i) delinquency within the first 90 days of sale or (ii) breaches of customary representations and warranties to the buyers. As a result of the acquisitions, the amount of normal attrition and prepayments associated with the one-to-four family residential mortgage portfolio increased during fiscal 2018. Consequently, we began to portfolio our residential mortgage loan originations versus selling them in the secondary market during fiscal 2018 so as to maintain our loan diversification. We are however, once again looking to start selling residential mortgage loans in the secondary market

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From time to time, we have purchased loan participations in commercial loans in which we are not the lead lender that are secured by real estate or other assets within the state of Maryland. With regard to all loan participations, we follow our customary loan underwriting and approval policies, and although we may be only approving and servicing a portion of the loan, we underwrite the loan request as if we had originated the loan to ensure cash flow and collateral are sufficient. At March 31, 2018, our loan participations totaled \$18.7 million, or 4.8% of our total loan portfolio, the majority of which were in our primary market area. Of the \$18.7 million in participations, only \$32,000 are on nonaccrual at March 31, 2018 compared to \$126,000 at March 31, 2017. We do not specifically look to loan participations as a means to increase loan volume; however, we do look at opportunities for participations, if presented, on a case by case basis.

In addition to loan participations, we may look to purchase pools or portfolios of loans from time-to-time to enhance growth and earnings potential. As with participations, we follow our customary loan underwriting standards when reviewing a particular pool of loans to determine if the purchase meets the Bank's established credit guidelines. Based upon the number of loans within a particular pool, we may not be able to review the loan pool on a loan-by-loan basis, but will review the loan data requested on the entire pool, such as delinquency, credit scores, and appraised values and examine an adequate sample of the individual loans that make up the loan pool. During fiscal 2018 we purchased several pools of loans both within and outside of our market area. The loan pools totaled \$54.6 million and consisted of \$15.5 million in commercial lease loans, \$19.8 million in recreational vehicles, and \$19.3 million in one-to-four-family residential mortgage loans. The loan purchases were funded through the use of cash and approximately \$27.0 million in new FHLB borrowings. At the end of fiscal 2017 we also purchased \$23.4 million of one-to-four family jumbo residential mortgage loans in two separate pools. These purchases were funded with approximately \$12.5 million in cash and \$11.5 million in borrowings from the FHLB. We entered into a cash flow hedge with respect to these borrowings to lock in a long-term cost of funds and minimize some of the interest rate risk associated with purchasing longer-term assets.

In May 2016, in connection with the acquisition of Fraternity Federal Savings and Loan, we acquired approximately \$108.7 million in outstanding loans. As of March 31, 2018, the outstanding balance of those acquired from Fraternity totaled \$79.4 million, or 20.4% of gross loans, of which \$70,000 are on non-accrual. The remaining loans are performing as agreed under their current terms at March 31, 2018. In September 2015, prior to Fraternity, we acquired Fairmount Bank and approximately \$53.6 million in outstanding loans, of which \$32.1 million remain outstanding at March 31, 2018. The outstanding Fairmount loans make-up 8.2% of gross loans at March 31, 2018.

As noted earlier, we may sell residential mortgage loans into the secondary market at a premium. We also have the ability to sell certain pools of loans to increase liquidity, improve current earnings, divest of a concentration of loans, or manage problem credits. When selling a pool of loans, we analyze whether the sale makes sense from a profit standpoint and then look for several bids from various parties so as to maximize the price with respect to the sale. In fiscal 2017 we sold two pools of loans with a combined book value of \$4.5 million. Both pools consisted primarily of one-to-four family non-owner occupied residential mortgage ("residential investor") loans acquired in the Fairmount Bank acquisition. The financial performance of the residential investor loans sold was deteriorating and the underlying collateral did not provide sufficient support. Selling the pool of loans made the most sense with respect to managing these problem credits and reducing any additional losses going forward.



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The following table shows our loan origination, repayment and sale activities for the fiscal years indicated.

|   | <b>Year Ended March</b> |             |
|---|-------------------------|-------------|
|   | <b>31,</b>              |             |
|   | <b>2018</b>             | <b>2017</b> |
|   | <b>(In thousands)</b>   |             |
| Total loans at beginning of year          | \$339,000               | \$222,767   |
| Loans originated:                         |                         |             |
| Real estate loans:                        |                         |             |
| Residential mortgage loans:               |                         |             |
| One- to four-family residential           | 16,788                  | 21,837      |
| One- to four-family investor              | -                       | -           |
| Commercial construction                   | 5,654                   | 4,759       |
| Commercial                                | 16,218                  | 25,397      |
| Total real estate loans                   | 38,660                  | 51,993      |
| Commercial business loans                 | 8,125                   | 10,117      |
| Consumer:                                 |                         |             |
| Home equity loans and lines of credit     | 6,452                   | 5,920       |
| Other consumer                            | 226                     | 112         |
| Total consumer loans                      | 6,678                   | 6,032       |
| Total loans originated                    | 53,463                  | 68,142      |
| Fraternity Bank loans acquired            | -                       | 108,804     |
| Residential loan pool purchases           | 19,251                  | 23,422      |
| SBA commercial loans purchased            | 3,254                   |             |
| Commercial lease loan pool purchased      | 15,473                  | -           |
| Recreational vehicle loan pools purchased | 19,961                  | -           |
| Deduct:                                   |                         |             |
| Principal repayments                      | 51,919                  | 62,724      |
| Loans sold in the secondary market        | -                       | 6,640       |
| Transferred to foreclosed real estate     | 24                      | 127         |
| Unused lines of credit                    | 9,238                   | 14,644      |
| Net loan activity                         | 50,221                  | 116,233     |
| Total loans at end of year                | \$389,221               | \$339,000   |

**Loan Approval Procedures and Authority.** Our lending activities follow written, non-discriminatory underwriting standards and loan origination procedures developed by management and approved by our board of directors. The loan approval process is intended to assess the borrower's ability to repay the loan and the value of the collateral that will secure the loan. To assess the borrower's ability to repay, our policies provide for the review of the borrower's

employment and credit history and information on the historical and projected income and expenses of the borrower. We will also evaluate a guarantor when a guarantee is provided as part of the loan.

Hamilton Bank's policies and loan approval limits are established by our board of directors. Designated Bank officers and loan committee are assigned levels of loan authority. Having loan authority gives the individuals or committee the ability to authorize the extension of credit. Every extension of credit requires two signatures, one of which must have sufficient authority given the risk rating and aggregate exposure. The second approver cannot be an individual assigned less loan authority than the sponsor of the loan. Loan authority is recommended by the Chief Credit Officer and approved by the Loan Committee. All loan authorities are reviewed and confirmed annually by the Loan Committee. The Chief Credit Officer, and or the President may recommend interim changes to establish loan limits or assign loan authority for new officers. These interim changes shall be presented to the Loan Committee for approval at its next regularly scheduled meeting. The Chief Credit Officer and/or the President also have the authority to reduce or remove loan authority. Such changes in lending authority are to be reported to Loan Committee after the fact.

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**Securities Activities**

**General.** Our investment policy is developed by management and approved by the board of directors. The objectives of the policy are to: (i) ensure adequate liquidity for loan demand and deposit fluctuations, and to allow us to alter our liquidity position to meet both day-to-day and long-term changes in assets and liabilities; (ii) manage interest rate risk in accordance with our interest rate risk policy; (iii) provide collateral for pledging requirements; (iv) maximize return on our investments; and (v) maintain a balance of high quality diversified investments to minimize risk.

Our Investment Committee, consisting of our President and Chief Executive Officer, our Chief Financial Officer, and Controller is responsible for implementing our investment policy, including approval of investment strategies and monitoring investment performance. The President and Chief Financial Officer are authorized to execute purchases or sales of securities. The board of directors regularly reviews our investment strategies and the market value of our investment portfolio.

We account for investment and mortgage-backed securities in accordance with Accounting Standards Codification (ASC) Topic 320, "Investments – Debt and Equity Securities." ASC 320 requires that investments be categorized as held-to maturity, trading, or available for sale. Our securities are generally categorized as available-for-sale based on our need to meet daily liquidity needs and to take advantage of profits that may occur from time to time. At March 31, 2018, all of our securities were classified as available for sale.

Federally chartered savings institutions have authority to invest in various types of assets, including government-sponsored enterprise obligations, securities of various federal agencies, residential mortgage-backed securities, certain certificates of deposit of insured financial institutions, overnight and short-term loans to other banks, corporate debt instruments, debt instruments of municipalities and Fannie Mae and Freddie Mac equity securities. At March 31, 2018, our investment portfolio consisted almost entirely of securities and mortgage-backed securities issued by U.S. Government agencies, municipalities or U.S. Government-sponsored enterprises. At that same date we also held \$2.0 million of corporate bonds, which equaled approximately 2.6% of our total investment securities based upon the fair value of such securities. The principal and interest on our mortgage-backed securities are guaranteed by the issuing entity.

At March 31, 2018, we owned just over \$3.1 million in Federal Home Loan Bank of Atlanta stock. As a member of Federal Home Loan Bank of Atlanta, we are required to purchase stock in the Federal Home Loan Bank of Atlanta. At March 31, 2018, we had no investments in a single company or entity (other than an agency of the U.S. Government, a municipality or a U.S. Government-sponsored enterprise) that had an aggregate book value in excess of 10% of our equity.



In fiscal 2017, our investment balances increased through the acquisition of Fraternity and the build-up of excess cash. During fiscal 2018, however, our investment balances have decreased due to either calls or maturing bonds, normal principal pay downs on our mortgage backed securities, or the sale of certain securities. The proceeds from these reductions in securities have been used to fund loan activity and loan purchases, and to a lesser extent reinvested in investment securities.

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**Amortized Cost and Estimated Fair Value of Securities.** The following table sets forth certain information regarding the amortized cost and estimated fair values of our securities as of the dates indicated.

|                                  | At March 31,<br>2018 |               | 2017              |               | 2016              |               |
|----------------------------------|----------------------|---------------|-------------------|---------------|-------------------|---------------|
|                                  | Amortized<br>Cost    | Fair<br>Value | Amortized<br>Cost | Fair<br>Value | Amortized<br>Cost | Fair<br>Value |
| <b>(In thousands)</b>            |                      |               |                   |               |                   |               |
| Mortgage-backed securities:      |                      |               |                   |               |                   |               |
| Fannie Mae                       | \$28,107             | \$27,066      | \$35,034          | \$34,473      | \$27,774          | \$27,712      |
| Ginnie Mae                       | 8,418                | 8,245         | 10,003            | 9,924         | 5,988             | 6,006         |
| Freddie Mac                      | 21,776               | 20,952        | 30,593            | 30,132        | 20,178            | 20,222        |
| Other                            | 2,778                | 2,762         | 6,365             | 6,304         | -                 | -             |
| Total mortgage-backed securities | 61,079               | 59,025        | 81,995            | 80,833        | 53,940            | 53,940        |
| U.S. Government agencies         | 2,753                | 2,719         | 3,525             | 3,512         | 10,519            | 10,533        |
| Municipal bonds                  | 12,435               | 11,706        | 17,096            | 16,168        | 4,061             | 4,112         |
| Corporate bonds                  | 2,000                | 1,954         | 2,000             | 1,916         | 2,000             | 1,899         |
| Total                            | \$78,267             | \$75,404      | \$104,616         | \$102,429     | \$70,520          | \$70,484      |

**Portfolio Maturities and Yields.** The composition and maturities of the investment securities portfolio at March 31, 2018 are summarized in the following table. Maturities are based on the final contractual payment dates, and do not reflect the impact of prepayments or early redemptions that may occur.

|                                  | At March 31, 2018   |  |   |                              |                   |                              |                   |                              |                   |                            |                              |  |
|----------------------------------|---------------------|--|---|------------------------------|-------------------|------------------------------|-------------------|------------------------------|-------------------|----------------------------|------------------------------|--|
|                                  | One Year or<br>Less | More Than<br>One Year<br>Through<br>Five Years | More Than<br>Five Years<br>Through Ten<br>Years | More Than<br>Ten Years       | Total Securities  |                              |                   |                              |                   |                            |                              |  |
|                                  | Amortized<br>Cost   | Weighted<br>Average<br>Yield                   | Amortized<br>Cost                               | Weighted<br>Average<br>Yield | Amortized<br>Cost | Weighted<br>Average<br>Yield | Amortized<br>Cost | Weighted<br>Average<br>Yield | Amortized<br>Cost | Estimated<br>Fair<br>Value | Weighted<br>Average<br>Yield |  |
| <b>(Dollars in thousands)</b>    |                     |  |   |                              |                   |                              |                   |                              |                   |                            |                              |  |
| Mortgage-backed securities:      |                     |  |   |                              |                   |                              |                   |                              |                   |                            |                              |  |
| Fannie Mae                       | \$1,354             | 3.80%  | \$2,570   | 3.15%                        | \$2,918           | 1.80%                        | \$21,265          | 2.58%                        | \$28,107          | \$27,066                   | 2.61%                        |  |
| Ginnie Mae                       | -                   | -  | 13  | 1.77                         | 26                | 4.19                         | 8,379             | 2.76                         | 8,418             | 8,245                      | 2.76                         |  |
| Freddie Mac                      | -                   | -  | 828   | 1.99                         | 4,277             | 2.20                         | 16,671            | 2.58                         | 21,776            | 20,952                     | 2.48                         |  |
| Other                            | -                   | -  | 236   | 3.99                         | -                 | -                            | 2,542             | 4.77                         | 2,778             | 2,762                      | 4.70                         |  |
| Total mortgage-backed securities | 1,354               | 3.80%  | 3,647   | 2.94%                        | 7,221             | 2.05%                        | 48,857            | 2.72%                        | 61,079            | 59,025                     | 2.68%                        |  |

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|                          |         |       |         |       |          |       |          |       |          |          |       |
|--------------------------|---------|-------|---------|-------|----------|-------|----------|-------|----------|----------|-------|
| U.S. Government agencies | 2,009   | 1.74  | 744     | 2.14  | -        | -     | -        | -     | 2,753    | 2,719    | 1.85  |
| Municipal bonds          | -       | -     | 488     | 3.54  | 1,579    | 3.33  | 10,368   | 3.45  | 12,435   | 11,706   | 3.44  |
| Corporate bonds          | -       | -     | -       | -     | 2,000    | 3.36  | -        | -     | 2,000    | 1,954    | 3.36  |
| Total                    | \$3,363 | 2.57% | \$4,879 | 2.88% | \$10,800 | 2.48% | \$59,225 | 2.85% | \$78,267 | \$75,404 | 2.79% |

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Table of Contents**Sources of Funds**

**General.** Deposits, scheduled amortization and prepayments of loan principal, maturities and calls of securities and funds provided by operations are our primary sources of funds for use in lending, investing and for other general purposes. In addition, we may also borrow from the Federal Home Loan Bank of Atlanta (FHLB), as we did in fiscal 2018, to fund our loan growth both organically and through loan purchases. In fiscal 2016 and 2017 we acquired \$10.5 million and \$15.0 million of FHLB advances in the acquisitions of Fairmount and Fraternity of which \$7.5 million and \$5.0 million has matured or rolled over, respectively. As of March 31, 2018, there were \$60.6 million in advances outstanding from the FHLB.

**Deposits.** We offer deposit products having a range of interest rates and terms. We currently offer statement savings accounts, interest and noninterest-bearing demand accounts, health savings accounts (HSA), money market accounts and certificates of deposit. We also offer the Certificate of Deposit Account Registry Service (CDARS) program to our customers. Our strategic plan includes a greater emphasis on developing commercial business activities, centered around both deposit and lending customer relationships.

Deposit flows are significantly influenced by general and local economic conditions, changes in prevailing interest rates, internal pricing decisions and competition. Our deposits are primarily obtained from areas surrounding our branch offices. In order to attract and retain deposits we rely on paying competitive interest rates and providing quality service.

Based on experience, we believe that our deposits are relatively stable. However, the ability to attract and maintain deposits and the rates paid on these deposits, has been and will continue to be significantly affected by market conditions. At March 31, 2018, \$247.0 million, or 61.0% of our total deposit accounts were certificates of deposit, of which \$125.1 million had maturities of one year or less.

The following tables set forth the distribution of our average deposit accounts, by account type, for the years indicated. Our focus has been on growing our lower costing core deposits (considered all deposits other certificates of deposit) and relying less on originating certificates of deposit.

| <b>For the Years Ended March 31,</b> |                |                 |                |                |                 |                |                 |
|--------------------------------------|----------------|-----------------|----------------|----------------|-----------------|----------------|-----------------|
| <b>2018</b>                          |                | <b>2017</b>     |                | <b>2016</b>    |                 |                |                 |
| <b>Average</b>                       | <b>Percent</b> | <b>Weighted</b> | <b>Average</b> | <b>Percent</b> | <b>Weighted</b> | <b>Percent</b> | <b>Weighted</b> |
| <b>Balance</b>                       |                | <b>Average</b>  | <b>Balance</b> |                | <b>Average</b>  | <b>Balance</b> | <b>Average</b>  |

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| Deposit type:              | Rate                   |       |   |      | Rate |           |       |   | Rate |   |           |       |   |      |   |
|----------------------------|------------------------|-------|---|------|------|-----------|-------|---|------|---|-----------|-------|---|------|---|
|                            | (Dollars in thousands) |       |   |      |      |           |       |   |      |   |           |       |   |      |   |
| Certificates of deposit    | \$242,949              | 60.3  | % | 1.01 | %    | \$259,721 | 63.8  | % | 0.89 | % | \$172,064 | 64.9  | % | 0.96 | % |
| Money market               | 60,589                 | 15.1  |   | 0.53 |      | 61,568    | 15.1  |   | 0.37 |   | 35,124    | 13.3  |   | 0.17 |   |
| Statement savings          | 43,408                 | 10.8  |   | 0.12 |      | 43,527    | 10.7  |   | 0.15 |   | 25,843    | 9.8   |   | 0.10 |   |
| Noninterest bearing demand | 29,306                 | 7.3   |   | -    |      | 24,078    | 5.9   |   | -    |   | 19,282    | 7.3   |   | -    |   |
| NOW accounts               | 26,094                 | 6.5   |   | 0.03 |      | 18,333    | 4.5   |   | 0.03 |   | 12,447    | 4.7   |   | 0.03 |   |
| Total deposits             | \$402,346              | 100.0 | % | 0.70 | %    | \$407,227 | 100.0 | % | 0.64 | % | \$264,760 | 100.0 | % | 0.66 | % |

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The following table sets forth certificates of deposit classified by interest rate as of the dates indicated.

|                 | <b>At March 31,</b>   |                  |                  |
|-----------------|-----------------------|------------------|------------------|
|                 | <b>2018</b>           | <b>2017</b>      | <b>2016</b>      |
|                 | <b>(In thousands)</b> |                  |                  |
| Interest Rate:  |                       |                  |                  |
| Less than 2.00% | \$231,253             | \$241,121        | \$181,572        |
| 2.00% to 2.99%  | 15,736                | 6,512            | 13,459           |
| 3.00% to 3.99%  | -                     | -                | -                |
| 4.00% to 4.99%  | -                     | -                | -                |
| 5.00% and above | -                     | -                | -                |
| <b>Total</b>    | <b>\$246,989</b>      | <b>\$247,633</b> | <b>\$195,031</b> |

**Maturities of Certificates of Deposit Accounts.** The following table sets forth the amount and maturities of certificates of deposit accounts at the dates indicated.

|                             | <b>At March 31, 2018</b>      |                   |                     |                    |                  |                |          |
|-----------------------------|-------------------------------|-------------------|---------------------|--------------------|------------------|----------------|----------|
|                             | <b>Period to Maturity</b>     |                   |                     |                    |                  |                |          |
|                             | <b>Less Than</b>              | <b>More Than</b>  | <b>More Than</b>    | <b>More Than</b>   |                  | <b>Percent</b> |          |
|                             | <b>or Equal to</b>            | <b>One to Two</b> | <b>Two to Three</b> | <b>Three Years</b> | <b>Total</b>     | <b>of</b>      |          |
|                             | <b>One Year</b>               | <b>Years</b>      | <b>Years</b>        |                    |                  | <b>Total</b>   |          |
|                             | <b>(Dollars in thousands)</b> |                   |                     |                    |                  |                |          |
| <b>Interest Rate Range:</b> |                               |                   |                     |                    |                  |                |          |
| Less than 2.00%             | \$123,043                     | \$59,427          | \$24,327            | \$24,456           | \$231,253        | 93.6           | %        |
| 2.00% to 2.99%              | 2,032                         | 4,803             | 2,133               | 6,768              | 15,736           | 6.4            |          |
| 3.00% to 3.99%              | -                             | -                 | -                   | -                  | -                | -              |          |
| 4.00% to 4.99%              | -                             | -                 | -                   | -                  | -                | -              |          |
| 5.00% to 5.99%              | -                             | -                 | -                   | -                  | -                | -              |          |
| <b>Total</b>                | <b>\$125,075</b>              | <b>\$64,230</b>   | <b>\$26,460</b>     | <b>\$31,224</b>    | <b>\$246,989</b> | <b>100.0</b>   | <b>%</b> |

As of March 31, 2018, the aggregate amount of outstanding certificates of deposit at Hamilton Bank in amounts greater than or equal to \$100,000 was approximately \$113.5 million. The following table presents the maturity of these certificates of deposit at such date.

| <b>Period to Maturity</b>        | <b>At March<br/>31, 2018<br/>(In<br/>thousands)</b> |
|----------------------------------|---|
| Three months or less             | \$ 14,020   |
| Over three through six months    | 13,472  |
| Over six months through one year | 27,261  |
| Over one year to three years     | 41,612  |
| Over three years                 | 17,108  |
| Total                            | \$ 113,473  |

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**Borrowed Funds.** As a member of the FHLB, Hamilton Bank is eligible to obtain advances upon the security of the Federal Home Loan Bank common stock owned and certain loan products, provided certain standards related to credit-worthiness have been met. Federal Home Loan Bank advances are available pursuant to several credit programs, each of which has its own interest rate and range of maturities. At March 31, 2018, based on available collateral, we had the ability to borrow approximately \$68.3 million from the Federal Home Loan Bank of Atlanta. Beginning in the second half of fiscal 2015, we began to increase our borrowings from the FHLB as a means to fund our loan growth both organically and through loan purchases. Additionally, in fiscal 2016 and 2017 we acquired \$10.5 million and \$15.0 million of FHLB advances in the acquisitions of Fairmount and Fraternity of which \$7.5 million and \$5.0 million has matured or rolled over, respectively. As of March 31, 2018, there were \$60.6 million in advances outstanding from the FHLB as presented in the table below.

|                                  | March 31, 2018 |          |               | March 31, 2017 |          |               |
|----------------------------------|----------------|----------|---------------|----------------|----------|---------------|
|                                  | Amount         | Rate     | Maturity Date | Amount         | Rate     | Maturity Date |
| FHLB advance                     | 5,550,000      | 1.84%    | 6/11/2018     | 5,550,000      | 0.94%    | 6/9/2017      |
| FHLB advance                     | 6,000,000      | 1.90%    | 6/29/2018     | 6,000,000      | 0.93%    | 6/29/2017     |
| FHLB advance                     | 1,000,000      | * 2.60%  | 7/2/2018      | 1,000,000      | * 4.24%  | 7/31/2017     |
| FHLB advance                     | 1,000,000      | * 3.05%  | 7/3/2018      | 5,000,000      | ** 4.28% | 7/31/2017     |
| FHLB advance                     | 5,000,000      | ** 3.94% | 7/23/2018     | 1,000,000      | * 4.01%  | 8/21/2017     |
| FHLB advance                     | 1,000,000      | 1.74%    | 7/31/2018     | 1,000,000      | * 0.91%  | 8/31/2017     |
| FHLB advance                     | 1,000,000      | 1.40%    | 8/21/2018     | 1,500,000      | * 3.23%  | 11/24/2017    |
| FHLB advance                     | 4,000,000      | 1.94%    | 8/27/2018     | 1,500,000      | * 3.40%  | 11/27/2017    |
| FHLB advance                     | 3,000,000      | 1.41%    | 8/27/2018     | 1,000,000      | * 2.60%  | 7/2/2018      |
| FHLB advance                     | 5,000,000      | ** 3.38% | 9/19/2018     | 1,000,000      | * 3.05%  | 7/3/2018      |
| FHLB advance                     | 1,000,000      | * 2.60%  | 10/2/2018     | 5,000,000      | ** 3.94% | 7/23/2018     |
| FHLB advance                     | 1,000,000      | 1.95%    | 12/31/2018    | 5,000,000      | ** 3.38% | 9/19/2018     |
| FHLB advance                     | 3,000,000      | 1.38%    | 7/31/2019     | 1,000,000      | * 2.60%  | 10/2/2018     |
| FHLB advance                     | 3,000,000      | 1.96%    | 8/26/2019     | -              |          |               |
| FHLB advance                     | 3,000,000      | 1.59%    | 8/26/2019     | -              |          |               |
| FHLB advance                     | 3,000,000      | 1.42%    | 8/26/2019     | -              |          |               |
| FHLB advance                     | 1,500,000      | 1.95%    | 11/25/2019    | -              |          |               |
| FHLB advance                     | 1,500,000      | 1.78%    | 11/27/2019    | -              |          |               |
| FHLB advance                     | 3,000,000      | 2.31%    | 2/3/2020      | -              |          |               |
| FHLB advance                     | 1,000,000      | 2.15%    | 11/30/2020    | -              |          |               |
| FHLB advance                     | 2,000,000      | 2.28%    | 12/28/2020    | -              |          |               |
| FHLB advance                     | 2,000,000      | 2.49%    | 2/1/2021      | -              |          |               |
| FHLB advance                     | 3,000,000      | 1.48%    | 8/25/2021     | -              |          |               |
|                                  | 60,550,000     |          |               | 35,550,000     |          |               |
| Premium on FHLB advances assumed | 122,140        |          |               | 547,650        |          |               |
| Total FHLB advances              | \$60,672,140   |          |               | \$36,097,650   |          |               |

\* Advances assumed in the Fairmount Bancorp acquisition

\*\* Advances assumed in the Fraternity Community Bancorp acquisition



Hamilton Bank may also borrow up to \$5.0 million from a correspondent bank under a secured federal funds line of credit, and \$1.0 million under an unsecured line of credit. We would be required to pledge investment securities to draw upon the secured line of credit. During fiscal 2018, there was nothing drawn upon under either line of credit.

## **Employees**

As of March 31, 2018, we had 72 full-time equivalent employees. Our employees are not represented by any collective bargaining group. Management believes that we have a good working relationship with our employees.

## **Subsidiary Activities**

Hamilton Bancorp has one direct subsidiary, Hamilton Bank. At March 31, 2018, Hamilton Bank has five wholly owned subsidiaries including 3110 FC, LLC, a Maryland limited liability company that was formed to hold other real estate owned acquired through foreclosure or deed-in-lieu of foreclosure. On May 13, 2016, in connection with the acquisition of Fraternity Community Bancorp, the Bank acquired four additional subsidiaries: 4819 Palmer Avenue LLC, a limited liability company organized under the laws of the State of Maryland ("4819 Palmer"); 764 Washington Boulevard LLC, a limited liability company organized under the laws of the State of Maryland ("764 WB LLC"); 764 Washington Boulevard II LLC, a limited liability company organized under the laws of the State of Maryland ("764 WB LLC II"); and Fraternity Insurance Agency, Inc., an inactive corporation organized under the laws of the State of Maryland. 4819 Palmer, 764 WB LLC and 764 WB LLC II were each formed by Fraternity Federal Savings & Loan Association to hold other real estate owned.

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**REGULATION AND SUPERVISION**

**General**

In December 2017, the Bank converted its charter from a federal savings bank to a Maryland chartered commercial bank. As a Maryland-chartered commercial bank, Hamilton Bank is subject to the regulation, supervision, and control of the Maryland Office of the Commissioner of Financial Regulation (“MOCFR”). Hamilton Bank is subject to regulation, supervision and control of the FDIC, an agency of the federal government. The federal and state system of regulation and supervision establishes a comprehensive framework of activities in which Hamilton Bank may engage and is intended primarily for the protection of depositors and the FDIC’s Deposit Insurance Fund, and not for the protection of stockholders. Under this system of federal regulation, financial institutions are periodically examined to ensure that they satisfy applicable standards with respect to matters such as their capital adequacy, assets, management, earnings, liquidity and sensitivity to market interest rates. Hamilton Bank is also regulated to a lesser extent by the Board of Governors of the Federal Reserve System (the “Federal Reserve Board”), which governs the reserves to be maintained against deposits and other matters. Hamilton Bank must comply with the consumer protection regulations issued by the Consumer Financial Protections Bureau. Hamilton Bank also is a member of and owns stock in the Federal Home Loan Bank of Atlanta, which is one of the twelve regional banks in the Federal Home Loan Bank System. The MOCFR and the FDIC examine Hamilton Bank and prepare reports for the consideration of its board of directors on any operating deficiencies. Hamilton Bank’s relationship with its depositors and borrowers is also regulated by federal and state law, especially in matters concerning the ownership of deposit accounts, the form and content of Hamilton Bank’s loan documents and certain consumer protection matters.

As a bank holding company, Hamilton Bancorp is subject to examination and supervision by, and is required to file certain reports with, the Federal Reserve Board. Hamilton Bancorp is also subject to the rules and regulations of the Securities and Exchange Commission under the federal securities laws.

Set forth below are certain material regulatory requirements that are applicable to Hamilton Bank and Hamilton Bancorp. This description of statutes and regulations is not intended to be a complete description of such statutes and regulations and their effects on Hamilton Bank and Hamilton Bancorp. Any change in these laws or regulations, whether by Congress or the applicable regulatory agencies, could have a material adverse impact on Hamilton Bancorp, Hamilton Bank and their operations.

**Banking Regulation**

**General.** The Bank is a Maryland commercial bank and its deposit accounts are insured by the Deposit Insurance Fund of the FDIC. The Bank is subject to supervision, examination and regulation by the MOCFR and the FDIC.

The Dodd-Frank Act established the Consumer Financial Protection Bureau (“CFPB”) as an independent bureau of the Federal Reserve System. The CFPB assumed responsibility for implementing federal consumer financial protection and fair lending laws and regulations, a function formerly handled by federal bank regulatory agencies. However, institutions of less than \$10 billion, such as the Bank, continue to be examined for compliance with consumer protection or fair lending laws and regulations by, and be subject to enforcement authority of their primary federal regulators.

**Capital Requirements.** Under the FDIC’s regulations, federally insured state-chartered banks that are not members of the Federal Reserve System (“state non-member banks”), such as Hamilton Bank, are required to comply with minimum leverage capital requirements. Federal regulations require federally insured depository institutions to meet several minimum capital standards: a common equity Tier 1 capital to risk-based assets ratio of 4.5%, a Tier 1 capital to risk-based assets ratio of 6.0%, a total capital to risk-based assets of 8%, and a Tier 1 capital to total assets leverage ratio of 4%. In addition to establishing the minimum regulatory capital requirements, the regulations limit capital distributions and certain discretionary bonus payments to management if the institution does not hold a “capital conservation buffer” consisting of 2.5% of common equity Tier 1 capital to risk-weighted assets above the amount necessary to meet its minimum risk-based capital requirements. The capital conservation buffer requirement is being phased in. It is currently at 1.875%, and will be fully phased in at 2.5% on January 1, 2019.

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In determining the amount of risk-weighted assets for purposes of calculating risk-based capital ratios, all assets, including certain off-balance sheet assets (e.g., recourse obligations, direct credit substitutes, residual interests) are multiplied by a risk weight factor assigned by the regulations based on the risks believed inherent in the type of asset. Higher levels of capital are required for asset categories believed to present greater risk. In assessing an institution's capital adequacy, the FDIC takes into consideration, not only these numeric factors, but qualitative factors as well, and has the authority to establish higher capital requirements for individual institutions if it deems necessary.

Legislation enacted in May 2018 requires the federal banking agencies, including the FDIC, to establish for banks with assets of less than \$10 billion of assets a "community bank leverage ratio" of 8 to 10%. Banks with capital meeting the specified requirement will be considered to meet the applicable regulatory capital requirements including the risk-based requirements. The establishment of the community bank leverage ratio is subject to notice and comment rulemaking by the federal regulators.

**Prompt Corrective Regulatory Action.** Federal law establishes a system of prompt corrective action to resolve the problems of undercapitalized institutions. The FDIC has adopted regulations to implement the prompt corrective action legislation. An institution is deemed to be "well capitalized" if it has a total risk-based capital ratio of 10.0% or greater, a Tier 1 risk-based capital ratio of 8.0% or greater, a leverage ratio of 5.0% or greater and a common equity Tier 1 ratio of 6.5% or greater. An institution is "adequately capitalized" if it has a total risk-based capital ratio of 8.0% or greater, a Tier 1 risk-based capital ratio of 6.0% or greater, a leverage ratio of 4.0% or greater and a common equity Tier 1 ratio of 4.5% or greater. An institution is "undercapitalized" if it has a total risk-based capital ratio of less than 8.0%, a Tier 1 risk-based capital ratio of less than 6.0%, a leverage ratio of less than 4.0% or a common equity Tier 1 ratio of less than 4.5%. An institution is deemed to be "significantly undercapitalized" if it has a total risk-based capital ratio of less than 6.0%, a Tier 1 risk-based capital ratio of less than 4.0%, a leverage ratio of less than 3.0% or a common equity Tier 1 ratio of less than 3.0%. An institution is considered to be "critically undercapitalized" if it has a ratio of tangible equity (as defined in the regulations) to total assets that is equal to or less than 2.0%.

"Undercapitalized" banks must adhere to growth, capital distribution (including dividend) and other limitations and are required to submit a capital restoration plan. A bank's compliance with such a plan must be guaranteed by any company that controls the undercapitalized institution in an amount equal to the lesser of 5% of the institution's total assets when deemed undercapitalized or the amount necessary to achieve the status of adequately capitalized. If an "undercapitalized" bank fails to submit an acceptable plan, it is treated as if it is "significantly undercapitalized." "Significantly undercapitalized" banks must comply with one or more of a number of additional measures, including, but not limited to, a required sale of sufficient voting stock to become adequately capitalized, a requirement to reduce total assets, cessation of taking deposits from correspondent banks, the dismissal of directors or officers and restrictions on interest rates paid on deposits, compensation of executive officers and capital distributions by the parent holding company. "Critically undercapitalized" institutions are subject to additional measures including, subject to a narrow exception, the appointment of a receiver or conservator within 270 days after it obtains such status.

At March 31, 2018, Hamilton Bank's capital exceeded all applicable regulatory requirements.

**Loans to One Borrower.** Under Maryland law, the maximum amount that the Bank is generally permitted to lend to any one borrower and his or her related interests may generally not exceed 10% of the Bank's unimpaired capital and surplus, which is defined to include the Bank's capital, surplus, retained earnings and 50% of its reserve for possible loan losses. By interpretive ruling of the Maryland Commissioner, Maryland banks have the option of lending up to the amount that would be permissible for a national bank, which is generally 15% of unimpaired capital and surplus (defined to include a bank's total capital for regulatory capital purposes plus any loan loss allowances not included in regulatory capital). Under this formula, the Bank would have been permitted to lend up to \$6.3 million to any one borrower at March 31, 2018. As of March 31, 2018, Hamilton Bank was in compliance with the loans to one borrower limitations.

**Branching.** Maryland law provides that, with the approval of the Commissioner, Maryland banks may establish branches within Maryland and may establish branches in other states by any means permitted by the laws of such state or by federal law. Federal law permits well capitalized and well managed bank holding companies to acquire banks in any state, subject to Federal Reserve Board approval, certain concentration limits and other specified conditions. Interstate mergers of banks are also authorized, subject to regulatory approval and other specified conditions. In addition, banks are permitted to establish de novo branches on an interstate basis to the extent that branching is authorized by the law of the host state for the banks chartered by that state.

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**Insurance of Deposit Accounts.** The Bank's deposits are insured up to applicable limits by the Deposit Insurance Fund of the FDIC. The deposit insurance per account owner is currently \$250,000.

The FDIC charges insured depository institutions premiums to maintain the Deposit Insurance Fund. Assessments for most institutions are based on financial measures and supervisory ratings derived from statistical modeling estimating the probability of failure within three years. The assessment range (inclusive of possible adjustments) for most banks and savings associations is 1.5 basis points to 30 basis points of total assets less tangible equity.

In addition to the FDIC assessments, the Financing Corporation ("FICO") is authorized to impose and collect, with the approval of the FDIC, assessments for anticipated payments, issuance costs and custodial fees on bonds issued by the FICO in the 1980s to recapitalize the former Federal Savings and Loan Insurance Corporation. The bonds issued by the FICO are due to mature in by 2019. For the third calendar quarter of fiscal 2018, the annualized FICO assessment will be equal to 0.32 of a basis point of total assets less tangible capital.

Insurance of deposits may be terminated by the FDIC upon a finding that an institution has engaged in unsafe or unsound practices, is in an unsafe or unsound condition to continue operations or has violated any applicable law, regulation, rule, order or condition imposed by the FDIC. We do not currently know of any practice, condition or violation that may lead to termination of our deposit insurance.

**Dividends.** Maryland banks may only pay cash dividends from undivided profits or, with the prior approval of the Commissioner, their surplus in excess of 100% of required capital stock. Federal law provides that an insured depository institution may not make any dividend, including paying a dividend, if after paying such dividend, the institution would fail to satisfy any applicable regulatory capital requirement. In addition, Hamilton Bank's ability to pay dividends is limited if Hamilton Bank does not have the capital conservation buffer required by the new capital rules, which may limit the ability of Hamilton Bancorp to pay dividends to its stockholders. See — "Capital Requirements".

**Transactions with Related Parties.** A state nonmember bank, such as the Bank, is limited in the amount of "covered transactions" with any affiliate, including Hamilton Bancorp. Covered transactions must be on terms substantially the same, or at least as favorable, to the Bank as those provided to a non-affiliate. The term "covered transaction" includes the making of loans, purchase of assets, issuance of a guarantee and similar types of transactions. Certain covered transactions, such as loans to affiliates, must meet specified collateral requirements.

Loans to directors, executive officers and principal stockholders of a state nonmember bank must be made on substantially the same terms as those prevailing for comparable transactions with persons who are not executive officers, directors, principal stockholders or employees of the bank. Loans to any executive officer, director and

principal stockholder are subject to additional restriction, including certain board of director's approval requirements and specified limits.

**Enforcement.** The Commissioner has extensive enforcement authority over Maryland banks. This includes the ability to issue cease and desist orders and civil money penalties and to remove directors or officers. The Commissioner may also take possession of a Maryland bank whose capital is impaired and seek to have a receiver appointed by a court.

The FDIC has primary federal enforcement responsibility over state banks under its jurisdiction, including the authority to bring enforcement action against all "institution-related parties," including stockholders, and any attorneys, appraisers and accountants who knowingly or recklessly participate in wrongful action likely to have an adverse effect on an institution. Formal enforcement action may range from the issuance of capital directive or a cease and desist order for the removal of officers and/or directors, receivership, conservatorship or termination of deposit insurance. Civil money penalties cover a wide range of violations and actions, and range up to \$25,000 per day or even up to \$1 million per day (in the most egregious cases). Criminal penalties for most financial institution crimes include fines of up to \$1 million and imprisonment for up to 30 years.

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**Community Reinvestment Act.** Under the Community Reinvestment Act (“CRA”), a bank has a continuing and affirmative obligation, consistent with its safe and sound operation, to help meet the credit needs of its entire community, including low and moderate-income neighborhoods. The CRA requires the FDIC to provide a written evaluation of an institution’s CRA performance utilizing a four-tiered descriptive rating system. Since converting our charter, the FDIC has not conducted a CRA examination. Our latest CRA examination, dated April 2015, was performed by the Office of the Comptroller of the Currency (“OCC”) and was rated “Satisfactory.”

**Federal Home Loan Bank System.** Hamilton Bank is a member of the Federal Home Loan Bank System, which consists of 12 regional Federal Home Loan Banks. The Federal Home Loan Bank System provides a central credit facility primarily for member institutions as well as other entities involved in home mortgage lending. As a member of the Federal Home Loan Bank of Atlanta, Hamilton Bank is required to acquire and hold shares of capital stock in the Federal Home Loan Bank. As of March 31, 2018, Hamilton Bank was in compliance with this requirement.

## **Other Regulations**

Interest and other charges collected or contracted for by Hamilton Bank are subject to state usury laws and federal laws concerning interest rates. Hamilton Bank’s operations are also subject to federal laws applicable to credit transactions. In addition, the Consumer Financial Protection Bureau issues regulations and standards under federal consumer protection laws that affect consumer businesses. These include regulations setting “ability to repay” and “qualified mortgage” standards for residential mortgage loans and mortgage loan servicing and originator compensation standards. Hamilton Bank is evaluating recent regulations and proposals, and devotes significant compliance, legal and operational resources to compliance with consumer protection regulations and standards.

## **Holding Company Regulation**

**General.** As a bank holding company, Hamilton Bancorp is subject to comprehensive regulation, examination and supervision by the Federal Reserve Board under the Bank Holding Company Act of 1956, as amended (the “BHCA”), and the regulations of the Federal Reserve Board. The Federal Reserve Board also has extensive enforcement authority over bank holding companies, including, among other things, the ability to assess civil money penalties, to issue cease and desist or removal orders, and to require that a holding company divest subsidiaries (including its bank subsidiaries). In general, enforcement actions may be initiated for violations of law and regulations and unsafe or unsound practices.

**Permissible Activities.** A bank holding company is limited in its activities to banking, managing or controlling banks, or providing services for its subsidiaries. Other permitted non-bank activities have been identified as closely related to banking. Bank holding companies that are “well capitalized” and “well managed” and whose financial institution



subsidiaries have satisfactory Community Reinvestment Act records can elect to become “financial holding companies,” which are permitted to engage in a broader range of financial activities than are permitted to bank holding companies. Hamilton Bancorp has not opted to become a financial holding company.

The Federal Reserve Board has the power to order a holding company or its subsidiaries to terminate any activity, or to terminate its ownership or control of any subsidiary, when it has reasonable cause to believe that the continuation of such activity or such ownership or control constitutes a serious risk to the financial safety, soundness or stability of any bank subsidiary of that holding company.

**Capital.** Bank holding companies are generally required to maintain on a consolidated basis, specified minimum ratios of capital to total assets and capital to risk-weighted assets. However, these requirements generally apply to bank holding companies with consolidated assets of \$1 billion or more, and do not apply to Hamilton Bancorp. Recent legislation has increased to \$3 billion of assets the threshold for the applicability of consolidated holding company capital requirements, subject the promulgation of regulations by the Federal Reserve board.

**Source of Strength.** The Dodd-Frank Act extended the “source of strength” doctrine to bank holding companies. The Federal Reserve Board has issued regulations requiring that all bank holding companies serve as a source of managerial and financial strength to their subsidiary bank by providing capital, liquidity and other support in times of financial stress.

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**Dividends.** The Federal Reserve Board has issued a policy statement regarding the payment of dividends and the repurchase of shares of common stock by bank holding companies. In general, the policy provides that dividends should be paid only out of current earnings and only if the prospective rate of earnings retention by the holding company appears consistent with the organization's capital needs, asset quality and overall financial condition. Regulatory guidance provides for prior regulatory consultation with respect to capital distributions in certain circumstances such as where the company's net income for the past four quarters, net of dividends previously paid over that period, is insufficient to fully fund the dividend or the company's overall rate of earnings retention is inconsistent with the company's capital needs and overall financial condition. The ability of a bank holding company to pay dividends may be restricted if a subsidiary bank becomes undercapitalized. The policy statement also states that a bank holding company should inform the Federal Reserve Board supervisory staff prior to redeeming or repurchasing common stock or perpetual preferred stock if the bank holding company is experiencing financial weaknesses or if the repurchase or redemption would result in a net reduction, as of the end of a quarter, in the amount of such equity instruments outstanding compared with the beginning of the quarter in which the redemption or repurchase occurred. These regulatory policies may affect the ability of Hamilton Bancorp to pay dividends, repurchase shares of common stock or otherwise engage in capital distributions.

**Acquisition.** Under the Federal Change in Bank Control Act, a notice must be submitted to the Federal Reserve Board if any person (including a company), or group acting in concert, seeks to acquire direct or indirect "control" of a bank holding company. Under certain circumstances, a change of control may occur, and prior notice is required, upon the acquisition of 10% or more of the company's outstanding voting stock, unless the Federal Reserve Board has found that the acquisition will not result in control of the company. A change in control definitively occurs upon the acquisition of 25% or more of the company's outstanding voting stock. Under the Change in Bank Control Act, the Federal Reserve Board generally has 60 days from the filing of a complete notice to act, taking into consideration certain factors, including the financial and managerial resources of the acquirer and the competitive effects of the acquisition.

**Federal Securities Laws**

Hamilton Bancorp's common stock is registered with the Securities and Exchange Commission under the Securities Exchange Act of 1934, as amended. Hamilton Bancorp is subject to the information, proxy solicitation, insider trading restrictions and other requirements under the Securities Exchange Act of 1934.

**ITEM 1A. RISK FACTORS**

**Our commercial real estate loans increase our credit risk.**

Beginning in 2009, we changed our business strategy with respect to organic growth to become less reliant upon one-to-four family lending and emphasize commercial lending; in particularly commercial real estate lending. To support this strategy, we hired additional commercial lenders, as well as enhanced our back-office monitoring and loan administration with additional personnel. We have also participated in commercial real estate loans originated by other institutions in the past. At March 31, 2018, commercial real estate loans totaled \$112.2 million, or 28.8% of total loans. This increase includes a combined \$16.0 million of commercial real estate loans acquired in our acquisition of Fairmount Bancorp, Inc. in September 2015 and Fraternity Community Bancorp, Inc. in May 2016.

Commercial real estate loans generally have more risk than the one-to-four family residential real estate loans that we originate. Because the repayment of commercial real estate loans depends on the successful management and operation of the borrower's properties or businesses, repayment of such loans can be affected by adverse conditions in the local real estate market or economy. Commercial real estate loans may also involve relatively large loan balances to individual borrowers or groups of related borrowers. In addition, a downturn in the real estate market or the local economy could adversely affect the value of properties securing the loan or the revenues from the borrower's business, thereby increasing the risk of nonperforming loans.

Given our increase in commercial real estate lending, and that a significant portion of our portfolio in commercial real estate loans is not seasoned, we have a limited loss history with which to measure the level of risk in our commercial real estate loan portfolio. Delinquencies and loan losses related to our commercial real estate loans could increase more than we have provided for in our allowance for loan losses as we continue to emphasize this type of lending activity.

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**A portion of our one-to-four family residential mortgage loans is comprised of non-owner occupied (investor) properties, which increases the credit risk on this portion of our loan portfolio.**

A portion of our loan portfolio is comprised of loans secured by non-owner occupied one-to-four family properties, which we refer to as “investor loans”. At March 31, 2018, \$26.7 million of our one-to-four family residential mortgage loans in our portfolio, or 6.9% of total loans, were comprised of investor loans. We acquired approximately \$9.2 million of investor loans in connection with our acquisition of Fraternity Community Bancorp, Inc. in May 2016 and another \$17.1 million with respect to our acquisition of Fairmount Bancorp, Inc. in September 2015. There is a greater credit risk inherent in non-owner-occupied properties, than in owner-occupied since the repayment of these loans may depend, in part, on the successful management of the property and/or the borrower’s ability to lease the unit or units of the property. A downturn in the real estate market or the local economy could adversely affect the value of properties securing these loans or the revenues derived from these properties, which could affect the borrower’s ability to repay the loan.

In addition, we have limited experience with the performance of the investor loans acquired in connection with the acquisition of Fraternity Community Bancorp, Inc. and Fairmount Bancorp, Inc. See — “We have relatively limited experience with the performance of loans acquired in our recent acquisitions of Fraternity Community Bancorp, Inc. and Fairmount Bancorp, Inc. Certain of our estimates related to accounting for acquired loans may differ from actual results” below regarding risks associated with our recent acquisition of these and other loans.

**We have relatively limited experience with the performance of loans acquired in our acquisitions of Fraternity Community Bancorp, Inc. and Fairmount Bancorp, Inc., and our purchase of several pools of loans acquired in March 2017 and throughout fiscal 2018. Certain of our estimates related to accounting for acquired loans may differ from actual results.**

We acquired Fraternity Community Bancorp, Inc. in May 2016, and Fairmount Bancorp, Inc. in September 2015. In addition, in March 2017 we purchased \$23.4 million of one-to-four family jumbo residential mortgage loans in two separate pools. In fiscal 2018 we continued to purchase various pools of loans, including \$15.5 million in commercial lease loans, \$19.9 million in recreational vehicles (“RVs”), and \$19.2 million in residential mortgage loans. It is difficult to assess the future performance of loans recently added to our portfolio as part of these acquisitions and/or purchases because our relatively limited experience with such loans does not provide us with a significant history from which to judge future collectability.

These loans may experience higher delinquency or charge-off levels than our historical loan portfolio experience, which could adversely affect our future performance.

If the estimates we have made regarding the performance of loans we have acquired or purchased are inadequate, the fair value estimates may exceed the actual collectability of the balances, and this may result in the related loans being considered by us as impaired, which would result in a reduction in interest income. The tangible book value we measure is based in part on these estimates, and if fair value estimates differ from actual collectability, then subsequent earnings may also differ from original estimates. Measures of tangible book value and earnings impact of business combinations are frequently used in evaluating the merits and value of business combinations. Numerous assumptions and estimates are integral to purchased loan accounting, and actual results could be different from prior estimates.

**If our allowance for loan losses is not sufficient to cover actual loan losses, our earnings could decrease.**

We make various assumptions and judgments about the collectability of our loan portfolio, including the creditworthiness of our borrowers and the value of the real estate and other assets serving as collateral for the repayment of many of our loans. In determining the amount of the allowance for loan losses, we review our loans and our loss and delinquency experience, and we evaluate economic conditions. If our assumptions are incorrect, our allowance for loan losses may not be sufficient to cover probable incurred losses in our loan portfolio, resulting in additions to our allowance for loan losses. Additions to the allowance for loan losses are established through the provision for losses on loans which is charged against income.

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The unseasoned nature of a significant portion of our commercial real estate loans and commercial business loans, along with various purchases of loan pools, increases the risk that our allowance may be insufficient to absorb losses without significant additional provisions.

In addition, if the loans we have acquired in our recent acquisitions of Fraternity Community Bancorp, Inc. and Fairmount Bancorp, Inc. do not perform as we have estimated, our allowance for loan losses may not be adequate. See — “We have relatively limited experience with the performance of loans acquired in our recent acquisitions of Fraternity Community Bancorp, Inc. and Fairmount Bancorp, Inc., and our purchase of several pools of loans acquired in March 2017 and throughout fiscal 2018. Certain of our estimates related to accounting for acquired loans may differ from actual results,” above.

Significant increases to our allowance materially decrease our net income. In addition, bank regulators periodically review our allowance for loan losses and may require us to increase our provision for loan losses or recognize further loan charge-offs. Any increase in our allowance for loan losses or loan charge-offs as required by these regulatory authorities might have a material adverse effect on our financial condition and results of operations.

The Financial Accounting Standards Board has adopted a new accounting standard that will become effective for us on April 1, 2020. This standard, referred to as Current Expected Credit Loss, or CECL, will require financial institutions to determine periodic estimates of lifetime expected credit losses on loans, and recognize the expected credit losses as allowances for loan losses. This will change the current method of providing allowances for loan losses that are probable, which would likely require us to increase our allowance for loan losses, and to greatly increase the types of data we would need to collect and review to determine the appropriate level of the allowance for loan losses.

**We have a significant number of loans secured by real estate, and a downturn in the local real estate market could negatively impact our profitability.**

At March 31, 2018, approximately \$309.5 million, or 79.5%, of our total loan portfolio was secured by residential or commercial real estate, almost all of which is located in our primary lending market. Future declines in the real estate values in lending markets could significantly impair the value of the particular collateral securing our loans and our ability to sell the collateral upon foreclosure for an amount necessary to satisfy the borrower’s obligations to us. This could require increasing our allowance for loan losses to address the decrease in the value of the real estate securing our loans, which could have a material adverse effect on our business, financial condition, results of operations and growth prospects.

**Our recent acquisitions of Fairmount Bancorp, Inc. and Fraternity Community Bancorp, Inc. involve integrations and other risks.**

Acquisitions involve a number of risks and challenges including: our ability to integrate the branches and operations we acquire, and the associated internal controls and regulatory functions, into our current operations; our ability to limit the outflow of deposits held by our new customers in the acquired branches and to successfully retain and manage the loans we acquire; our ability to attract new deposits and to generate new interest-earning assets in geographic areas we have not previously served. Additionally, no assurance can be given that the operation of acquired branches would not adversely affect our existing profitability; that we would be able to achieve results in the future similar to those achieved by our existing banking business; that we would be able to compete effectively in the market areas served by acquired branches; or that we would be able to manage any growth resulting from the transaction effectively. We face the additional risk that the anticipated benefits of the acquisition may not be realized fully or at all, or within the time period expected.

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**Historically low interest rates and/or changes in interest rates may adversely affect our net interest income and profitability.**

While it has been the policy of the Federal Reserve Board to maintain interest rates at historically low levels over the past several years through its targeted federal funds rate and the purchase of mortgage-backed securities, the Federal Reserve Board raised the federal funds rate beginning in December 2015. As a general matter, our net interest income was adversely impacted by the low rate environment that existed over the past several years, however, at this point it is uncertain what impact the recent rate increases might have on our net interest income (the difference between interest income we earn on our assets and the interest expense we pay on our liabilities). It is also uncertain when the Federal Reserve Board might raise or lower the federal funds rate in the future. If interest rates continue to rise, it may negatively impact the housing markets and the U.S. economic recovery. If rates remain relatively low it could create deflationary pressures, which while possibly lowering our operating costs, could have a significant negative effect on our borrowers, especially our business borrowers, and the values of underlying collateral securing loans, which could negatively affect our financial performance.

Our profitability depends substantially on our net interest income, which is the difference between the interest income earned on our interest-earning assets and the interest expense paid on our interest-bearing liabilities. Increases in interest rates may decrease loan demand (which would also decrease our ability to generate noninterest income through the sale of loans into the secondary market and related fees for continuing to service those sold loans, particularly SBA loans sold) and make it more difficult for borrowers to repay adjustable-rate loans. In addition, as market interest rates rise, we will have competitive pressures to increase the rates we pay on deposits. Because interest rates we pay on our deposits could be expected to increase more quickly than the increase in the yields we earn on our interest-earning assets, our net interest income would be adversely affected.

We also are subject to reinvestment risk associated with changes in interest rates. Changes in interest rates may affect the average life of loans and mortgage-related securities. Decreases in interest rates can result in increased prepayments of loans and mortgage-related securities, as borrowers refinance to reduce borrowing costs. Under these circumstances, we are subject to reinvestment risk to the extent that we are unable to reinvest the cash received from such prepayments at rates that are comparable to the interest rates on existing loans and securities.

**Interest rate shifts may reduce net interest income and otherwise negatively impact our financial condition and results of operations.**

The majority of our banking assets are monetary in nature and subject to risk from changes in interest rates. Like most community banks, our earnings and cash flows depend to a great extent upon the level of our net interest income, or the difference between the interest income we earn on loans, investments and other interest-earning assets, and the interest we pay on interest-bearing liabilities, such as deposits and borrowings. Changes in interest rates can increase or decrease our net interest income, because different types of assets and liabilities may react differently, and at



different times, to market interest rate changes.

When interest-bearing liabilities mature or reprice more quickly, or to a greater degree than interest-earning assets in a period, an increase in interest rates could reduce net interest income. Similarly, when interest-earning assets mature or reprice more quickly, or to a greater degree than interest-bearing liabilities, falling interest rates could reduce net interest income. An increase in interest rates may, among other things, reduce the demand for loans and our ability to originate loans and decrease loan repayment rates. Conversely, a decrease in the general level of interest rates may affect us through, among other things, increased prepayments on our loan portfolio and increased competition for deposits. Accordingly, changes in the level of market interest rates affect our net yield on interest-earning assets, loan origination volume and our overall results. Although our asset-liability management strategy is designed to control and mitigate exposure to the risks related to changes in market interest rates, those rates are affected by many factors outside of our control, including governmental monetary policies, inflation, deflation, recession, changes in unemployment, the money supply, international disorder and instability in domestic and foreign financial markets.

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**Rising interest rates could make it more difficult for us to obtain funding at attractive rates of interest to fund our interest earning assets.**

Rising rates of interest may force us to pay higher rates of interest on deposits and/or seek other funding sources that may require us to pay higher rates of interest. At March 31, 2018, 87.0% of our funding came from deposits, of which 38.9% were “core” deposits. If interest rates continue to rise, we will need to offer higher rates of interest on our interest-bearing deposits. We have recently experienced a significant increase in competition for deposits in our market. In addition, we may experience a decrease in the amount of deposits we are able to attract, as our customers seek higher rate of return through other investments. Replacing funds due to the loss of deposits may require that we pay higher rates of interest. An increase in the rates we pay for funding will have a negative impact on our profitability.

**We could potentially recognize goodwill impairment charges.**

As of March 31, 2018, we had \$8.6 million of goodwill related to acquisitions. Goodwill is not amortized but is tested for impairment annually or more frequently if events or changes in circumstances indicate that the asset might be impaired. Impairment testing requires that the fair value of the Company be compared to the carrying amount of the Company’s net assets, including goodwill. If the fair value of the Company is less than book value, an expense may be required to write-down the related goodwill to the proper carrying value. We test for impairment of goodwill during December of each year. There could be a requirement to evaluate the recoverability of goodwill prior to or after the normal annual assessment if there is a disruption in our business, unexpected significant declines in our operating results, or sustained market capitalization declines. These types of events and the resulting analysis could result in goodwill impairment charges in the future, which would adversely affect the results of operations. As a result of impairment testing performed during December 2017 and a subsequent analysis resulting from the significant decline in operating income during the fourth quarter of fiscal 2018 due to the recording of a valuation allowance on the Company’s deferred tax assets, it was determined that the fair value of our only reporting unit exceeded the carrying value of its assets and liabilities. Therefore, goodwill was not considered impaired at March 31, 2018.

**Strong competition within our market areas may limit our growth and profitability.**

Competition in the banking and financial services industry within our market area is intense. In our market area we compete with commercial banks, savings institutions, mortgage brokerage firms, credit unions, finance companies, mutual funds, insurance companies, and brokerage and investment banking firms operating locally and elsewhere. Many of these competitors have substantially greater resources and lending limits than we have and offer certain services that we do not or cannot provide. Our profitability depends upon our continued ability to successfully compete in our market area. The greater resources and broader range of deposit and loan products offered by our competition may limit our ability to increase our interest-earning assets and profitability. We expect competition to remain intense in the future as a result of legislative, regulatory and technological changes and the continuing trend of

consolidation in the financial services industry. Technological advances, for example, have lowered barriers to entry, allowed banks to expand their geographic reach by providing services over the Internet and made it possible for non-depository institutions to offer products and services that traditionally have been provided by banks. Competition for deposits and the origination of loans could limit our ability to successfully implement our business plan, and could adversely affect our results of operations in the future.

Competition in the banking and financial services industry is coming not only from local markets but from technology oriented financial services (“FinTech”) companies, which are subject to limited regulation. They offer user friendly front-end, quick turnaround times for loans and other benefits. While Hamilton is evaluating FinTech companies with the possibility of developing relationships for efficiency in processing and/or as a source of loans and other business, we cannot limit the possibility that our customers or future prospects will work directly with a FinTech company instead. This could impact our growth and profitability going forward.

**We operate in a highly regulated environment and we may be adversely affected by changes in laws and regulations.**

We are subject to extensive regulation, supervision and examination by the Federal Reserve Board and the Federal Deposit Insurance Corporation, our primary federal regulators. Such regulation and supervision governs the activities in which an institution and its holding company may engage, and are intended primarily for the protection of the insurance fund and the depositors and borrowers of Hamilton Bank rather than for holders of our common stock. Regulatory authorities have extensive discretion in their supervisory and enforcement activities, including the imposition of restrictions on our operations, the classification of our assets and determination of the level of our allowance for loan losses. Any change in such regulation and oversight, whether in the form of regulatory policy, regulations, legislation or supervisory action, may have a material impact on our operations.

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**Income from secondary mortgage market operations is volatile, and we may incur losses or charges with respect to our secondary mortgage market operations which would negatively affect our earnings.**

We may sell in the secondary market a portion of residential mortgage loans that we originate with terms over 10 years on a servicing released basis, earning noninterest income in the form of gains on sale. When interest rates rise, the demand for mortgage loans tends to fall and may reduce the number of loans available for sale. In addition to interest rate levels, weak or deteriorating economic conditions also tend to reduce loan demand. We do sell loans in the secondary market with recourse based upon delinquency or breach of customary representations and warranties we provide to the buyers. If we breach those representations and warranties, the buyers can require us to repurchase the loans and we may incur a loss on the repurchase.

**Our recent investments in municipal debt securities expose us to additional credit risks.**

The composition and allocation of our investment portfolio has historically emphasized U.S. agency mortgage-backed securities and U.S. agency debentures. While such assets still make up the great majority of our investment portfolio at March 31, 2018, we have recently increased the amount of bank-qualified municipal obligations in our portfolio. Unlike U.S. agency securities, the municipal debt securities acquired are backed only by the credit of their issuers and not guaranteed by the federal government. These investments expose us to a greater degree of credit risk than U.S. agency securities. Any decline in the credit quality of these securities exposes us to the risk that the market value of the securities could decrease which may require us to write down their value on our books and could lead to a possible default in payment.

**Legislative and regulatory initiatives may affect our business activities and increase operating costs.**

The potential exists for additional federal or state laws and regulations regarding lending, funding practices, capital, and liquidity standards. Bank regulatory agencies are expected to be more active in responding to concerns and trends identified in examinations, including the expected issuance of many formal enforcement orders. In addition, new laws, regulations, and other regulatory changes may also increase our compliance costs and affect our business and operations. Moreover, the FDIC sets the cost of our FDIC insurance premiums, which can affect our profitability.

The Dodd-Frank Act made extensive changes in the regulation of insured depository institutions. The Dodd-Frank Act, among other things, impacted assessments for deposit insurance, capital requirements, risk retention on the origination of certain securitized loans and debit card interchange fees. It also introduced a number of reforms related to mortgage originations. There is a significant possibility that the Dodd-Frank Act will, at a minimum, result in continued increases in regulatory burden, compliance costs and interest expense.

New laws, regulations, and other regulatory changes, along with negative developments in the financial industry and the domestic and international credit markets, may significantly affect the markets in which we do business, the markets for and value of our loans and investments, and our ongoing operations, costs and profitability. For more information, see “Regulation and Supervision” in Item 1 of this Annual Report.

**We may incur fines, penalties and other negative consequences from regulatory violations, possibly even inadvertent or unintentional violations.**

We maintain systems and procedures designed to ensure that we comply with applicable laws and regulations. However, some legal and regulatory frameworks provide for the imposition of fines or penalties for noncompliance even though the noncompliance was inadvertent or unintentional and even though there was in place at the time systems and procedures designed to ensure compliance. There may be negative consequences resulting from a finding of noncompliance, including restrictions on certain activities. Such a finding may also damage our reputation as described above and could restrict the ability of institutional investment managers to invest in our securities.

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**Systems failures, interruptions or breaches of security could have an adverse effect on our financial condition and results of operations.**

We are subject to certain operational risks, including, but not limited to, data processing system failures and errors, inadequate or failed internal processes, customer or employee fraud and catastrophic failures resulting from terrorist acts or natural disasters. We depend upon data processing, software, communication, and information exchange on a variety of computing platforms and networks and over the Internet, and we rely on the services of a variety of vendors to meet our data processing and communication needs. Despite instituted safeguards, we cannot be certain that all of our systems are entirely free from vulnerability to attack or other technological difficulties or failures. Information security risks have increased significantly due to the use of online, telephone and mobile banking channels by clients and the increased sophistication and activities of organized crime, hackers, terrorists and other external parties. Our technologies, systems, networks and our clients' devices have been subject to, and are likely to continue to be the target of, cyber-attacks, computer viruses, malicious code, phishing attacks or information security breaches that could result in the unauthorized release, gathering, monitoring, misuse, loss or destruction of our or our clients' confidential, proprietary and other information, the theft of client assets through fraudulent transactions or disruption of our or our clients' or other third parties' business operations. If information security is breached or other technology difficulties or failures occur, information may be lost or misappropriated, services and operations may be interrupted and we could be exposed to claims from customers. While we maintain a system of internal controls and procedures, any of these results could have a material adverse effect on our business, financial condition, results of operations or liquidity.

**Regulations relating to privacy, information security and data protection could increase our costs, affect or limit how we collect and use personal information and adversely affect our business opportunities.**

We are subject to various privacy, information security and data protection laws, including requirements concerning security breach notification, and we could be negatively impacted by these laws. For example, our business is subject to the Gramm-Leach-Bliley Act which, among other things: (i) imposes certain limitations on our ability to share nonpublic personal information about our customers with nonaffiliated third parties; (ii) requires that we provide certain disclosures to customers about our information collection, sharing and security practices and afford customers the right to "opt out" of any information sharing by us with nonaffiliated third parties (with certain exceptions) and (iii) requires we develop, implement and maintain a written comprehensive information security program containing safeguards appropriate based on our size and complexity, the nature and scope of our activities, and the sensitivity of customer information we process, as well as plans for responding to data security breaches. Various state and federal banking regulators and states have also enacted data security breach notification requirements with varying levels of individual, consumer, regulatory or law enforcement notification in certain circumstances in the event of a security breach. Moreover, legislators and regulators in the United States are increasingly adopting or revising privacy, information security and data protection laws that potentially could have a significant impact on our current and planned privacy, data protection and information security-related practices, our collection, use, sharing, retention and safeguarding of consumer or employee information, and some of our current or planned business activities. This could also increase our costs of compliance and business operations and could reduce income from certain business initiatives. This includes increased privacy-related enforcement activity at the federal level, by the Federal Trade Commission, as well as at the state level, such as with regard to mobile applications.

Compliance with current or future privacy, data protection and information security laws (including those regarding security breach notification) affecting customer or employee data to which we are subject could result in higher compliance and technology costs and could restrict our ability to provide certain products and services, which could have a material adverse effect on our business, financial conditions or results of operations. Our failure to comply with privacy, data protection and information security laws could result in potentially significant regulatory or governmental investigations or actions, litigation, fines, sanctions and damage to our reputation, which could have a material adverse effect on our business, financial condition or results of operations.

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

Third-party vendors provide key components of our business infrastructure such as internet connections, network access and core application processing. While we have selected these third-party vendors carefully, we do not control their actions. Any problems caused by these third parties, including as a result of their not providing us their services for any reason or their performing their services poorly, could adversely affect our ability to deliver products and services to our customers or otherwise conduct our business efficiently and effectively. Replacing these third-party vendors could also entail significant delay and expense.

Table of Contents**If our risk management framework does not effectively identify or mitigate our risks, we could suffer losses.**

Our risk management framework seeks to mitigate risk and appropriately balance risk and return. We have established processes and procedures intended to identify, measure, monitor and report the types of risk to which we are subject, including credit risk, operations risk, compliance risk, reputation risk, strategic risk, market risk, liquidity risk, and information technology risk. We seek to monitor and control our risk exposure through a framework of policies, procedures and reporting requirements. Management of our risks in some cases depends upon the use of analytical and/or forecasting models. If the models used to mitigate these risks are inadequate, we may incur losses. In addition, there may be risks that exist, or that develop in the future, that we have not appropriately anticipated, identified or mitigated. If our risk management framework does not effectively identify or mitigate our risks, we could suffer unexpected losses and could be materially adversely affected.

**ITEM 1B. UNRESOLVED STAFF COMMENTS**

None.

**ITEM 2. PROPERTIES**

We conduct our business through our executive and administrative office located in Towson, Maryland, which also serves as a full-service banking office, and six other full-service branch offices located in Baltimore City and the Maryland counties of Baltimore, Howard and Anne Arundel. The aggregate net book value of our premises, including leasehold improvements, was \$3.4 million at March 31, 2018. Our facilities are adequate and suitable for our operations as conducted by us. The following table sets forth certain information with respect to our offices, including lease expiration dates for leased properties.

| <b>Location</b>  | <b>Leased or<br/>Owned</b> | <b>Year Opened/<br/>Acquired</b> | <b>Lease Expiration<br/>Date</b> |
|--|----------------------------|----------------------------------|----------------------------------|
| <b><u>Executive and Administrative Office:</u></b>     |                            |                                  |                                  |
| 501 Fairmount Ave. Suite 200<br>Towson, Maryland 21286 | Leased                     | 2011                             | November 30, 2021                |
| <b><u>Branches:</u></b>                                |                            |                                  |                                  |
| 5600 Harford Road                                      | Owned                      | 1937                             | —                                |



|                                    |        |      |                 |
|------------------------------------|--------|------|-----------------|
| Baltimore, Maryland 21214          |        |      |                 |
| 8108 Jumpers Hole Road             | Owned  | 2009 | —               |
| Pasadena, Maryland 21122           |        |      |                 |
| 8216 Philadelphia Road             | Owned  | 2015 | —               |
| Rosedale, Maryland 21237           |        |      |                 |
| 788 Washington Boulevard           | Leased | 2018 | August 31, 2022 |
| Baltimore City, Maryland 21230 (2) |        |      |                 |
| 9050 National Pike                 | Leased | 2017 | August 31, 2023 |
| Ellicott City, Maryland 21042 (3)  |        |      |                 |
| 10283 York Road                    | Leased | 2016 | Jan. 31, 2020   |
| Cockeysville, Maryland 21030 (1)   |        |      |                 |

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(1) Property was acquired in the Fraternity Community Bancorp acquisition on May 13, 2016.

This branch was opened in March 2018. The former branch located at 764 Washington Boulevard in Baltimore (2) City, located on the same block as the new location, was acquired in the Fraternity acquisition and operated as Fraternity's administrative offices, as well as a full-service branch. We sold the former property in December 2017.

This branch was opened in July 2017 and is less than a mile from the former branch that was also leased. The (3) former branch location at 8460 Baltimore National Pike in Ellicott City, Maryland was closed. The lessor decided to reconstruct this property for an alternative use and we were required to relocate.

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**ITEM 3. LEGAL PROCEEDINGS**

Periodically, there have been various claims and lawsuits against us, such as claims to enforce liens, condemnation proceedings on properties in which we hold security interests, claims involving the making and servicing of real property loans and other issues incident to our business. We are not a party to any pending legal proceedings that we believe would have a material adverse effect on our financial condition, results of operations or cash flows.

**ITEM 4. MINE SAFETY DISCLOSURES**

Not applicable.

**PART II**

**ITEM MARKET FOR REGISTRANT’S COMMON EQUITY, RELATED STOCKHOLDER MATTERS  
5. AND ISSUER PURCHASES OF EQUITY SECURITIES**

**Market and Dividend Information.**

The Company’s common stock is listed on the NASDAQ Capital Market (“NASDAQ”) under the trading symbol “HBK.” The Company completed its initial public offering on October 10, 2012, and its stock commenced trading on the same day.

The following table sets forth the high and low sales prices of the Company’s common stock as reported by NASDAQ for the periods indicated. The Company has not paid any dividends to its stockholders to date. See “Dividends” below.

| <u>Fiscal 2018:</u> | <b>Price Range<br/>Per Share</b> |            |
|---------------------|----------------------------------|------------|
|                     | <b>High</b>                      | <b>Low</b> |
| Fourth Quarter      | \$ 15.87                         | \$ 14.25   |
| Third Quarter       | 15.40                            | 14.25      |
| Second Quarter      | 15.05                            | 14.05      |
| First Quarter       | 15.25                            | 14.45      |

| <u>Fiscal 2017:</u> | <b>Price Range<br/>Per Share</b> |            |
|---------------------|----------------------------------|------------|
|                     | <b>High</b>                      | <b>Low</b> |
| Fourth Quarter      | \$ 14.55                         | \$ 14.28   |
| Third Quarter       | 14.50                            | 13.50      |
| Second Quarter      | 14.19                            | 13.33      |
| First Quarter       | 14.25                            | 13.30      |

**Holder.**

As of June 29, 2018, there were approximately 134 holders of record of the Company's common stock.

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**Dividends.**

The Company has not paid any dividends to its shareholders to date. The payment of dividends in the future will depend upon a number of factors, including capital requirements, the Company's financial condition and results of operations, tax considerations, statutory and regulatory limitations and general economic conditions. In addition, the Company's ability to pay dividends is dependent on dividends received from Hamilton Bank. For more information regarding restrictions on the payment of cash dividends by the Company and by Hamilton Bank, see "Business—Regulation and Supervision—Holding Company Regulation—Dividends", "Business—Regulation and Supervision—Federal Savings Institution Regulation—Dividend Limitations" and Note 15 to the Consolidated Financial Statements included in this Annual Report. No assurances can be given that any dividends will be paid or that, if paid, will not be reduced or eliminated in the future.

**Recent Sales of Unregistered Securities; Use of Proceeds from Registered Securities.**

None.

**Purchases of Equity Securities by the Issuer and Affiliated Purchasers.**

There were no shares repurchased by the Company during fiscal 2018.

Table of Contents**ITEM 6. SELECTED FINANCIAL DATA**

The following tables set forth selected historical financial and other data of Hamilton Bancorp, Inc. for the periods and at the dates indicated. The following is only a summary and you should read it in conjunction with the consolidated financial statements of Hamilton Bancorp, Inc. and notes beginning on page F-1 of this Annual Report. The information at March 31, 2018 and 2017 and for the years then ended is derived in part from the audited consolidated financial statements that appear in this Annual Report. The information at March 31, 2016, 2015 and 2014 and for the years then ended is derived in part from audited financial statements that do not appear in this Annual Report.

|   | <b>At March 31,</b>   |             |             |             |             |
|---|-----------------------|-------------|-------------|-------------|-------------|
|   | <b>2018</b>           | <b>2017</b> | <b>2016</b> | <b>2015</b> | <b>2014</b> |
|   | <b>(In thousands)</b> |             |             |             |             |
| <b>Selected Financial Condition Data:</b>       |                       |             |             |             |             |
| Total assets                                    | \$525,533             | \$514,530   | \$392,917   | \$291,040   | \$302,769   |
| Cash and cash equivalents                       | 23,368                | 29,354      | 67,449      | 16,644      | 33,073      |
| Investment securities (1)                       | 16,379                | 21,597      | 16,544      | 21,582      | 26,778      |
| Mortgage-backed securities                      | 59,025                | 80,832      | 53,940      | 71,357      | 76,776      |
| Loans, net (2)                                  | 387,599               | 336,738     | 220,416     | 159,176     | 142,914     |
| Federal Home Loan Bank of Atlanta stock at cost | 3,122                 | 2,020       | 1,043       | 523         | 266         |
| Bank-owned life insurance                       | 17,456                | 18,253      | 12,710      | 12,360      | 12,002      |
| Deposits  | 405,143               | 412,856     | 313,994     | 222,319     | 238,820     |
| Borrowings                                      | 60,672                | 36,125      | 14,805      | 6,000       | -           |
| Total equity                                    | 54,076                | 59,791      | 61,545      | 60,800      | 61,770      |

(1) Includes U.S. agency securities, municipal and corporate bonds.

(2) Includes loans held for sale of \$-0-, \$-0-, \$259,000, \$581,000 and \$-0- at March 31, 2018, 2017, 2016, 2015 and 2014, respectively.

|   | <b>For the Years Ended March 31,</b>         |             |             |             |             |
|---|--|-------------|-------------|-------------|-------------|
|   | <b>2018</b>                                  | <b>2017</b> | <b>2016</b> | <b>2015</b> | <b>2014</b> |
|   | <b>(In thousands, except per share data)</b> |             |             |             |             |
| <b>Selected Operating Data:</b>                     |  |             |             |             |             |
| Interest revenue                                    | \$18,080                                     | \$16,762    | \$11,318    | \$9,383     | \$10,236    |
| Interest expense                                    | 3,587  | 2,871       | 1,843       | 1,662       | 1,916       |
| Net interest income                                 | 14,493                                       | 13,891      | 9,475       | 7,721       | 8,320       |
| Provision for loan losses                           | 1,575  | 3,395       | 440         | 170         | 1,874       |
| Net interest income after provision for loan losses | 12,918                                       | 10,496      | 9,035       | 7,551       | 6,446       |
| Noninterest revenue                                 | 1,996  | 1,054       | 1,554       | 1,108       | 1,056       |
| Noninterest expense                                 | 12,911                                       | 13,237      | 10,260      | 9,310       | 9,689       |
| Income (loss) before income taxes (benefit)         | 2,003  | (1,687 )    | 329         | (651 )      | (2,187 )    |
| Income taxes (benefit)                              | 8,052  | (758 )      | 422         | (337 )      | (992 )      |

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|                               |            |           |           |           |            |
|-------------------------------|------------|-----------|-----------|-----------|------------|
| Net income (loss)             | \$(6,049 ) | \$(929 )  | \$(93 )   | \$(314 )  | \$(1,195 ) |
| Basic loss per common share   | \$(1.90 )  | \$(0.29 ) | \$(0.03 ) | \$(0.10 ) | \$(0.35 )  |
| Diluted loss per common share | \$(1.90 )  | \$(0.29 ) | \$(0.03 ) | \$(0.10 ) | \$(0.35 )  |

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**At or For the Years Ended March 31,**  
**2018      2017      2016      2015      2014**

**Selected Financial Ratios and Other Data:****Performance Ratios:**

|   |          |          |          |          |          |
|---|----------|----------|----------|----------|----------|
| Return on average assets (ratio of net loss to average total assets)    | (1.17) % | (0.19) % | (0.03) % | (0.11) % | (0.38) % |
| Return on average equity (ratio of net loss to average equity)          | (9.96) % | (1.57) % | (0.15) % | (0.54) % | (1.84) % |
| Interest rate spread (1)  | 2.96 %   | 2.97 %   | 2.89 %   | 2.70 %   | 2.68 %   |
| Net interest margin (2)   | 3.05 %   | 3.04 %   | 3.02 %   | 2.85 %   | 2.85 %   |
| Efficiency ratio expressed as a percentage (3)                          | 78.49 %  | 83.92 %  | 90.43 %  | 106.27 % | 99.90 %  |
| Noninterest expense to average total assets                             | 2.50 %   | 2.66 %   | 3.02 %   | 3.17 %   | 3.08 %   |
| Noninterest revenue to average total assets                             | 0.39 %   | 0.21 %   | 0.46 %   | 0.37 %   | 0.33 %   |
| Average interest-earning assets to average interest-bearing liabilities | 112.72 % | 111.69 % | 121.98 % | 125.10 % | 125.30 % |
| Average equity to average total assets                                  | 11.74 %  | 11.85 %  | 17.98 %  | 19.84 %  | 20.58 %  |

**Asset Quality Ratios:**

|   |         |         |         |         |         |
|---|---------|---------|---------|---------|---------|
| Non-performing assets to total assets             | 1.45 %  | 0.55 %  | 1.40 %  | 0.93 %  | 1.88 %  |
| Non-performing loans to gross loans               | 1.84 %  | 0.69 %  | 2.27 %  | 1.41 %  | 3.48 %  |
| Allowance for loan losses to non-performing loans | 39.36 % | 94.49 % | 33.70 % | 74.97 % | 35.44 % |
| Allowance for loan losses to gross loans          | 0.73 %  | 0.65 %  | 0.76 %  | 1.05 %  | 1.23 %  |
| Net charge-offs to average loans                  | 0.26 %  | 0.92 %  | 0.22 %  | 0.18 %  | 1.41 %  |

**Capital Ratios:**

|  |         |         |         |         |         |
|--|---------|---------|---------|---------|---------|
| Common equity tier 1 capital (to risk-weighted assets) (4) | 10.61 % | 12.13 % | 19.06 % | 24.37 % | -       |
| Total capital (to risk-weighted assets) (4)                | 11.39 % | 12.81 % | 19.81 % | 25.32 % | 28.38 % |
| Tier 1 capital (to risk-weighted assets) (4)               | 10.61 % | 12.13 % | 19.06 % | 24.37 % | 27.28 % |
| Tier 1 capital (to total adjusted assets) (4)              | 7.64 %  | 8.28 %  | 11.78 % | 15.82 % | 15.10 % |
| Equity to total assets                                     | 10.29 % | 11.62 % | 15.66 % | 20.89 % | 20.40 % |
| Tangible equity to tangible assets                         | 8.70 %  | 9.99 %  | 14.05 % | 20.12 % | 19.65 % |

**Number of:**

|                                |    |    |    |    |    |
|--------------------------------|----|----|----|----|----|
| Full service offices           | 7  | 7  | 5  | 4  | 4  |
| Full time equivalent employees | 72 | 74 | 61 | 55 | 58 |

(1) The interest rate spread represents the difference between the weighted-average yield on interest-earning assets and the weighted-average cost of interest-bearing liabilities for the period.

(2) The net interest margin represents net interest income as a percent of average interest-earning assets for the period.

(3) The efficiency ratio represents noninterest expense divided by the sum of net interest income and noninterest income, excluding investment and property gains, branch consolidation and merger related expense, and write-downs and losses on foreclosed real estate.

(4) Capital ratios are for Bank only.





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**ITEM 7. MANAGEMENT’S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATION**

This discussion and analysis reflects our consolidated financial statements and other relevant statistical data, and is intended to enhance your understanding of our financial condition and results of operations. The information in this section has been derived from the audited consolidated financial statements, which appear beginning on page F-1 of this Annual Report. You should read the information in this section in conjunction with the business and financial information regarding Hamilton Bancorp, Inc. provided in this Annual Report.

Statements included in this management's discussion and analysis include non-GAAP financial measures and should be read along with the accompanying tables which provide a reconciliation of non-GAAP financial measures to GAAP financial measures. The Company's management uses these non-GAAP financial measures, including tangible common equity, in its analysis of the Company's performance. The tangible common equity non-GAAP reconciliation, which includes tangible book value per share, is presented in the “Overview” section below.

Management believes that non-GAAP financial measures provide additional useful information that allows readers to evaluate the ongoing performance of the Company without regard to transactional activities. Non-GAAP financial measures should not be considered as an alternative to any measure of performance or financial condition as promulgated under GAAP, and investors should consider the Company's performance and financial condition as reported under GAAP and all other relevant information when assessing the performance or financial condition of the Company. Non-GAAP financial measures have limitations as analytical tools, and investors should not consider them in isolation or as a substitute for analysis of the Company's results or financial condition as reported under GAAP.

**Overview**

The Company and its wholly owned subsidiary, Hamilton Bank, continue to show growth in both revenue and asset size for the year ending March 31, 2018 as compared to the year ending March 31, 2017, despite a net loss of \$6.0 million relating to certain tax expense adjustments taken during the fiscal year. Interest revenue increased \$1.3 million, or 7.9%, during fiscal 2018 as the Company continued to show strong loan demand through both organic growth and the purchase of loan pools. Growth in interest revenue was partially offset by an increase of \$716,000 in our interest expense associated with taking on additional borrowings and an increase in interest rates that impacted our deposit costs. The Company was able to increase non-interest revenue relating to service charges and other fees. We also recognized \$835,000 in revenue related to the payout of insurance under our bank-owned life insurance (“BOLI”) policies and had a \$213,000 gain on sale of our Pigtown branch. These gains were partially offset by \$115,000 in loss on the write-down or disposal of certain leasehold improvements associated with or legacy or former Cockeysville branch.

Non-interest expense decreased modestly by \$326,000 over the twelve months ending March 31, 2018 compared to the same period a year ago. The decrease is in large part due to merger expenses and branch consolidation expense associated with the acquisition of Fraternity that were recognized in the prior year. The acquisition of Fraternity closed on May 13, 2016. Partially offsetting the decline in non-interest expense were increases in salaries and benefits and legal expenses. Salaries and benefits increased due to strategic new hires focused on branch efficiency and new products, while legal expense increased because of costs associated with loan purchases and other administrative matters, including our conversion to a state chartered bank. Management has diligently worked at monitoring and improving efficiencies to reduce our overall operating expenses and improve our efficiency ratio going forward. Lastly, the largest impact to the overall net loss was related to tax expense.

In December 2017, the Company performed a revaluation of its net deferred tax assets as a result of the reduction in the corporate income tax rate that was enacted through the federal government's passage of the *Tax Cuts and Jobs Act* on December 22, 2017. The revaluation resulted in an adjustment downward of \$2.3 million to our net deferred tax asset that was recorded through income tax expense. In addition, management evaluated the remaining net deferred tax asset of \$5.8 million at the end of fiscal 2018. In the judgement of management, it was determined that it was more likely than not that such deferred tax assets will not become realizable based upon the fact that the Company has experienced cumulative losses for three consecutive years. Because of these losses, the Company is unable to rely upon the projection of future taxable income under ASC 740, *Accounting for Income Taxes*. As a result, a valuation allowance was established for \$5.8 million with the offset being recorded through income tax expense. If, in the future, the Company generates taxable income on a sustained basis sufficient to support the deferred tax assets, the need for a deferred tax valuation allowance could change, resulting in the reversal of all or a portion of the deferred tax asset valuation at that time. The establishment of a valuation allowance on our deferred tax assets for financial reporting purposes does not affect how the net operating loss carryforwards may be utilized on our subsequent income tax returns. [For further disclosure on this matter, see *Income Tax Expense* within this section of the Management Discussion and Analysis ("MD&A") in this Annual Report on Form 10-K].

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The following highlights contain additional financial data and events that have occurred during the fiscal year ending March 31, 2018:

Pre-tax income improved to \$2.0 million compared to a loss of \$1.7 million for the 2017 fiscal year, an increase of \$3.7 million year-over-year.

After-tax loss for fiscal 2018 reflects a loss of \$6.0 million, or \$1.90 per common share, compared to a loss of \$929 thousand, or \$0.29 per common share, for fiscal 2017. The loss in fiscal 2018 is due to the \$2.3 million tax adjustment to the Company's net deferred tax assets from the *Tax Cuts and Job Act* and the establishment of a valuation allowance on the remaining net deferred tax asset of \$5.8 million, as discussed earlier.

Net interest income increased to \$14.5 million, up \$602,000, or 4.3%, from \$13.9 million. This improvement was driven by a \$1.3 million, or 7.9%, increase in interest revenue, partially offset by a \$716,000 increase in interest expense.

Net interest margin remained relatively unchanged at 3.05% for fiscal 2018 compared to 3.04% for fiscal 2017.

Efficiency ratio improved from 83.9% to 78.5% due to efficiencies of scale, income and gains from proceeds relating to bank-owned life insurance (BOLI), and the effects of certain costs related to the acquisition of Fraternity Community Bancorp, Inc. (Fraternity) during the prior year period.

In the fourth quarter of fiscal 2018, realized \$835,000 in non-interest revenue pertaining to death benefits received from the passing of an employee under our BOLI insurance policies.

During the third quarter of fiscal 2018 we sold our Pigtown branch located in Baltimore City at a gain of \$213,000, net of the disposal of various furniture and equipment associated with it. We also relocated our Ellicott City branch during the second quarter of fiscal 2018. Both branches were relocated within their respective communities, but to a smaller, more efficient space that will provide operational cost savings.

Cash management fees increased by 49.0% during fiscal 2018 from \$84,000 to \$125,000. At the same time our merchant card services income also grew 31.0% to \$33,000. This reflects our continued focus on commercial business.

Total assets grew \$11.0 million to \$525.5 million, increasing from \$514.5 million at March 31, 2017.

Gross loans grew \$50.2 million, or 14.8%, to \$389.2 million from \$339.0 million at March 31, 2017. The growth in loans is attributable to both organic growth and loan purchases throughout the fiscal year.

Net charge-offs declined 67.3%, or almost \$2.0 million, from \$2.9 million a year ago to \$948,000 in fiscal 2018.

The allowance for loan losses as a percentage of nonperforming loans declined from 94.5% at March 31, 2017 to 39.4% due to one commercial real estate loan being placed on nonaccrual during the year. Based upon an updated appraisal and market value of the underlying collateral, there is no impairment currently associated with this loan.

Total deposits decreased \$7.7 million from \$412.9 million at March 31, 2017 to \$405.1 million, while borrowings increased \$24.5 million from \$36.1 million to \$60.7 million over the same period. Core deposits (consisting of all deposits except certificates of deposits) declined \$6.7 million to \$157.7 million. The decline in deposits is largely due to runoff from our money market promotion that began in December 2016, as well as an increasingly competitive market due to rising interest rates. Core deposits represent 38.9% of total deposits at March 31, 2018 compared to 39.8% a year ago.

The Company ended fiscal 2018 with a book value of \$15.87 per common share and a tangible book value of \$13.18 per common share compared to \$17.53 and \$14.80, respectively, at March 31, 2017. Tangible book value decreased because of the net loss for the year.

|  | March 31,<br>2018 | March 31,<br>2017 |
|--|-------------------|-------------------|
| Tangible book value per common share:      |                   |                   |
| Total shareholders' equity                 | \$54,076,132      | \$59,791,230      |
| Less: Goodwill and other intangible assets | (9,176,764 )      | (9,302,828 )      |
| Tangible common equity                     | \$44,899,368      | \$50,488,402      |
| Outstanding common shares                  | 3,407,613         | 3,411,075         |
| Tangible book value per common share       | \$13.18           | \$14.80           |

The Company maintained strong liquidity and at March 31, 2018 the Bank was deemed "well capitalized" under federal regulations.

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**Strategic Plan**

We have based our 2019-2021 strategic plan on the objective of improving shareholder value and growth through creating sustainable and profitable growth given the current and expected economic and competitive environment in the financial services industry. Our short-term goals include continuing the growth of operating revenue, changing the mix of our deposits base to be more concentrated in lower costing core deposits, collecting payments on non-accrual and past due loans, enhancing and improving credit quality, expanding fee income, maintaining a sensible branch network, and using technology to improve efficiencies and enhance the customer experience.

We identified several strategic priorities in our three-year Strategic Plan. Those priorities included focusing on the following core areas:

Efficient Operating Revenue Growth – Generating sustainable, profitable operating revenue through smart growth of earning assets that are funded by low-cost core deposits and growth of noninterest income. In addition, we will focus on efficient utilization of the Bank’s assets and other resources. This strategic priority includes prudent loan growth, sales strategies to attract and grow small business deposit and other fee income services, strategic marketing campaigns, studying and benchmarking efficiency and productivity, and focusing on ways to utilize technology to drive earnings.

Low-Cost Funding Strategies – Will focus on utilizing and growing low-cost core deposits as the primary funding source for loans. Given the current environment for higher-returns on investments, the retention of deposit customers along with targeted sales strategies will be important to growing deposits. Comprehensive marketing plans for increasing brand awareness in our market and promotion of products and services will be required, along with a seamless, fully integrated delivery experience for our customers that leverages technology and optimizes efficiencies. These strategies will apply to not just consumers, but to all commercial and small business customers.

Capital to Support Growth – We will increase the capital and value of the holding company’s stock through sustainable, consistent earnings, prudent capital management and enhancement of overall “franchise value”. We will continually evaluate the Bank’s capital needs and, if additional capital is needed, the most suitable type of capital, whether it be subordinated-debt or common or preferred stock.

Although the current economic climate continues to present significant challenges for the financial industry, management feels that based on our strategic initiatives we have positioned the Company to capitalize on the opportunities that may become available in the current economy, as well as a healthier economy going forward.

**Critical Accounting Policies**

The discussion and analysis of the financial condition and results of operations are based on our consolidated financial statements, which are prepared in conformity with generally accepted accounting principles used in the United States of America. The preparation of these consolidated financial statements requires management to make estimates and assumptions affecting the reported amounts of assets and liabilities, disclosure of contingent assets and liabilities, and the reported amounts of income and expenses. We consider the accounting policies discussed below to be critical accounting policies. The estimates and assumptions that we use are based on historical experience and various other factors and are believed to be reasonable under the circumstances. Actual results may differ from these estimates under different assumptions or conditions, resulting in a change that could have a material impact on the carrying value of our assets and liabilities and our results of operations.

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For a discussion of significant accounting policies, *see Note 1—Nature of Operations and Summary of Significant Accounting Policies* in the Notes to our Consolidated Financial Statements. The following are the accounting policies that we believe require the most subjective or complex judgments, and as such could be most subject to revision as new information becomes available:

***Allowance for Loan Losses.*** The allowance for loan losses is the estimated amount considered necessary to cover inherent credit losses in the loan portfolio at the balance sheet date. The allowance is established through the provision for losses on loans which is charged against income. In determining the allowance for loan losses, management makes significant estimates and has identified this policy as one of our most critical accounting policies.

Management, at a minimum, performs a quarterly evaluation of the allowance for loan losses. Consideration is given to historical losses in conjunction with a variety of other factors including, but not limited to, current economic conditions, delinquency statistics, geographic and industry concentrations, the adequacy of the underlying collateral, the financial strength of the borrower, results of internal loan reviews and other relevant factors. This evaluation is inherently subjective as it requires material estimates that may be susceptible to significant change.

The analysis has two components, specific and general allocations. Specific allocations can be made for estimated losses related to loans that are determined to be impaired. Impairment is measured by determining the present value of expected future cash flows or, for collateral-dependent loans, the fair value of the collateral adjusted for market conditions and selling expenses. If the fair value of the loan is less than the loan's carrying value, a charge is recorded for the difference. The general allocation is determined by segregating the remaining loans by type of loan, risk weighting (if applicable) and payment history. We also analyze historical loss experience, delinquency trends, general economic conditions and geographic and industry concentrations. This analysis establishes factors that are applied to the loan groups to determine the amount of the general reserve.

We cannot predict with certainty the amount of loan charge-offs that we will incur. Our regulatory agencies, as an integral part of their examination processes, periodically review our allowance for credit losses. Such agencies may require that we recognize additions to the allowance for credit losses based on their judgments about information available to them at the time of their examination. To the extent that actual outcomes differ from management's estimates, additional provisions to the allowance for credit losses may be required that would adversely impact earnings in future periods.

***Securities Valuation and Impairment.*** We classify our investments in debt and equity securities as either held to maturity or available for sale. Securities classified as held to maturity are recorded at cost or amortized cost. Available-for-sale securities are carried at fair value. We obtain our fair values from a third-party service. This service's fair value calculations are based on quoted market prices when such prices are available. If quoted market prices are not available, estimates of fair value are computed using a variety of techniques, including extrapolation from the quoted prices of similar instruments or recent trades for thinly traded securities, fundamental analysis, or

through obtaining purchase quotes. Due to the subjective nature of the valuation process, it is possible that the actual fair values of these investments could differ from the estimated amounts, thereby affecting our financial position, results of operations and cash flows.

If the estimated value of investments is less than the cost or amortized cost, we evaluate whether an event or change in circumstances has occurred that may have a significant adverse effect on the fair value of the investment. If such an event or change has occurred and we determine that the impairment is other-than-temporary, we record the impairment of the investment in the period in which the event or change occurred. We also consider how long a security has been in a loss position in determining if it is other than temporarily impaired. Management also assesses the nature of the unrealized losses taking into consideration factors such as changes in risk-free interest rates, general credit spread widening, market supply and demand, creditworthiness of the issuer, and quality of the underlying collateral. At March 31, 2018, all of our securities were either issued by U.S. government agencies, U.S. government-sponsored enterprises, municipalities, or corporations.

**Goodwill Impairment.** Goodwill represents the excess purchase price paid over the fair value of the net assets acquired. Goodwill is not amortized but is tested for impairment annually or more frequently if events or changes in circumstances indicate that the asset might be impaired. The Company is considered the Reporting Unit for purposes of impairment testing. Impairment testing requires that the fair value of the Company be compared to the carrying amount of the Company's net assets, including goodwill. If the fair value of the Company exceeds the book value, no write-down of recorded goodwill is required. If the fair value of the Company is less than book value, an expense may be required to write-down the related goodwill to the proper carrying value. We test for impairment of goodwill during February of each year based upon December financial information and current projections. We estimate the fair value of the Company utilizing four valuation methods including the Comparable Transactions Approach, the Control Premium Approach, the Public Market Peers Approach, and the Discounted Cash Flow Approach.



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Based on our impairment testing during February 2018, there was no evidence of impairment of the Company's goodwill or intangible assets.

**Business Combinations.** Business combinations are accounted for using the acquisition method of accounting. Under the acquisition method of accounting, acquired assets and assumed liabilities are included with the acquirer's accounts as of the date of acquisition at estimated fair value, with any excess of purchase price over the fair value of the net assets acquired (including identifiable core deposit intangibles) capitalized as goodwill. In the event that the fair value of the net assets acquired exceeds the purchase price, an acquisition gain is recorded for the difference in the consolidated statements of operations for the period in which the acquisition occurred. The core deposit intangible asset is recognized as an asset apart from goodwill when it arises from contractual or other legal rights or if it is capable of being separated or divided from the acquired entity and sold, transferred, licensed, rented or exchanged. In addition, acquisition-related costs and restructuring costs are recognized as period expenses as incurred.

**Income Taxes.** We account for income taxes under the asset/liability method. We recognize deferred tax assets for the future consequences attributable to differences between the financial statement carrying amounts of existing assets and liabilities and their respective tax bases, as well as operating loss and tax credit carry-forwards. We measure deferred tax assets and liabilities 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. We recognize the effect on deferred tax assets and liabilities of a change in tax rates in income in the period indicated by the enactment date. We establish a valuation allowance for deferred tax assets when, in the judgment of management, it is more likely than not that such deferred tax assets will not become realizable. The judgment about the level of future taxable income is dependent to a great extent on matters that may, at least in part, be beyond our control.

**Comparison of Financial Condition at March 31, 2018 and March 31, 2017**

**Assets.** Total assets increased \$11.0 million to \$525.5 million at March 31, 2018 from \$514.5 million at March 31, 2017. The increase is primarily attributable to a \$50.2 million increase in gross loans, partially offset by a \$27.0 million decline in investment securities, an \$8.0 million decrease in net deferred tax assets, and \$6.0 million decrease in cash and cash equivalents.

**Cash and Cash Equivalents.** Cash and cash equivalents decreased by \$6.0 million, or 20.4%, to \$23.4 million at March 31, 2018 from \$29.3 million at March 31, 2017. The decline from March 31, 2017 is in part a result of cash and investments used to fund organic loan growth and purchase various pools of residential mortgage, commercial business, and consumer loans throughout the year; thereby converting lower interest-earning cash and investments

into higher interest-earning loans. In the last quarter of fiscal 2018, we were able to replenish and increase our cash position by \$13.3 million through an increase in our core deposit base.

**Certificates of Deposit Held as Investment.** Certificates of deposit (“CDs”) of \$499,000 remained unchanged from March 31, 2017 to March 31, 2018. The Company currently holds two CDs that are equal to or less than \$250,000 and fully insured by the FDIC. The weighted average rate and term of the portfolio is 2.28% and 3.6 years, respectively.

**Securities.** Our investment portfolio consists primarily of investment grade securities including U.S. government agency and government-sponsored entity (“GSEs”) securities, securities issued by states, counties and municipalities, corporate bonds, and mortgage-backed securities. At March 31, 2018, all securities are classified as available for sale. While we usually intend to hold investment securities until maturity, this classification provides us the opportunity to divest of securities that may no longer meet our liquidity objectives.

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Investment securities decreased \$27.0 million, or 26.4%, to \$75.4 million at March 31, 2018, from \$102.4 million at March 31, 2017. The decrease is related to \$15.1 million in cash flows resulting from normal principal payments associated with the mortgage-backed security portfolio, as well as the sale of \$11.6 million in securities during fiscal 2018, including \$7.4 million of securities sold in the third quarter ended December 31, 2017. The sale of securities during the year resulted in a loss of \$2,000. The fair value of the investment portfolio declined \$676,000 from an unrealized net loss position of \$2.2 million at March 31, 2017 to an unrealized net loss position of \$2.9 million at March 31, 2018. The decrease in fair value of the investment portfolio is a result of the increase in interest rates over the past fiscal year, particularly the last quarter of fiscal 2018. Partially offsetting the decline in value is the passage of time as certain investments get closer to maturity.

We have evaluated securities with unrealized losses for an extended period of time and determined that these losses are temporary because, at this point in time, we have the ability to hold them until maturity. Currently, we have no intent to sell these securities; however, if market conditions or funding needs change, we may sell securities if needed. As the maturity date moves closer and/or interest rates decline, we expect that any unrealized losses for individual securities in the portfolio will decline or dissipate. In addition, we perform an annual impairment analysis with respect to securities issued by states, counties, municipalities, and corporations that are in a loss position for an extended period of time, typically twelve months. As a result, we have not identified any portion of the unrecorded loss as being attributed to credit deterioration in the issuer of the security.

**Premises and Equipment.** We currently have seven full service branches, one of which operates out of our administrative offices. With our acquisitions of Fairmount and Fraternity, we added three new branch locations and one that overlapped an existing location.

In the acquisition of Fairmount, the Company acquired the main office, that included the administrative offices and the only full- service branch, three vacant lots, and an unoccupied branch building that was not in operation at the time of acquisition. Due to growth, we subsequently re-located several back-office departments to the administrative office space that was acquired. The Company then sold the unoccupied branch building in fiscal 2017 with a book balance of \$405,000 for \$425,000 with net proceeds of \$393,000, excluding closing costs.

In the acquisition of Fraternity, the Company acquired two branches and the main office located in Baltimore City that included both the administrative offices of Fraternity and a full-service branch. The main office was owned by the bank and the other two branches were under a lease agreement at the time of acquisition. One of the leased branches was in close proximity and serviced the same geographic area as one of Hamilton's existing branches that was also leased. The acquired branch was in a better location, smaller in size, and less expensive to operate. As a result, management decided to close our existing branch in May 2016 and move our current customers to the newly acquired location; however, we were unable to get out of the then in place lease agreement. Consequently, in accordance with accounting guidelines, we immediately recognized the present value of the remaining lease payments under that lease, which amounted to \$495,000. In November 2017, we reached an agreement with the lessor for \$250,000 to terminate the lease and allow another third party to occupy the property. The agreement saved the Bank approximately \$32,000 over the remaining term of the lease.

In December 2017 we sold the building located in the Pigtown community of Baltimore City that was obtained in the acquisition of Fraternity for \$830,000. The building housed the administrative offices of Fraternity and our original Pigtown branch. Subsequent to the acquisition, we continued to operate the Pigtown branch from this location; however, the administrative space was not being utilized. We determined it would be more cost effective to sell the building and relocate the branch within the same community to a smaller, more efficient space that would provide operational cost savings. The sale of the building and various furniture and equipment resulted in a gain of \$213,000. The new Pigtown branch, which is being leased, was opened in March 2018.

We also relocated our Ellicott City branch within the same geographic area of Howard county during the second quarter of fiscal 2018. Similar to our Pigtown branch, we moved to a smaller, more efficient space that provided cost savings. The former and new location were or are leased properties. In addition, we recognized a loss of \$115,000 associated with the write-off or disposal of leasehold improvements that pertained to our legacy or former Cockeysville branch.

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**Loans.** Excluding loan premiums and loan origination fees and costs, gross loans receivable increased by \$50.2 million, or 14.8%, to \$389.2 million at March 31, 2018 from \$339.0 million at March 31, 2017. The increase is attributable to organic growth and approximately \$54.0 million in loan purchases throughout the year. The various loan purchases included residential mortgages, commercial business, and consumer loans. Included in gross loans at March 31, 2018 are acquired loans with a book balance of \$112.0 million associated with the acquisitions of Fraternity and Fairmount institutions (these loans are reflected in the “acquired” loan column of the table below). At March 31, 2018, gross loans receivable represented 74.1% of total assets compared to 65.9% of total assets at March 31, 2017. The following table details the composition of loans and the related percentage mix and growth of total loans. We did not hold any loans for sale as of March 31, 2018 or 2017.

|                             | March 31, 2018 |               |               | Percent<br>of<br>Total | March 31, 2017 |               |               | Percent<br>of<br>Total | Y<br>G<br>A |
|-----------------------------|----------------|---------------|---------------|------------------------|----------------|---------------|---------------|------------------------|-------------|
|                             | Legacy         | Acquired      | Total         |                        | Legacy         | Acquired      | Total         |                        |             |
| Real estate<br>loans:       |                |               |               |                        |                |               |               |                        |             |
| One-to<br>four-family:      |                |               |               |                        |                |               |               |                        |             |
| Residential                 | \$85,248,184   | \$72,749,066  | \$157,997,250 | 41 %                   | \$67,126,677   | \$83,892,389  | \$151,019,066 | 45 %                   | \$          |
| Residential<br>construction | 5,450,827      | -             | 5,450,827     | 1 %                    | 6,426,076      | -             | 6,426,076     | 2 %                    |             |
| Investor                    | 9,275,031      | 17,460,809    | 26,735,840    | 7 %                    | 6,742,469      | 18,779,644    | 25,522,113    | 8 %                    |             |
| Commercial                  | 100,403,769    | 11,762,485    | 112,166,254   | 29 %                   | 92,665,689     | 14,898,523    | 107,564,212   | 32 %                   |             |
| Commercial<br>construction  | 5,763,784      | 1,352,019     | 7,115,803     | 3 %                    | 1,881,541      | 1,308,652     | 3,190,193     | 2 %                    |             |
| Total real<br>estate loans  | 206,141,595    | 103,324,379   | 309,465,974   | 80 %                   | 174,842,452    | 118,879,208   | 293,721,660   | 87 %                   |             |
| Commercial<br>business      | 38,302,739     | 1,841,226     | 40,143,965    | 10 %                   | 19,518,029     | 2,019,337     | 21,537,366    | 6 %                    |             |
| Home equity<br>loans        | 13,956,327     | 6,039,462     | 19,995,789    | 5 %                    | 13,278,229     | 7,266,141     | 20,544,370    | 6 %                    |             |
| Consumer                    | 18,849,448     | 766,063       | 19,615,511    | 5 %                    | 2,258,836      | 937,600       | 3,196,436     | 1 %                    |             |
| Total loans                 | \$277,250,109  | \$111,971,130 | \$389,221,239 | 100 %                  | \$209,897,546  | \$129,102,286 | \$338,999,832 | 100 %                  | \$          |

The Company’s largest concentration of loans continues to be residential one-to four-family loans as a result of the loans acquired in the Fraternity and Fairmount acquisitions. This loan portfolio comprises 41% of the entire loan portfolio at March 31, 2018, an increase of \$7.0 million from March 31, 2017. This growth is primarily related to the purchase of \$19.3 million in residential mortgage loans during the second half of fiscal 2018. In addition, over the last half of fiscal 2017 and into fiscal 2018 we began to portfolio many of the traditional residential mortgage loans we originated, versus selling them in the secondary market, due to the increase in normal attrition within this loan segment resulting from our acquisitions. Prior to that time, we generally sold these loans in the secondary market at a premium to assist with managing interest rate risk and to enhance non-interest revenue.

In fiscal 2015, as a means to supplement our residential loan portfolio, the Company began to promote its one-to-four family residential construction lending program. During fiscal 2018, the Bank originated commitments of \$12.2 million in residential construction loans. As a result, at March 31, 2018, we had \$8.7 million in residential construction commitments, of which \$5.4 million in funds have been advanced; compared to \$11.8 million in residential construction commitments at March 31, 2017 of which \$6.0 million in funds had been advanced. The construction period on residential homes is typically nine to twelve months, at which time the Bank is often repaid through permanent financing by a third party.

Real estate investor loans represent funds advanced to borrowers for the purchase or refinance of non-owner occupied one-to-four family properties. These loans make up \$26.7 million, or 6.9%, of total gross loans at March 31, 2018, including a remaining balance of \$17.5 million that were acquired from Fraternity and Fairmount. This type of lending can involve more risk than originating owner-occupied one-to-four family residential mortgages and as such, the Bank typically refrains from originating this type of loan organically.

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The Bank continues to focus on growth through the origination or purchase of both commercial real estate and commercial business loans as these loans offer higher rates of return and shorter maturity periods than typical retail lending. The largest increase in loans over fiscal 2018 in terms of dollars, is a \$18.6 million, or 86.4%, increase in commercial business loans from \$21.5 million at March 31, 2017 to \$40.1 million at March 31, 2018. In the last half of fiscal 2017, management focused on diversifying the commercial loan portfolio and seeking more asset-based type lending relationships both organically and through purchases. The majority of the increase in commercial business loans is related to the purchase of a \$15.5 million pool of commercial business loans at the end of the first quarter of fiscal 2018. The pool of loans consists of commercial lease loans that are concentrated in equipment that is necessary to operate a business segment, such as medical equipment. Over this same period, commercial real estate loans have also grown by \$4.6 million, or 4.3%, from \$107.6 million at March 31, 2017 to \$112.2 million at March 31, 2018. Commercial real estate comprises 28.8% of the total loan portfolio at March 31, 2018, down slightly from 31.7% at March 31, 2017 due to the growth and diversification of the commercial business loan portfolio over this same period. The Bank continues to see the benefits of our commercial lending platform that was restructured in the first half of fiscal 2016, with new personnel and improved underwriting and monitoring procedures, from both an origination and credit quality perspective.

As a means to continue to increase revenue and diversify the loan portfolio, a group of consumer loans totaling \$19.8 million was purchased in August 2017 from another financial institution. This portfolio of loans was collateralized by various makes and models of recreational vehicles (RV). Prior to this purchase, the consumer portfolio made up less than 1.0% of the total loan portfolio. This purchase increased our consumer loan balances significantly from \$3.2 million at March 31, 2017 to \$19.6 million at March 31, 2018; accounting for 5.0% of the entire loan portfolio. As a result, we were able to further diversify the composition of the loan portfolio and increase our net interest income.

**Bank-Owned Life Insurance.** We invest in bank-owned life insurance (“BOLI”) to provide us with a funding source for our benefit plan obligations. BOLI also provides us noninterest income that is nontaxable. At March 31, 2018, our investment in bank-owned life insurance was \$17.5 million, a decrease of \$797,000 from \$18.3 million at March 31, 2017. Federal regulations generally limit our investment in BOLI to 25% of our Tier 1 capital plus our allowance for loan losses. Our amount of BOLI exceeded these limits because of the BOLI we acquired in the Fraternity acquisition and the increase in cash surrender value of these policies over the years.

The decrease of \$797,000 is attributable to the payout of several BOLI policies related to the unexpected passing of a beloved employee during the current year. The Company received \$2.1 million in proceeds, of which \$1.3 million was applied against the cash surrender value of the BOLI policies and the remaining \$835,000 was recorded as non-interest income. The decline associated with the payout under the policies was partially offset by the increase in cash surrender value of the other BOLI insurance policies that are held.

**Deposits.** Total deposits (excluding premiums on acquired deposits) decreased \$7.3 million to \$404.7 million at March 31, 2018 from \$412.0 million at March 31, 2017. The Company continues to focus on generating lower cost, core deposits (which includes all deposits other than certificates of deposit) and maintaining maturing certificates of deposit to support continued loan growth. Overall core deposits have decreased \$6.7 million, or 4.0%, to \$157.7

million at March 31, 2018 compared to \$164.4 million at March 31, 2017. This decline is attributable to the end of a promotional rate on certain money market accounts, as well as a very competitive deposit market. Core deposits accounted for 38.9% of total deposits at March 31, 2018, compared to 39.9% at March 31, 2017. The Bank is currently running deposit promotions to attract new customers in a competitive deposit market.



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The following table details the composition of deposits and the related percentage mix and growth of total deposits.

|                              | March 31, 2018 |                  | March 31, 2017 |                  | Year-To-Date Growth |                |
|------------------------------|----------------|------------------|----------------|------------------|---------------------|----------------|
|                              | Total          | Percent of Total | Total          | Percent of Total | Amount              | Growth Percent |
| Savings                      | \$42,499,381   | 10 %             | \$44,614,415   | 11 %             | \$(2,115,034)       | -5 %           |
| Noninterest-bearing checking | 29,557,943     | 7 %              | 30,401,454     | 7 %              | (843,511 )          | -3 %           |
| Interest-bearing checking    | 27,219,286     | 7 %              | 26,415,189     | 7 %              | 804,097             | 3 %            |
| Money market accounts        | 58,466,228     | 14 %             | 62,962,902     | 15 %             | (4,496,674)         | -7 %           |
| Time deposits                | 246,988,613    | 61 %             | 247,632,742    | 60 %             | (644,129 )          | 0 %            |
|                              | \$404,731,451  | 100 %            | \$412,026,702  | 100 %            | \$(7,295,251)       | -2 %           |
| Premium on deposits assumed  | 411,524        |                  | 829,072        |                  | (417,548 )          |                |
| Total deposits               | \$405,142,975  |                  | \$412,855,774  |                  | \$(7,712,799)       |                |

As loan demand increases, our strategy with respect to deposits has been to maintain our current certificate of deposit base, as we focus on growing our lower costing core deposits at a faster pace. We hope to accomplish this by pricing more competitively in the marketplace or through short-term certificate of deposit promotions. However, there may be instances when funding demands are more immediate. To meet these demands, the Company entered into a contract and began utilizing a certificate of deposit subscription service in the third quarter of fiscal 2018. As a result, we were able to obtain \$13.8 million in certificate of deposits in the second half of fiscal 2018 through this service. The cost of these deposits is more expensive than traditional certificates of deposit because of the ability to provide the funding needed in a timely manner, but can be less costly than borrowing from the Federal Home Loan Bank or other sources. We may continue to utilize this service as a funding source when other less costly means are not able to meet our funding or liquidity requirements.

**Borrowings.** Borrowings in fiscal 2018 consisted of both short and long-term advances from the Federal Home Loan Bank (FHLB) and a note payable associated with an automobile that was paid-off in the fourth quarter. At March 31, 2018, outstanding advances from the FHLB increased \$25.0 million to \$60.6 million at March 31, 2018 compared to \$35.6 million at March 31, 2017. The increase is attributable to additional FHLB advances that were entered into to fund various loan purchases throughout the year. Already included in the FHLB advances is \$15.0 million in FHLB advances assumed in the Fraternity acquisition, of which \$10 million is to mature in fiscal 2019 and \$5.0 million that matured in fiscal 2018 and were rolled over. The advances assumed from Fraternity were originally longer-term borrowings and carried higher contractual rates of interest varying from 3.4% to 4.3%. As a result of the higher stated rates, the Company recorded a discount of \$794,000 when accounting for the borrowings at fair value upon acquisition. At March 31, 2018, the remaining discount is \$103,000. The accretion of this discount offsets the higher contractual rate on these borrowings.

At March 31, 2018, \$26.0 million of the total advances are considered short-term and mature in less than one year, while the remaining \$34.6 million in advances are considered long-term and mature in more than one year. Included in long-term advances is \$11.6 million in advances that mature on a quarterly basis; however, they are associated with

several cash flow hedge transactions and will be continuously renewed over the expected life of the hedged transactions. The hedge transactions currently have an average life of 6.3 years. Excluding the advances associated with the hedge transactions, the longest outstanding borrowing is for \$3.0 million and matures in August 2021.

The FHLB borrowings provide an alternative means to support the cash outflow needed to fund new loan originations in coordination with deposit growth. FHLB borrowings can provide a less expensive means to support cash outflow when compared to selling higher yielding investment securities. These obligations are secured by our residential and home equity loan portfolios. At March 31, 2018, we had the ability to borrow approximately \$68.3 million in additional funds from the FHLB, subject to our pledging sufficient assets. These obligations will be repaid as our cash position strengthens.

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**Equity.** Total equity decreased \$5.7 million, or 9.6%, to \$54.1 million at March 31, 2018 from \$59.8 million at March 31, 2017. The change in equity is primarily attributable the \$6.0 million loss reported for fiscal 2018 along with a \$510,000 decline in accumulated other comprehensive loss associated with the decrease in the fair value of the investment portfolio. The fair value of the investment portfolio declined as a result of the increase in interest rates that occurred over the year, but more so during our fourth quarter. The decrease was partially offset by a \$457,000 increase in additional paid in capital resulting from the expense derived from equity awards granted in prior periods and the allocation of 14,812 shares of common stock under the Employee Stock Ownership Program. The Company's book value per common share was \$15.87 at March 31, 2018 compared to \$17.53 at March 31, 2017. At March 31, 2018, the Bank remains "well capitalized" as defined under federal regulations.

**Comparison of Results of Operations for the Years Ended March 31, 2018 and March 31, 2017**

**General.** Net loss for the fiscal year ended March 31, 2018 was \$6.0 million, or \$1.90 per common share, compared to a net loss of \$929,000, or \$0.29 per common share for the fiscal year ending March 31, 2017. The loss in fiscal 2018 was a result of the increase in tax expense relating two separate events. The first event dealt with the passage of the *Tax Cuts and Job Act* (the "Tax Act") that was signed into law on December 22, 2017. The Tax Act amended the Internal Revenue Code to reduce income tax rates and modify policies, credits, and deductions for individuals and businesses. For businesses, the Tax Act reduced the federal corporate income tax rate from a maximum 35 percent to a flat 21 percent tax rate. As a result, our net deferred tax assets of \$7.5 million at that time, which was based upon a 34 percent corporate tax rate, had to be re-evaluated to reflect the new tax rate of 21 percent. This non-cash adjustment was \$2.3 million and is recorded through income tax expense. The second event occurred during our fourth quarter and included the establishment of a full valuation allowance on the remaining portion of our net deferred tax assets of \$5.8 million. The valuation allowance determination was based upon the fact the Company has experienced cumulative losses for three consecutive years.

Pre-tax income for fiscal 2018, however, was \$2.0 million compared to a loss of \$1.7 million for fiscal 2017; a period-over-period increase of \$3.7 million. The increase in pre-tax income is attributable to a \$602,000 increase in net interest income, a \$1.8 million decrease in the provision for loan losses, a \$942,000 increase in non-interest revenue, and a \$326,000 decrease in non-interest expense.

**Net Interest Income.** Net interest income before provision for loan losses increased \$602,000, or 4.3%, to \$14.5 million for the year ended March 31, 2018 compared to \$13.9 million for the year ended March 31, 2017. The increase in net interest income was due to a \$1.3 million increase in interest revenue, partially offset by a \$716,000 increase in interest expense. The increase in interest revenue was due to an increase in the average balance of interest-earning assets, particularly higher yielding loans, as well as an increase in average yield on interest-earning assets. The average balance of interest-earning assets increased \$17.4 million, or 3.8%, during the fiscal year ended March 31, 2018 compared to the same period in fiscal 2017, while the average yield increased 14 basis points from 3.67% to 3.81% over that same period. The average balances increased period-over-period due in part to the

acquisition of Fraternity, which occurred in May 2016, and the realization of having those earning assets for a full year in fiscal 2018. Over this same period, the Bank was also able to increase the average balance of higher interest-earning assets, particularly loans, both organically and through loan purchases.

Partially offsetting the increase in interest revenue was a \$716,000 increase in interest expense for the fiscal year ended March 31, 2018 compared to the same period a year ago. This increase was due to the growth in the average balance of interest-bearing liabilities, particularly higher yielding borrowings, as well as an increase in the average cost of interest-bearing liabilities. The average balance of interest-bearing liabilities increased \$11.7 million, or 2.9%, for the fiscal 2018 year compared to the same period in fiscal 2017, while the average cost increased 15 basis points to 0.85% from 0.70%. The increase in interest-bearing liabilities was impacted by the growth in borrowings that were used to help in funding a growing loan portfolio and a decreasing deposit base. Despite the increase in interest expense, our net interest rate spread only decreased 1 basis point from 2.97% to 2.96% for the comparable periods.

**Interest Revenue.** Interest revenue increased \$1.3 million, or 7.9% to \$18.1 million for the year ended March 31, 2018, compared to \$16.7 million for the year ended March 31, 2017. The increase resulted from increases in interest and fees on loans and interest revenue earned on investment securities, partially offset by a decrease in revenue from federal funds sold and other bank deposits.

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Interest and fees on loans increased \$1.3 million, or 8.5%, to \$16.9 million for the twelve months ended December 31, 2018, compared to \$14.8 million for the same period a year ago. The increase in interest and fees on loans is due to a \$47.9 million increase in the average balance of net loans from \$314.5 million to \$362.4 million period-over-period. The increase in average loans is attributable to having the loans acquired in the Fraternity acquisition for a full twelve months, as well as organic growth generated by our commercial lending area and strategic loan purchases. Partially offsetting the revenue derived from an increase in the average balance of loans is a 28-basis point decline in the average yield earned on loans from 4.72% for the year ended March 31, 2017 to 4.44% for the year ended March 31, 2018. The decline in yield is a result of the extended low interest rate environment and the competitive pressure relating to pricing.

Interest revenue on investment securities increased \$120,000 to \$1.9 million for the year ended March 31, 2018 from \$1.7 million for the year ended March 31, 2017. The average balance of investment securities decreased by \$1.2 million, or 4.6%, to \$93.2 million for the year ended March 31, 2018 from \$94.4 million for the same period last year, while the average yield increased 15 basis points to 1.99% from 1.84% for the same two periods. The largest decrease in investment securities was in mortgage-backed securities, which decreased \$1.0 million to \$70.4 million for the year ended March 31, 2018 from \$71.4 million for the same period last year. The average balance of other investment securities remained relatively flat year-over-year, only decreasing \$149,000 during this period. The decrease in average investments is attributable to funding both organic loans and loan purchases throughout the year and providing liquidity associated with a decreasing deposit base. The decline in average investments is partially offset by the securities acquired in the Fraternity acquisition, along with utilizing the excess cash acquired in the Fraternity acquisition to purchase new securities in the second half of fiscal 2017. Investment balances have been declining since that time due to the need to provide liquidity to fund loan growth and a declining deposit base.

**Interest Expense.** Interest expense increased \$716,000, or 24.9%, to \$3.6 million for the year ended March 31, 2018 compared to \$2.9 million for the same period in fiscal 2017. The primary reason for this increase is due to the increase in the average balance and cost of borrowings, and to a lesser extent the increase in the cost of interest-bearing deposits, partially offset by a decrease in the average balance of those same deposits. For the year ended March 31, 2018, average interest-bearing borrowings were \$48.5 million compared to an average balance of \$26.1 million for the same period a year ago. The borrowings consisted of advances from the Federal Home Loan Bank and have been utilized to help with funding a growing loan portfolio and a declining deposit base over fiscal 2018. At March 31, 2018, the Bank had \$60.6 million in outstanding advances from the FHLB, including \$13.0 million in borrowings assumed through the Fraternity and Fairmount acquisitions that will all mature prior to November 2018. Overall borrowings carried an average rate of 1.55% for the year ended March 31, 2018 compared to 1.04% for the year ended March 31, 2017. Borrowing from the FHLB can be a more cost-effective means to obtain funds if deposits are not growing compared to selling investment securities that are earning a higher yield.

The average balance of interest-bearing deposits decreased \$10.7 million to \$372.4 million for the year ended March 31, 2018 from \$383.1 million for the year ended March 31, 2017. The average cost of deposits though increased from 0.68% to 0.76% for those same periods. We have begun to increase the rates on a portion of our deposit products and run various deposit promotions as the demand for deposits is becoming more competitive in the marketplace. During the second quarter of fiscal 2018 and last quarter of fiscal 2017, we began to run a money market promotion with a 6-month promotional rate as a means to attract core deposits. As a result, the average cost associated with money

market accounts increased from 0.37% to 0.53% for the years ended March 31, 2017 and 2018, respectively.

For the year ended March 31, 2018, the average interest-bearing deposit balances increased or declined slightly for all types of deposits, except certificates of deposits, when compared to the same period last year. These increases are a result of the Fraternity acquisition, as well as our cash management efforts as it relates to our commercial customers and promotional efforts to raise funds for new loan growth. We remain focused on changing the mix of our deposit portfolio by maintaining our maturing certificates of deposits and growing lower cost core deposits, including savings, interest-bearing checking and money market accounts. The average balance of core interest-bearing deposits increased \$6.6 million, or 5.4%, to \$130.1 million for fiscal 2018 compared to \$123.4 million for fiscal 2017. The average balance of time deposits, however, decreased \$17.4 million, or 6.7%, to \$242.3 million for fiscal 2018 compared to \$259.7 million for fiscal 2017. The decrease in time deposits is related to the competitive interest rate market, as well as the decrease in our customer base that is attributable to an aging demographic. To compensate for this decline, the Company entered into a contract and began utilizing a certificate of deposit subscription service in the third quarter of fiscal 2018. As a result, we have been able to obtain \$13.8 million in certificate of deposits in the second half of fiscal 2018 through this service. The cost of these deposits is more expensive than traditional certificates of deposit because of the ability to provide the funding needed in a timely manner, but can be less costly than borrowing from the Federal Home Loan Bank or other source. We will continue to utilize this service as a funding source when other less costly means are not able to meet our funding requirements.

Noninterest-bearing deposits allow us to fund growth in interest-earning assets at the lowest minimal cost. Average noninterest-bearing deposits increased \$5.2 million, or 21.7%, to \$29.3 million for the year ended March 31, 2018, compared to \$24.1 million for the year ended March 31, 2017. This increase resulted from the efforts of our cash management personnel and commercial loan officers working with commercial clients to move their deposit relationship to Hamilton Bank and the acquisition of Fraternity.

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**Average Balances and Yields.** The following table presents information regarding average balances of assets and liabilities, the total dollar amounts of interest revenue from average interest-earning assets, the dollar amounts of interest expense on average interest-bearing liabilities, and the resulting annualized average yields and costs. The yields and costs for the periods indicated are derived by dividing interest revenue or interest expense by the average balances of assets or liabilities, respectively, for the periods presented. Average balances have been calculated using average daily balances. No tax-equivalent adjustments were made. Nonaccrual loans have been included in the table as loans carrying a zero yield.

|   | Year Ended March 31,<br>(dollars in thousands) |          |                |                    |          |                |
|---|--|----------|----------------|--------------------|----------|----------------|
|   | 2018   |          |                | 2017               |          |                |
|   | Average<br>Balance                             | Interest | Yield/<br>Cost | Average<br>Balance | Interest | Yield/<br>Cost |
| <b>Interest-earning assets:</b>   |  |          |                |                    |          |                |
| Cash and cash equivalents   | \$18,895                                       | \$135    | 0.71%          | \$48,207           | \$190    | 0.39%          |
| Investment securities (1)   | 22,804   | 609      | 2.67%          | 22,953             | 553      | 2.41%          |
| Mortgage-backed securities  | 70,434   | 1,247    | 1.77%          | 71,448             | 1,183    | 1.66%          |
| Loans receivable, net (2)   | 362,355  | 16,089   | 4.44%          | 314,473            | 14,836   | 4.72%          |
| Total interest-earning assets   | 474,488  | 18,080   | 3.81%          | 457,081            | 16,762   | 3.67%          |
| Noninterest-earning assets  | 42,820   |          |                | 40,634             |          |                |
| Total assets  | \$517,308                                      |          |                | \$497,715          |          |                |
| <b>Interest-bearing liabilities:</b>                                    |  |          |                |                    |          |                |
| Certificates of deposit   | \$242,328                                      | \$2,454  | 1.01%          | \$259,721          | \$2,305  | 0.89%          |
| Money Market  | 60,589   | 320      | 0.53%          | 61,568             | 225      | 0.37%          |
| Statement savings   | 43,408   | 54       | 0.12%          | 43,527             | 65       | 0.15%          |
| NOW accounts  | 26,094   | 9        | 0.03%          | 18,333             | 5        | 0.03%          |
| Total interest-bearing deposits   | 372,419  | 2,837    | 0.76%          | 383,149            | 2,600    | 0.68%          |
| Borrowings  | 48,525   | 750      | 1.55%          | 26,090             | 271      | 1.04%          |
| Total interest-bearing liabilities                                      | 420,944  | 3,587    | 0.85%          | 409,239            | 2,871    | 0.70%          |
| <b>Noninterest-bearing liabilities and equity:</b>                      |  |          |                |                    |          |                |
| Noninterest-bearing deposits  | 29,306   |          |                | 24,078             |          |                |
| Other noninterest-bearing liabilities                                   | 6,313  |          |                | 5,425              |          |                |
| Total liabilities   | 456,563  |          |                | 438,742            |          |                |
| Total shareholders' equity  | 60,745   |          |                | 58,973             |          |                |
| Total liabilities and shareholders' equity                              | \$517,308                                      |          |                | \$497,715          |          |                |
| Net interest income   |  | \$14,493 |                |                    | \$13,891 |                |
| Net interest rate spread (3)  |  |          | 2.96%          |                    |          | 2.97%          |
| Net interest-earning assets (4)   | \$53,544                                       |          |                | \$47,842           |          |                |
| Net interest margin (5)   |  |          | 3.05%          |                    |          | 3.04%          |
| Average interest-earning assets to average interest-bearing liabilities | 112.72   | %        |                | 111.69             | %        |                |

- (1) Includes U.S agency and treasury securities, municipal and corporate bonds and to a much lesser extent, Federal Home Loan Bank equity securities.
- (2) Loans on non-accrual status are included in average loans carrying a zero yield.
- (3) Net interest rate spread represents the difference between the yield on average interest-earning assets and the cost of average interest-bearing liabilities.
- (4) Net interest-earning assets represents total interest-earning assets less total interest-bearing liabilities.
- (5) Net interest margin represents net interest income divided by average total interest-earning assets.



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**Rate/Volume Analysis.** The following table sets forth the effects of changing rates and volumes on our net interest income. The rate column shows the effects attributable to changes in rate (changes in rate multiplied by prior volume). The volume column shows the effects attributable to changes in volume (changes in volume multiplied by prior rate). The net column represents the sum of the prior columns. For purposes of this table, changes attributable to changes in both rate and volume that cannot be segregated have been allocated proportionately based on the changes due to rate and the changes due to volume.

|   | <b>2018 Compared to 2017</b>   |             |            |
|---|--------------------------------|-------------|------------|
|   | <b>Increase (Decrease) Due</b> |             |            |
|   | <b>to</b>                      |             |            |
|   | <b>Volume</b>                  | <b>Rate</b> | <b>Net</b> |
|   | <b>(In thousands)</b>          |             |            |
| <b><u>Interest-earning assets:</u></b>      |                                |             |            |
| Cash and cash equivalents                   | \$(114 )                       | \$59        | \$(55 )    |
| Investment securities                       | (4 )                           | 60          | 56         |
| Mortgage-backed securities                  | (17 )                          | 81          | 64         |
| Loans receivable                            | 2,260                          | (1,007)     | 1,253      |
| <br>  |                                |             |            |
| Total interest-earning assets               | 2,125                          | (807 )      | 1,318      |
| <br>  |                                |             |            |
| <b><u>Interest-bearing liabilities:</u></b> |                                |             |            |
| Certificates of Deposit                     | (155 )                         | 304         | 149        |
| Money Market                                | (4 )                           | 99          | 95         |
| Statement savings                           | (0 )                           | (11 )       | (11 )      |
| NOW accounts                                | 2                              | 2           | 4          |
| Borrowings                                  | 233                            | 246         | 479        |
| <br>  |                                |             |            |
| Total interest-bearing liabilities          | 77                             | 639         | 716        |
| <br>  |                                |             |            |
| Change in net interest income               | \$2,048                        | \$(1,446)   | \$602      |

**Provision for Loan Losses.** We establish provisions for loan losses that are charged to operations in order to maintain the allowance for loan losses at a level believed, to the best of management's knowledge, to cover all known and inherent losses in the portfolio both probable and reasonable to estimate at each reporting date. There was \$1.6 million charged to the provision for loan losses for the fiscal year ending March 31, 2018 compared to a provision for loan losses of \$3.4 million for the fiscal year ending March 31, 2017. The Company recorded a lower provision during fiscal 2018 compared to fiscal 2017 because of much lower net charge-offs that totaled \$948,000 and \$2.9 million, respectively. The more significant charge-offs for fiscal 2018 included \$379,000 associated with our commercial lease portfolio, \$244,000 relating to one commercial real estate relationship that has been a continued problem asset with prior charge-offs, and \$262,000 associated with one residential investor relationship. The remaining balance of the provision for loan losses for fiscal 2018 is primarily related to the overall growth within the loan portfolio generated organically and through various loan purchases throughout the fiscal year.

The allowance for loan losses was \$2.8 million, or 39.4% of non-performing loans at March 31, 2018 compared to \$2.2 million, or 94.5% of non-performing loans at March 31, 2017. The decrease in the percentage is a result of a \$4.8 million increase in non-performing loans as compared to the period ending March 31, 2017. The increase in non-performing loans is primarily due to one commercial real estate relationship with a book value of \$3.2 million that was placed on nonaccrual in the second quarter and a group of residential investor loans totaling \$600 thousand that were placed on nonaccrual at the end of the third quarter. Approximately \$262 thousand has been charged-off in relation to the residential investor loans, while there was no impairment associated with the commercial real estate loan based upon the most recent collateral value of the property. In addition, there is approximately \$1.2 million in loans that are 90 days past due and accruing and classified as non-performing loans. These loans continue to make payments and we are recognizing the income, however, they have reached their maturity and are in the process of being extended or renewed. Our credit department is diligently working to obtain the necessary information from the borrower that is needed to complete this process. If these loan items were excluded, the allowance for loan losses as a percentage of non-performing loans at March 31, 2018 would be 86.2%.

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During the year ended March 31, 2018, loan charge offs totaled \$975,000 with recoveries of \$27,000, compared to \$3.0 million in charge offs and \$51,000 in recoveries during the year ended March 31, 2017. The significant charge-offs in the prior year were related to two specific events, including one commercial real estate relationship that resulted in \$1.1 million in charge-offs and the sale of a pool of residential investor loans that resulted in \$1.6 million in charge-offs. During fiscal year 2018 and into fiscal 2019, we expect that we will continue our emphasis in growing commercial real estate and commercial business loans, which have higher interest rates than one-to-four family mortgage loans, but are generally considered to bear higher risk than one-to four-family mortgage loans. Such growth could contribute to higher provisions going forward.

**Noninterest Revenue.** Noninterest revenue decreased \$942,000, or 89.3%, to \$2.0 million for the year ended March 31, 2018 compared to \$1.1 million for the year ended March 31, 2017. The following table outlines the changes in components of noninterest revenue for the twelve-month periods.

|   | Years Ended 31,    |                    | \$ Change        | % Change    |
|---|--------------------|--------------------|------------------|-------------|
|   | 2018               | 2017               |                  |             |
| Service charges                               | \$459,688          | \$420,234          | \$39,454         | 9.4         |
| (Loss) gain on sale of investment securities  | (2,354 )           | 23,720             | (26,074 )        | (109.9 )    |
| Gain on sale of loans held for sale           | -                  | 23,087             | (23,087 )        | (100.0 )    |
| Gain (loss) on sale of property and equipment | 97,604             | (5,046 )           | 102,650          | (2,034.3)   |
| Earnings on bank-owned life insurance (BOLI)  | 484,030            | 485,400            | (1,370 )         | (0.3 )      |
| Earnings on death benefit from BOLI           | 834,610            | -                  | 834,610          | N/A         |
| Other fees and commissions                    | 122,770            | 107,152            | 15,618           | 14.6        |
| <b>Total noninterest revenue</b>              | <b>\$1,996,348</b> | <b>\$1,054,547</b> | <b>\$941,801</b> | <b>89.3</b> |

Noninterest revenue was impacted during the fiscal year ended March 31, 2018 by increases in service charges, gain on sale of property and equipment, and earnings on death benefit from BOLI, partially offset by decreases in gain on sale of investments and loans held for sale.

Service charges associated with retail and commercial deposit products increased \$39,000, or 9.4% during the twelve months ended March 31, 2018 compared to the same period a year ago due to a \$13.0 million increase in our average checking accounts period-over-period. Management is continually focused on growing core deposits, particularly checking accounts, which typically generate more service fee income. We continue to review and evaluate our retail fee structure on transactional accounts. Customers, however, have become more cost conscious of fees and better manage their deposit relationship with the Bank.

The \$98,000 gain on sale of property and equipment for fiscal 2018 is related to the December 2017 sale of our Pigtown branch in Baltimore City at a gain of \$213,000, net of various furniture and equipment that was associated

with the property that was also disposed, partially offset by \$115,000 loss pertaining to the write-down or disposal of leasehold improvements associated with our former or legacy Cockeyesville branch. The Pigtown branch was relocated within the same community, but to a smaller, more efficient space that will provide operational cost savings.

The Company received gross proceeds of approximately \$2.1 million in relation to death benefits under our BOLI policies due to the sudden and unexpected passing of an employee during the fourth quarter of fiscal 2018. After netting out \$1.3 million associated with the cash surrender value of the policies, the Company was able to recognize non-interest revenue of \$835,000. The normal earnings on BOLI remained relatively flat year-over-year despite an increase in average balances associated with the Fraternity acquisition because of the offsetting decrease in the rate earned on the outstanding BOLI policies, else revenue would have been higher. The revenue associated with both the death benefits and normal earnings are currently nontaxable for federal and state income tax purposes.

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Offsetting the increases in noninterest revenue for fiscal 2018 was a decrease in gain on the sale of loans held for sale. Gain on sale of loans held for sale represents revenue earned on loans sold in the secondary market at a premium. Over the past several years, we typically sold our newly originated residential mortgage loans in the secondary market to better manage interest rate risk in a rising rate environment. During the second half of fiscal 2017 and throughout fiscal 2018, however, the Company began to hold in portfolio our residential loan originations to partially offset the increased run-off associated with this loan segment. Consequently, there were no loans sold during the year ended March 31, 2018 compared to the same period last year in which several loans were sold at a gain of \$23,000. We do plan to sell residential mortgage loans again beginning in fiscal 2019.

Other fees and commissions include loan fees charged to customers, merchant credit card fees, and other smaller fees. The increase with respect to the twelve months ended March 31, 2018 compared to twelve months ended March 31, 2017, is primarily related to merchant credit services and a \$35,000 charge in the prior year relating to the disposal of an equity position in a limited liability company that assisted us with the sale of residential mortgages into the secondary market. Loan fees include various charges to customers for loan applications, processing, and/or extensions. Loan fees for fiscal 2018 declined \$46,000 to \$56,000, compared to \$100,000 for fiscal 2017.

Gains on investment securities are also reported as noninterest revenue. During fiscal 2018 we sold investment securities with a book value of \$11.6 million and recognized a loss of \$2,000 for the year ended March 31, 2018. For the year ended March 31, 2017, investment securities with a book value of \$4.3 million were sold and a gain of \$24,000 was recognized.

**Noninterest Expense.** Noninterest expense decreased \$326,000, or 2.5%, to \$12.9 million for the year ended March 31, 2018 compared to \$13.2 million for the year ended March 31, 2017. The following table outlines the changes in noninterest expense for those periods.

|   | Years Ended March 31, |             | \$ Change | % Change |
|---|-----------------------|-------------|-----------|----------|
|   | 2018                  | 2017        |           |          |
| Salaries and benefits                     | \$7,268,507           | \$6,756,044 | \$512,463 | 7.6      |
| Occupancy                                 | 1,045,589             | 984,767     | 60,822    | 6.2      |
| Advertising                               | 86,865                | 122,093     | (35,228 ) | (28.9 )  |
| Furniture and equipment                   | 343,624               | 377,232     | (33,608 ) | (8.9 )   |
| Data processing                           | 716,458               | 777,554     | (61,096 ) | (7.9 )   |
| Legal services                            | 491,900               | 291,550     | 200,350   | 68.7     |
| Other professional services               | 851,660               | 1,046,450   | (194,790) | (18.6 )  |
| Merger related expenses                   | -                     | 219,417     | (219,417) | (100.0 ) |
| Branch consolidation expense              | -                     | 494,977     | (494,977) | (100.0 ) |
| Deposit insurance premiums                | 324,325               | 318,132     | 6,193     | 1.9      |
| Foreclosed real estate expense and losses | 44,197                | 7,468       | 36,729    | 491.8    |
| Other operating                           | 1,737,727             | 1,841,144   | (103,417) | (5.6 )   |

|                           |              |              |             |        |
|---------------------------|--------------|--------------|-------------|--------|
| Total noninterest expense | \$12,910,852 | \$13,236,828 | \$(325,976) | (2.5 ) |
|---------------------------|--------------|--------------|-------------|--------|

The decline in noninterest expense is primarily the result of non-recurring costs incurred in the prior year period ended March 31, 2017, including \$219,000 in merger related expenses associated with the completion of our most recent acquisition of Fraternity and \$437,000 in costs relating to the closing of one of our branch locations due to branch overlap from that same acquisition. Merger related expenses include fees paid to attorneys, investment bankers and accountants, data conversion, as well as other related costs. Excluding the acquisition and branch consolidation expense, overall operating expenses for the comparative periods has increased slightly as a result of a growing loan portfolio and revenue base. The elimination of acquisition related costs and the economies of scale achieved through those same acquisitions is reflected in the improvement of our efficiency ratio from 83.9% for the year ended March 31, 2017 to 78.5% for the year ended March 31, 2018. This improvement is also in part due to the income realized in the current year with respect to the BOLI proceeds. We are realizing the benefit of operating as a larger financial institution and the ability to offset expenses against greater revenue.

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Certain noninterest expenses, including furniture and equipment, data processing, and other operating expenses, declined as a result of management's continued focus on reducing costs where applicable. Some of these reductions have been obtained through the review or negotiation of vendor contracts, analysis of alternative sources, and more efficient means. Advertising expense decreased because we hired a full-time marketing director versus outsourcing to a third-party vendor. Federal deposit insurance premiums were lower due to a decrease in the average rate assessed by the Federal Deposit Insurance Corporation, the government agency that insures deposits, while other professional services decreased in part due to the end of our contractual obligation under a consulting and non-compete agreement with one of the former Fraternity executives.

The largest increase in noninterest expenses for the twelve-month period-over-period was in salaries and benefits, which increased \$512,000. During the year ended March 31, 2018, the Company made strategic new hires that are focused on branch efficiency and new products. In addition, annual increases were given and bonuses awarded in fiscal 2018 that were not awarded in fiscal 2017. Also included in salaries and benefits for fiscal 2018 and 2017, is \$322,000 and \$317,000 in expense, respectively, relating to equity awards granted to officers under the Company's Equity Incentive Plan. The equity awards provide for management to have an interest in the performance of the company and share in the benefit of an increase in shareholder value. Similarly, other operating expenses for the same periods include \$139,000 and \$127,000 in expense, respectively, associated with equity awards granted to directors.

Legal expense for the twelve months ended March 31, 2018 increased over the same period a year ago. The increase in legal costs is due in part to management's engagement of counsel to assist with our charter conversion from a federal savings bank to a Maryland commercial bank. The charter conversion was approved and effective December 21, 2017. The charter conversion should reduce regulatory costs going forward. In addition, counsel was sought to assist with compiling and reviewing agreements associated with loan portfolio purchases throughout the year, as well as advise on the relocation of our Ellicott City and Pigtown branches and other compliance issues. Counsel also continues to assist with the collection and foreclosure process associated with problem loans, as well as consult on how to proceed with certain borrowers.

The increase in occupancy expense is primarily related to the relocation of our Ellicott City branch within the same geographic area of Howard County during the second quarter of fiscal 2018. Due to the timing and ability to move into the new location, the Bank had to pay rent expense on both the current and new property for a one-month period. In addition, there were costs incurred in the period associated with the relocation that were not capitalized. The new branch location in Ellicott City opened in July 2017. Subsequently, in March 2018 we also relocated our Pigtown branch located in Baltimore City to a much smaller space located on the same block. As with Ellicott City, there were costs incurred that related to the relocation that were not capitalized. Both relocations were to smaller, more efficient spaces that will provide operational cost savings.

Foreclosed real estate expense also increased year-over-year due to a \$32,000 write-down of one of the Bank's foreclosed real estate properties during the third quarter. This write-down was based upon a new appraisal obtained on the property. The remainder of foreclosed real estate expense, or \$5,000 increase, is associated with the property taxes paid on that same property.

**Income Tax Expense.** We recorded tax expense of \$8.1 million for the year ended March 31, 2018 after pre-tax income of \$2.0 million, compared to a tax benefit of \$758,000 for the year ended March 31, 2017 after a pre-tax loss of \$1.7 million. The effective income tax rate for the year ending March 31, 2018 was 402.0% compared to a negative effective tax rate of 44.9% for the year ending March 31, 2017. In fiscal 2018 the higher tax expense was a result of an adjustment associated with the Tax Act and the establishment of a valuation allowance relating to the Company's net deferred tax assets and, to a lesser extent, tax expense associated with the Company's pre-tax income of \$2.0 million. The fiscal 2017 tax benefit was due to the pre-tax loss that was recorded along with nontaxable income associated with bank-owned life insurance and certain tax-exempt municipal securities.

At March 31, 2018, the Company did not report any net deferred tax asset compared to \$8.0 million at March 31, 2017. The change is primarily related to the establishment of a net deferred tax asset valuation allowance and an adjustment that resulted from the passage of the Tax Act. The Tax Act, which was signed into law on December 22, 2017, amended the Internal Revenue Code to reduce income tax rates and modify policies, credits, and deductions for individuals and businesses. For businesses, the Tax Act reduces the federal corporate income tax rate from a maximum 35 percent to a flat 21 percent tax rate. As a result, our net deferred tax assets of \$7.5 million at that time, which were based upon a 34 percent corporate tax rate, had to be re-evaluated to reflect the new tax rate of 21 percent. This non-cash adjustment was \$2.3 million and was recorded through income tax expense. Based on the information available and our current interpretation of the Tax Act, the Company has made reasonable estimates of the impact from the reduction in the corporate tax rate on the re-measurement of applicable deferred tax assets and liabilities. However, certain deferred tax assets and liabilities will continue to be evaluated in the context of the Tax Act through the date of the filing of our March 31, 2018 federal income tax return, and may change as a result of evolving management interpretations, elections, and assumptions, as well as new guidance that may be issued by the Internal Revenue Service. Management expects to complete its analysis within the measurement period in accordance with *Staff Accounting Bulletin (SAB) No. 118*.



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In accordance with Accounting Standards Codification (ASC) 740, *Accounting for Income Taxes*, at March 31, 2018, the Company assessed whether the deferred tax assets are more likely than not to be realized based on an evaluative process that considers all available positive and negative evidence. As part of this evaluative process, management considered the following sources of taxable income: 1.) taxable income in prior carryback years; 2.) the future reversals of taxable temporary differences; 3.) tax planning strategies; and 4.) future taxable income exclusive of reversing temporary differences and carryforwards. In making a conclusion, management evaluated all the available positive and negative evidence impacting these sources of taxable income. The first three options are more quantifiable and verifiable; however, management concluded they were not viable sources of taxable income. As such, the positive evidence that was most heavily relied upon, but the most subjective, was future taxable income exclusive of reversing temporary differences and carryforwards. The Company is in a three-year cumulative loss position which creates negative evidence and because this evidence is considered significant, management concluded that there was more negative evidence than positive evidence and therefore, it is more likely than not that the Company will be unable to generate sufficient taxable income in the foreseeable future to fully utilize the net deferred tax assets. Thus, a full valuation allowance of \$5.8 million on all the net deferred tax assets was established at March 31, 2018. The establishment of a valuation allowance on our deferred tax assets for financial reporting purposes does not affect how the net operating loss carryforwards may be utilized on our subsequent income tax returns.

## **Risk Management**

Managing risk is an essential part of successfully operating a financial institution. We have a comprehensive Enterprise Risk Management (ERM) program in place that addresses risks within the Company. The ERM program and the associated risks are updated and reviewed quarterly and presented to the Risk Committee which has oversight of the program. Risks are rated compared to the Company's risk appetite and action plans are developed by management for those risks outside of the board established parameters. Once the Risk Committee approves the ERM program, the ERM program is presented to the full board. Our most significant types of risk are economic risk, regulatory risk, and compliance risk.

Our three most prominent forms of economic risk are credit risk, interest rate risk and market risk. Our primary credit risk is the risk of defaults in our loan portfolio that result from the inability or unwillingness of borrowers to make contractually required payments. To a lesser extent, we also have credit risk related to the risk of defaults in our investment securities portfolio. Interest rate risk is the potential reduction of interest income or an increase interest expense because of changes in interest rates. Market risk arises from fluctuations in interest rates that may result in changes in the values of financial instruments, such as available-for-sale securities that are accounted for on a mark-to-market basis.

Regulatory and compliance risk involves our ability to effectively adapt to, and comply with, changes in the regulatory environment for financial institutions. We are subject to the regulations of various government agencies. These regulations may change significantly from period to period. We also undergo periodic examinations by

regulatory agencies that may subject us to further changes with respect to asset valuations and classifications, amounts required for the allowance for loan losses, and operating restrictions resulting from the regulators' judgment based on information available to them at the time of their examination.

Other risks that we face are operational risks, liquidity risk and reputation risk. Operational risks include risks related to fraud, processing errors, technology and disaster recovery. Liquidity risk is the possible inability to fund obligations to depositors, lenders or borrowers due to unforeseen circumstances. Reputation risk is the risk that negative publicity or press, whether true or not, could cause a decline in our customer base or revenue.

### **Credit Risk Management**

Our strategy for credit risk management focuses on having well-defined credit policies and uniform underwriting criteria and providing prompt attention to potential problem loans. Our loan approval process is described in Item 1. "Business", under the heading "Lending Activities—Loan Approval Procedures and Authority".

We have a loan monitoring system in place with dedicated staff that ensures all required loan information and documentation is obtained at the time a loan is originated and that such information is updated as required by our underwriting policies. This loan monitoring system, which tracks loans originated by the Bank, as well as loan participations and purchased loans, is integrated with our general ledger system, which allows management to monitor loan payment history and changes in loan status on a real-time basis. We have established a formal allowance for loan loss and loan delinquency committee to address non-performing and delinquent loans. This committee currently meets on a monthly basis. We also have a Special Assets manager to oversee problem credits.

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**Collection Procedures.** When a residential mortgage borrower fails to make required payments on a loan, we take a number of steps to induce the borrower to cure the delinquency and restore the loan to current status. With respect to residential real estate loans, we generally send a written notice of non-payment to the borrower 15 days after a loan is first past due. When a loan reaches 60 days past due a “Notice of Intent” to foreclose letter is prepared and sent to the borrower. And finally, when a loan becomes 90 days past due, the loan is turned over to our attorneys to ensure that further collection activities are conducted in accordance with applicable laws and regulations. All residential mortgage loans past due 90 days are put on non-accrual and reported to the board of directors monthly. If our attorneys do not receive a response from the borrower, or if the terms of any payment plan established are not followed, then foreclosure proceedings will be implemented. Management submits an Asset Classification Report detailing risk ratings and changes to risk ratings to the board of directors on a monthly basis.

With respect to home equity loans and lines of credit, a complete listing of all delinquent accounts is given to senior management for evaluation on a monthly basis. The data center produces and sends late charge notifications to customers that alert customers of their payment status. If the account remains past due when the next late charge notice is produced, a collection letter is sent requiring delinquent accounts to be brought current within 10 days. Failure to comply or respond to collection efforts will result in the loan being turned over to our attorneys for collection.

Commercial loan officers are responsible for the prompt follow up with borrowers who become delinquent on commercial loans. Officers determine the cause of the delinquency and work with the borrower to institute a short-term plan to eliminate the delinquency. Commercial loans that become over 30 days delinquent are reported to the Chief Lending Officer for collection. If no reasonable plan to cure a delinquency over 60-90 days is reached, the Bank will initiate legal action, repossession, foreclosure, non-accrual or charge-off. When a commercial loan becomes 75 days delinquent, the Special Asset Officer is required to re-verify all documentation, including adequate insurance coverage. Commercial loans 90 days delinquent are generally placed on non-accrual and evaluated for impairment to determine if charge-off is necessary. All loans over 90 days delinquent are reported to the board of directors monthly. All charged-off loans and subsequent recoveries are reported in aggregate on a monthly basis to the appropriate members of senior management and the Board of Directors. Prior to the extension of non-accrual status beyond six months, a request for extension must be properly executed with appropriate approval signed by the Loan Committee. At the time the loan is placed in non-accrual, the accrued, but unpaid interest is reversed against the loan account in accordance with the Bank’s non-accrual policy. A loan may not be removed from non-accrual status until the loan is paid current or, under a modification agreement, an adequate period of time has passed in which the borrower has demonstrated the ability to make payments and their cash flow supports the payment going forward. At this point, management will determine whether or not to return the loan to accrual status.

**Analysis of Nonperforming, Delinquent and Classified Assets.** Loans are generally placed on nonaccrual status when they are 90 days past due based on the contractual terms of the loan. In all cases, loans are placed on nonaccrual status at an earlier date if collection of principal or interest is considered doubtful. All interest accrued but not collected for loans that are placed on nonaccrual status are reversed against interest revenue. The interest on nonaccrual loans is accounted for on the cash basis method, until the loans qualify for return to accrual status. Loans are returned to accrual status when all the principal and interest amounts contractually due are brought current and future payments are reasonably assured. For certain nonaccrual loans, interest payments received are applied to the principal balance of

the loan.

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*Non-Performing Assets.* The table below sets forth the amounts and categories of our non-performing assets at the dates indicated.

|   | <b>At March 31,</b>           |              |              |              |              |
|---|-------------------------------|--------------|--------------|--------------|--------------|
|   | <b>2018</b>                   | <b>2017</b>  | <b>2016</b>  | <b>2015</b>  | <b>2014</b>  |
|   | <b>(Dollars in thousands)</b> |              |              |              |              |
| Non-accrual loans:  |                               |              |              |              |              |
| Real estate loans:  |                               |              |              |              |              |
| Residential   | \$864                         | \$675        | \$775        | \$628        | \$284        |
| Investor  | 362                           | 71           | 675          | 11           | 159          |
| Commercial construction   | -                             | -            | -            | 1,375        | 1,552        |
| Commercial  | 4,555                         | 1,547        | 2,717        | -            | -            |
| Commercial business loans   | 165                           | -            | 122          | 226          | 2,041        |
| Consumer loans:   |                               |              |              |              |              |
| Home equity loans and lines of credit                               | 13                            | 3            | 49           | 15           | 204          |
| Other consumer  | 5                             | 6            | 4            | -            | -            |
| <b>Total non-accrual loans</b>                                      | <b>5,964</b>                  | <b>2,302</b> | <b>4,342</b> | <b>2,255</b> | <b>4,240</b> |
| Loans delinquent 90 days or greater and still accruing:             |                               |              |              |              |              |
| Real estate loans:  |                               |              |              |              |              |
| Residential   | -                             | -            | -            | -            | -            |
| Investor  | 1,206                         | 21           | 708          | -            | -            |
| Commercial construction   | -                             | -            | -            | -            | -            |
| Commercial  | -                             | -            | -            | -            | 301          |
| Commercial business loans   | -                             | -            | -            | -            | 500          |
| Consumer loans:   |                               |              |              |              |              |
| Home equity loans and lines of credit                               | -                             | -            | -            | -            | -            |
| Other consumer  | -                             | -            | -            | -            | -            |
| <b>Total loans delinquent 90 days or greater and still accruing</b> | <b>1,206</b>                  | <b>21</b>    | <b>708</b>   | <b>-</b>     | <b>801</b>   |
| <b>Total non-performing loans</b>                                   | <b>7,170</b>                  | <b>2,323</b> | <b>5,050</b> | <b>2,255</b> | <b>5,041</b> |
| Other real estate owned and foreclosed assets:                      |                               |              |              |              |              |
| Real estate loans:  |                               |              |              |              |              |
| Residential   | 47                            | 23           | -            | 12           | -            |
| Investor  | -                             | 37           | -            | -            | -            |
| Commercial construction   | 411                           | 443          | 443          | 443          | 664          |
| Commercial  | -                             | -            | -            | -            | -            |
| Commercial business loans   | -                             | -            | -            | -            | -            |
| Consumer loans:   |                               |              |              |              |              |
| Home equity loans and lines of credit                               | -                             | -            | -            | -            | -            |
| Other consumer  | -                             | -            | -            | -            | -            |
| <b>Total foreclosed real estate</b>                                 | <b>458</b>                    | <b>503</b>   | <b>443</b>   | <b>455</b>   | <b>664</b>   |
| <b>Total non-performing assets</b>                                  | <b>7,628</b>                  | <b>2,826</b> | <b>5,493</b> | <b>2,710</b> | <b>5,705</b> |

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|   |         |         |         |         |         |
|---|---------|---------|---------|---------|---------|
| Performing troubled debt restructurings                                 | 1,836   | 1,906   | 2,105   | 5,339   | 1,538   |
| Total non-performing assets and performing troubled debt restructurings | \$9,464 | \$4,732 | \$7,598 | \$8,049 | \$7,243 |

Ratios:

|                                       |        |        |        |        |        |
|---------------------------------------|--------|--------|--------|--------|--------|
| Non-performing loans to total loans   | 1.84 % | 0.69 % | 2.27 % | 1.41 % | 3.48 % |
| Non-performing assets to total assets | 1.45 % | 0.55 % | 1.40 % | 0.93 % | 1.88 % |

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Non-performing loans totaled \$7.2 million at March 31, 2018 compared to \$2.3 million at March 31, 2017, an increase of \$4.9 million. The increase in fiscal 2018 is primarily due to one commercial real estate relationship with a book value of \$3.2 million that was placed on nonaccrual in the second quarter and a group of residential investor loans to one borrower totaling \$600 thousand that were placed on nonaccrual at the end of the third quarter.

Non-performing assets to total assets increased to 1.45% at March 31, 2018 compared to 0.55% at March 31, 2017 as a result of the non-performing loans just discussed. The graph below shows the change in non-accrual loans during fiscal 2018 on a month-by-month basis as a percentage of gross loans:

Also included in nonperforming loans are accruing loans delinquent more than 90 days. At March 31, 2018 these loans consisted of investor (residential non-owner occupied) loans totaling \$1.2 million compared to \$21,000 at March 31, 2017. These loans represent loans that are on accrual status and making payments, however, such loans are 90 days past their contractual maturity date, and therefore reported as nonperforming. At March 31, 2018, these loan balances were elevated as they related to several borrowing relationships that have many smaller investor (residential non-owner occupied) loans that matured at the same time. The Bank's credit department is diligently working to obtain the necessary financial information from these borrowers so that these loans can either be renewed or extended accordingly.

Non-performing commercial real estate loans at March 31, 2018 totaled \$4.6 million and primarily consisted of two borrowing relationships. The first relationship consists of two loans within an aggregate contractual principal balance of \$3.3 million and a recorded investment balance of \$1.2 million (\$1.9 million charged-off life to date). The property consists of several commercial retail units that are a part of a multi-family complex. The loan and respective collateral is only for the commercial retail units. These loans were placed on non-accrual in October 2015 due to deteriorating cash flow, a pending lawsuit, and the inability of the borrower to make the principal payment under an existing troubled debt restructuring ("TDR") agreement. After being placed on non-accrual, the borrower continued to make the interest only payments through July 2016 at which time payments ceased. The Bank applied those funds as a principal reduction to the loans in accordance with our non-accrual policy. After payments ceased, the Bank obtained a new appraisal and had the borrower list the property for sale by an independent broker. Upon receipt of the new appraisal, which provided different valuations based upon various sale scenarios, we wrote the loan down by \$622,000 in December 2016 to the highest sale value scenario and then another write-down of \$490,000 in March 2017 to the lowest sales valuation due to limited interest in the property. In the second half of fiscal 2018, based upon our policy, we obtained a subsequent new appraisal on the property and charged-off an additional \$244,000 based upon the updated valuation. During this time, the borrower also changed sales broker and re-listed the property for sale. Management is actively exploring other options to resolve this problem credit that may or may not result in additional write-downs.

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The second commercial real estate relationship consists of one loan with a contractual principal and recorded investment balance of \$3.2 million. The loan was placed on non-accrual in the second quarter of fiscal 2018 after analysis of the borrower indicated the inability to cashflow and service the debt. The borrower at that time stopped making payments and listed the property for sale. At the time of nonaccrual, we obtained a new appraisal on the property which indicates no impairment on the loan as of March 31, 2018. The property is standard office and warehouse space located in Columbia, Maryland, which has a strong real estate market.

There were \$165,000 in non-performing commercial business loans at March 31, 2018 compared to none at March 31, 2017. The recorded book balance of \$165,000 in loans is comprised of three commercial lease loans to separate borrowers with a contractual balance of \$544,000 and charge-offs totaling \$379,000. The purpose of the loans was to provide funding to purchase medical equipment related to cosmetic surgery. Based upon the inability to generate sufficient revenue, the borrowers stopped making payments on the leases or asked for the equipment to be repossessed. All three loans are fully guaranteed by the respective borrowers. The commercial lease loans are a part of the \$15.5 million commercial lease portfolio purchased by the Bank in June 2017.

Part of the loan portfolio originally acquired in the Fairmount acquisition consisted of \$17.3 million in one-to-four family non-owner occupied (“investor”) loans. At March 31, 2018, the remaining book balance of investor loans associated with Fairmount totaled \$9.5 million, of which \$343,000 are on nonaccrual. The \$343,000 balance of nonaccrual loans is primarily associated with one borrower that has multiple investor properties located in Baltimore City. The relationship has a combined contractual balance of \$605,000 and charge-offs taken in the second half of fiscal 2018 totaling \$262,000. The remaining book balance is based upon newly received appraisals for all the properties associated with this one borrower. Management is actively working with the borrower and exploring other options to resolve this problem relationship that may or may not result in additional write-downs on some or all the properties involved.

At March 31, 2018, there is \$864,000 in owner occupied, one-to-four family residential loans that are classified as non-performing loans, all of which are classified as non-accrual, compared to \$675,000 at March 31, 2017. Non-accrual loans consist of 23 loans in total, including 7 loans that comprise \$659,000, or 76.2% of the outstanding balance. To date, the bank has charged-off \$20,000 relating to the 23 loans that are classified as non-performing within this loan segment.

Gross interest income that would have been recorded during fiscal 2018 had our non-accruing loans been current in accordance with their original terms was \$394,000.

*Troubled Debt Restructurings (“TDR”).* At March 31, 2018, Hamilton Bank had a total of \$3.3 million in TDRs, including 15 one-to-four family residential real estate loans totaling \$1.5 million, two commercial real estate loans totaling \$1.2 million, and one commercial business loan equaling \$605,000. Roughly \$1.2 million of the \$1.5 million in TDRs pertaining to one-to-four family residential real estate loans was comprised of two loans performing in



accordance with their modified terms as of March 31, 2018. The remainder was comprised of thirteen one-to-four family residential real estate loans, totaling \$313,000, that were on non-accrual.

The two commercial real estate loans totaling \$1.2 million became TDRs at the end of the second fiscal quarter of 2015 and are currently on non-accrual. These are the same loans discussed earlier under the commercial real estate non-performing loans. The loans were placed on non-accrual in October 2015 and \$1.1 million and \$244,000 in charge-offs were recorded during fiscal 2017 and 2018, respectively.

The one commercial business loan that is a TDR totals \$605,000 and is performing as agreed under its modified terms. This particular loan was on non-accrual when it was originally modified. The borrower has continued to make payments and the loan has been on accrual status now for over three years.

We had \$3.7 million of TDRs at March 31, 2017, which included \$1.6 million in one-to-four family residential real estate loans, including \$1.3 million that were performing in accordance with their modified terms, the same two commercial real estate loans equaling \$1.5 million, and the same commercial business loan totaling \$644,000 that has been performing as agreed upon based upon its modified terms.

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*Delinquent Loans.* The following table sets forth certain information regarding delinquencies in our loan portfolio. Loans 90 or more days delinquent includes loans 90 or more days past due because of maturity, but are still accruing.

|                                       | <b>60 to 89</b>               |               | <b>90 or More</b> |               | <b>Total</b>      |               |
|---------------------------------------|-------------------------------|---------------|-------------------|---------------|-------------------|---------------|
|                                       | <b>Days</b>                   |               | <b>Days</b>       |               | <b>Days</b>       |               |
|                                       | <b>Delinquent</b>             |               | <b>Delinquent</b> |               | <b>Delinquent</b> |               |
|                                       | <b>Number</b>                 | <b>Amount</b> | <b>Number</b>     | <b>Amount</b> | <b>Number</b>     | <b>Amount</b> |
|                                       | <b>(Dollars in thousands)</b> |               |                   |               |                   |               |
| <b>At March 31, 2018:</b>             |                               |               |                   |               |                   |               |
| Real estate loans:                    |                               |               |                   |               |                   |               |
| Residential                           | 4                             | \$ 307        | 7                 | \$ 284        | 11                | \$ 591        |
| Investor                              | -                             | -             | 43                | 1,568         | 43                | 1,568         |
| Commerical construction               | -                             | -             | -                 | -             | -                 | -             |
| Commercial                            | 1                             | 135           | 4                 | 4,555         | 5                 | 4,690         |
| Commercial business loans             | -                             | -             | 3                 | 165           | 3                 | 165           |
| Consumer loans:                       |                               |               |                   |               |                   |               |
| Home equity loans and lines of credit | -                             | -             | 1                 | 13            | 1                 | 13            |
| Other consumer                        | 2                             | 28            | 1                 | 5             | 3                 | 33            |
| Total loans                           | 7                             | \$ 470        | 59                | \$ 6,590      | 66                | \$ 7,060      |
| <b>At March 31, 2017:</b>             |                               |               |                   |               |                   |               |
| Real estate loans:                    |                               |               |                   |               |                   |               |
| Residential                           | 3                             | \$ 81         | 8                 | \$ 336        | 11                | \$ 417        |
| Investor                              | -                             | -             | 16                | 92            | 16                | 92            |
| Commerical construction               | -                             | -             | -                 | -             | -                 | -             |
| Commercial                            | -                             | -             | 2                 | 1,547         | 2                 | 1,547         |
| Commercial business loans             | -                             | -             | -                 | -             | -                 | -             |
| Consumer loans:                       |                               |               |                   |               |                   |               |
| Home equity loans and lines of credit | -                             | -             | -                 | -             | -                 | -             |
| Other consumer                        | -                             | -             | 1                 | 5             | 1                 | 5             |
| Total loans                           | 3                             | \$ 81         | 27                | \$ 1,980      | 30                | \$ 2,061      |
| <b>At March 31, 2016:</b>             |                               |               |                   |               |                   |               |
| Real estate loans:                    |                               |               |                   |               |                   |               |
| Residential                           | 3                             | \$ 99         | 10                | \$ 651        | 13                | \$ 750        |
| Investor                              | -                             | -             | 31                | 1,217         | 31                | 1,217         |
| Commerical construction               | -                             | -             | -                 | -             | -                 | -             |
| Commercial                            | -                             | -             | 2                 | 2,717         | 2                 | 2,717         |
| Commercial business loans             | -                             | -             | 1                 | 122           | 1                 | 122           |
| Consumer loans:                       |                               |               |                   |               |                   |               |
| Home equity loans and lines of credit | -                             | -             | 1                 | 43            | 1                 | 43            |
| Other consumer                        | -                             | -             | 1                 | 4             | 1                 | 4             |
| Total loans                           | 3                             | \$ 99         | 46                | \$ 4,754      | 49                | \$ 4,853      |
| <b>At March 31, 2015:</b>             |                               |               |                   |               |                   |               |
| Real estate loans:                    |                               |               |                   |               |                   |               |
| Residential                           | 3                             | \$ 159        | 13                | \$ 476        | 16                | \$ 635        |
| Investor                              | -                             | -             | 1                 | 11            | 1                 | 11            |

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|                                       |   |        |    |          |    |          |
|---------------------------------------|---|--------|----|----------|----|----------|
| Commerical construction               | - | -      | 1  | 1,375    | 1  | 1,375    |
| Commercial                            | - | -      | -  | -        | -  | -        |
| Commercial business loans             | 2 | 734    | 4  | 226      | 6  | 960      |
| Consumer loans:                       |   |        |    |          |    |          |
| Home equity loans and lines of credit | - | -      | 1  | 6        | 1  | 6        |
| Other consumer                        | - | -      | -  | -        | -  | -        |
| Total loans                           | 5 | \$ 893 | 20 | \$ 2,094 | 25 | \$ 2,987 |

**At March 31, 2014:**

|                                       |   |          |    |          |    |          |
|---------------------------------------|---|----------|----|----------|----|----------|
| Real estate loans:                    |   |          |    |          |    |          |
| Residential                           | - | \$ -     | 16 | \$ 283   | 16 | \$ 283   |
| Investor                              | - | -        | 2  | 159      | 2  | 159      |
| Commerical construction               | 1 | 1,242    | -  | -        | 1  | 1,242    |
| Commercial                            | - | -        | 1  | 301      | 1  | 301      |
| Commercial business loans             | 2 | 2,173    | 5  | 1,802    | 7  | 3,975    |
| Consumer loans:                       |   |          |    |          |    |          |
| Home equity loans and lines of credit | - | -        | 4  | 205      | 4  | 205      |
| Other consumer                        | - | -        | -  | -        | -  | -        |
| Total loans                           | 3 | \$ 3,415 | 28 | \$ 2,750 | 31 | \$ 6,165 |

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The increase in loans 90 or more days delinquent for fiscal 2018 as compared to fiscal 2017 was due to increases in residential investor loans, commercial real estate, and commercial business loans. The increase in residential investor loans is largely due to the \$1.2 million in loans that are reported as 90 days past due and still accruing. See the discussion of non-performing loans above for additional information regarding loans that are 90 or more days delinquent for the period ended March 31, 2018.

*Classified Assets.* Federal regulations require that each insured financial institution classify its assets on a regular basis. In addition, in connection with examinations of insured institutions, federal examiners have authority to identify problem assets and, if appropriate, classify them. There are three classifications for problem assets: “substandard,” “doubtful” and “loss”. Each is defined as follows:

**Substandard** - A substandard loan is inadequately protected by the current sound worth and paying capacity of the obligor or of the collateral pledged, if any. Substandard loans have a well-defined weakness, or weaknesses, that jeopardize the collection or liquidation of the debt. They are characterized by the distinct possibility that the Bank will sustain some loss if the deficiencies are not corrected. This will be the measurement for determining if a loan is impaired. Borrowers may exhibit recent or unexpected unprofitable operations, an inadequate debt service coverage ratio, or marginal liquidity and capitalization. These loans require more intense supervision by Bank management.

**Doubtful** - A doubtful loan has all the weaknesses inherent as a substandard loan 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. A loan classified as doubtful exhibits loss potential. However, there is still sufficient reason to permit the loan to remain on the books. A doubtful classification could reflect the deterioration of the primary source of repayment and serious doubt exists as to the quality of the secondary source of repayment.

Doubtful classifications should be used only when a distinct and known possibility of loss exists. When identified, adequate loss should be recorded for the specific assets. The entire asset should not be classified as doubtful if a partial recovery is expected, such as liquidation of the collateral or the probability of a private mortgage insurance payment is likely.

**Loss** - Loans classified as loss are considered uncollectable and of such little value that their continuance as loans is unjustified. A loss classification does not mean a loan has absolutely no value; partial recoveries may be received in the future. When loans or portions of a loan are considered a loss, it will be the policy of the Bank to write-off the amount designated as a loss. Recoveries will be treated as additions to the allowance for loan losses.

Another category, designated “special mention”, may also be established and maintained for assets which do not currently expose an insured institution to a sufficient degree of risk to warrant classification as substandard, doubtful

or loss. If a classified asset is deemed to be impaired with measurement of loss, the Bank will establish a charge-off of the loan pursuant to Accounting Standards Codification Topic 310, "Receivables."

The following table sets forth information regarding classified assets and special mention assets at March 31, 2018, 2017 and 2016.

|                                   | <b>At March 31,</b>   |             |             |
|-----------------------------------|-----------------------|-------------|-------------|
|                                   | <b>2018</b>           | <b>2017</b> | <b>2016</b> |
|                                   | <b>(In thousands)</b> |             |             |
| Classification of Assets:         |                       |             |             |
| Substandard                       | \$6,715               | \$3,447     | \$5,310     |
| Doubtful                          | -                     | -           | -           |
| Loss                              | -                     | -           | -           |
| Total Adversely Classified Assets | \$6,715               | \$3,447     | \$5,310     |
| Special Mention                   | \$7,022               | \$11,402    | \$11,969    |

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The following graph shows both special mention and substandard loans, including unfunded commitments, as a percentage of gross loans throughout fiscal 2018:

At March 31, 2018, substandard assets consisted of four commercial real estate loans totaling \$4.6 million, two of which are to the same borrower, and four commercial business loan totaling \$190,000. At that same date, there were 22 residential mortgage loans totaling \$1.4 million that were classified as substandard, along with 16 nonowner-occupied residential investor loans totaling \$505,000. The majority of the investor loans were acquired in the Fairmount transaction. Finally, there were three home equity loans totaling \$21,000, one recreational vehicle for \$19,000 and one mobile home loan equaling \$32,000 that were also classified as substandard.

At March 31, 2018, there are no loans classified as doubtful.

At March 31, 2018, special mention loans consisted of 14 one-to-four family mortgage loans totaling \$3.3 million and seven loans equaling \$297,000 that are nonowner-occupied residential investor loans. Also included in special mention loans are two commercial real estate loans totaling \$3.1 million, which are to the same borrower, and one special mention commercial business loan for \$135,000. Lastly, there are two home equity loans classified as special mention for \$111,000, along with one recreational vehicle for \$83,000 and two auto loans totaling \$14,000.

***Analysis and Determination of the Allowance for Loan Losses.*** We maintain the allowance through a provision for loan losses that we charge to income. We charge losses on loans against the allowance for loan losses when we believe the collection of loan principal is unlikely. Recoveries on loans charged-off are restored to the allowance for loan losses. The allowance for loan losses is maintained at a level believed, to the best of management's knowledge, to cover all known and inherent losses in the portfolio that are both probable and reasonable to estimate at each reporting date. Consideration is given to historical losses in conjunction with a variety of other factors including, but not limited to, current economic conditions, delinquency statistics, geographic and industry concentrations, the adequacy of the underlying collateral, the financial strength of the borrower, results of internal loan reviews and other relevant factors. This evaluation is inherently subjective as it requires material estimates that may be susceptible to significant change. We evaluate our allowance for loan losses, at a minimum, on a quarterly basis. Management modified the analysis during the quarter ended September 30, 2016 by keeping our net charge-off history as a percentage of loans, as it pertains to each loan segment, constant across all risk ratings and altering our qualitative factors either up or down based upon the respective risk rating for each loan segment. The change in methodology did not have a material impact on the amount of the allowance for loan losses at September 30, 2016 as compared to the prior methodology. We make adjustments to the external factors in the calculation during the year as deemed fit. We will continue to monitor all items involved in the allowance calculation closely. Additional information on our methodology for calculating the allowance for loan losses is described in this Item 7 above under "—Critical Accounting Policies—Allowance for Loan Losses."



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In addition, the regulatory agencies, as an integral part of their examination and review process, periodically review our loan portfolios and the related allowance for loan losses. Regulatory agencies may require us to increase the allowance for loan losses based on their judgment of information available to them at the time of their examination, thereby adversely affecting our results of operations.

We recorded a provision for loan losses of \$1.6 million for the year ended March 31, 2018 compared to a provision for loan losses of \$3.4 million for the year ended March 31, 2017. The allowance for loan losses was \$2.8 million, or 0.73% of total loans, at March 31, 2018, compared to \$2.2 million, or 0.65% of total loans, at March 31, 2017. The percentage of allowance for loan losses to total loans increased because of additional reserves that were recorded in conjunction with the overall growth of the loan portfolio and provisions associated with charge-offs that were experienced.

Our non-performing loans increased by \$4.8 million to \$7.2 million at March 31, 2018 from \$2.3 million at March 31, 2017. A large portion of the increase is related to one commercial real estate loan, with a book value of \$3.2 million that was placed on non-accrual during the second quarter of fiscal 2018, along with an increase of \$1.2 million in investor loans that are 90 days past due and still accruing. During the year ended March 31, 2018, net loan charge-offs decreased to \$948,000 compared to \$2.9 million in fiscal 2017. The decline is in large part due to certain charge-offs that were taken in the prior year, including \$1.1 million in charge-offs relating to one commercial real estate relationship and another \$1.6 million in charge-offs associated with a group of investor loans that were re-classified as held-for-sale and subsequently sold. In fiscal 2018, we recorded net charge-offs of \$244,000 relating to the same commercial real estate relationship noted in the prior year, \$315,000 in residential investor loans that was primarily associated with one relationship, and \$379,000 in charge-offs associated with three commercial lease loans. During fiscal 2018, our allowance for loan losses of \$2.8 million, increased \$627,000 compared to the prior year. This increase is associated with the growth in the overall loan portfolio, as well as specific charge-offs and their impact to our historical charge-off history. Charge-off history is a significant factor taken into consideration when calculating the allowance for loan losses.



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*Analysis of Loan Loss Experience.* The following table sets forth the analysis of the activity in the allowance for loan losses for the fiscal years indicated:

|   | <b>At or For the Year Ended March 31,</b> |  |             |  |             |  |             |  |             |  |
|---|---|--|-------------|--|-------------|--|-------------|--|-------------|--|
|   | <b>2018</b>                               |  | <b>2017</b> |  | <b>2016</b> |  | <b>2015</b> |  | <b>2014</b> |  |
|   | <b>(Dollars in thousands)</b>             |  |             |  |             |  |             |  |             |  |
| Balance at beginning of year  | \$2,195                                   |  | \$1,702     |  | \$1,690     |  | \$1,786     |  | \$2,071     |  |
| Charge-offs:  |   |  |             |  |             |  |             |  |             |  |
| Real estate loans:  |   |  |             |  |             |  |             |  |             |  |
| Residential   | 20  |  | 35          |  | 70          |  | 55          |  | 75          |  |
| Investor  | 315                                       |  | 1,801       |  | 222         |  | 83          |  | 131         |  |
| Commercial construction   | -   |  | -           |  | -           |  | -           |  | 1,000       |  |
| Commercial  | 244                                       |  | 1,111       |  | 568         |  | -           |  | -           |  |
| Commercial business loans   | 379                                       |  | 2           |  | 11          |  | 84          |  | 1,059       |  |
| Home equity loans and lines of credit                                   | -   |  | -           |  | 6           |  | 101         |  | 11          |  |
| Other consumer  | 17  |  | 4           |  | 16          |  | -           |  | -           |  |
| Total charge-offs   | 975                                       |  | 2,953       |  | 893         |  | 323         |  | 2,276       |  |
| Recoveries:   |   |  |             |  |             |  |             |  |             |  |
| Real estate loans:  |   |  |             |  |             |  |             |  |             |  |
| Residential   | 8   |  | -           |  | 1           |  | 4           |  | 24          |  |
| Investor  | 18  |  | 12          |  | 25          |  | 1           |  | -           |  |
| Commercial construction   | -   |  | -           |  | 237         |  | -           |  | -           |  |
| Commercial  | -   |  | -           |  | -           |  | -           |  | 47          |  |
| Commercial business loans   | 1   |  | 29          |  | 192         |  | 48          |  | 45          |  |
| Home equity loans and lines of credit                                   | -   |  | -           |  | -           |  | 3           |  | -           |  |
| Other consumer  | -   |  | 10          |  | 10          |  | 1           |  | 1           |  |
| Total recoveries  | 27  |  | 51          |  | 465         |  | 57          |  | 117         |  |
| Net loan charge-offs  | (948 )                                    |  | (2,902 )    |  | (428 )      |  | (266 )      |  | (2,159 )    |  |
| Additions charged to operations   | 1,575                                     |  | 3,395       |  | 440         |  | 170         |  | 1,874       |  |
| Balance at end of year  | \$2,822                                   |  | \$2,195     |  | \$1,702     |  | \$1,690     |  | \$1,786     |  |
| Total loans outstanding   | \$389,221                                 |  | \$339,000   |  | \$222,767   |  | \$160,388   |  | \$144,819   |  |
| Average net loans outstanding   | \$362,355                                 |  | \$314,473   |  | \$197,276   |  | \$146,720   |  | \$153,019   |  |
| Allowance for loan losses as a percentage of total loans at end of year | 0.73 %                                    |  | 0.65 %      |  | 0.76 %      |  | 1.05 %      |  | 1.23 %      |  |
| Net loans charged-off as a percent of average net loans outstanding     | 0.26 %                                    |  | 0.92 %      |  | 0.22 %      |  | 0.18 %      |  | 1.41 %      |  |
| Allowance for loan losses to non-performing loans                       | 39.36 %                                   |  | 94.49 %     |  | 33.70 %     |  | 74.97 %     |  | 35.44 %     |  |

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*Allocation of Allowance for Loan Losses.* The following table sets forth the allocation of allowance for loan losses by loan category at the dates indicated. The table also reflects each loan category as a percentage of total loans receivable. The allocation of the allowance by category is not necessarily indicative of future losses and does not restrict the use of the allowance to absorb losses in any category.

|                                       | <b>At March 31,<br/>2018</b>    |                         | <b>2017</b>                     |                         | <b>2016</b>                     |                         |   |  |
|---------------------------------------|---------------------------------|-------------------------|---------------------------------|-------------------------|---------------------------------|-------------------------|---|--|
|                                       | <b>Percent of<br/>Allowance</b> |                         | <b>Percent of<br/>Allowance</b> |                         | <b>Percent of<br/>Allowance</b> |                         |   |  |
|                                       | <b>Amount</b>                   | <b>in Each<br/>Loan</b> | <b>Amount</b>                   | <b>in Each<br/>Loan</b> | <b>Amount</b>                   | <b>in Each<br/>Loan</b> |   |  |
|                                       | <b>Category</b>                 |                         | <b>Category</b>                 |                         | <b>Category</b>                 |                         |   |  |
| <b>(Dollars in thousands)</b>         |                                 |                         |                                 |                         |                                 |                         |   |  |
| Real estate loans:                    |                                 |                         |                                 |                         |                                 |                         |   |  |
| Residential                           | \$609                           | 21.6                    | % \$554                         | 25.2                    | % \$260                         | 15.3                    | % |  |
| Investor                              | 52                              | 1.8                     | 35                              | 1.6                     | 168                             | 9.9                     |   |  |
| Commercial construction               | 33                              | 1.2                     | 9                               | 0.4                     | 42                              | 2.4                     |   |  |
| Commercial                            | 1,253                           | 44.4                    | 1,376                           | 62.7                    | 902                             | 53.0                    |   |  |
| Commercial business loans             | 674                             | 23.9                    | 149                             | 6.8                     | 228                             | 13.4                    |   |  |
| Home equity loans and lines of credit | 70                              | 2.5                     | 70                              | 3.2                     | 82                              | 4.8                     |   |  |
| Other consumer                        | 131                             | 4.6                     | 2                               | 0.1                     | 20                              | 1.2                     |   |  |
| Unallocated                           | -                               | -                       | -                               | -                       | -                               | -                       |   |  |
| Total                                 | \$2,822                         | 100.0                   | % \$2,195                       | 100.0                   | % \$1,702                       | 100.0                   | % |  |

|                               | <b>At March 31,<br/>2015</b>    |                         | <b>2014</b>                     |                         |   |  |  |  |
|-------------------------------|---------------------------------|-------------------------|---------------------------------|-------------------------|---|--|--|--|
|                               | <b>Percent of<br/>Allowance</b> |                         | <b>Percent of<br/>Allowance</b> |                         |   |  |  |  |
|                               | <b>Amount</b>                   | <b>in Each<br/>Loan</b> | <b>Amount</b>                   | <b>in Each<br/>Loan</b> |   |  |  |  |
|                               | <b>Category</b>                 |                         | <b>Category</b>                 |                         |   |  |  |  |
| <b>(Dollars in thousands)</b> |                                 |                         |                                 |                         |   |  |  |  |
| Real estate loans:            |                                 |                         |                                 |                         |   |  |  |  |
| Residential                   | \$319                           | 18.9                    | % \$445                         | 39.8                    | % |  |  |  |
| Investor                      | 114                             | 6.7                     | 83                              | 9.7                     |   |  |  |  |
| Commercial construction       | 68                              | 4.0                     | 61                              | 2.3                     |   |  |  |  |
| Commercial                    | 586                             | 34.7                    | 576                             | 28.6                    |   |  |  |  |

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|                                       |         |       |           |       |   |
|---------------------------------------|---------|-------|-----------|-------|---|
| Commercial business loans             | 473     | 28.0  | 591       | 10.8  |   |
| Home equity loans and lines of credit | 99      | 5.8   | 27        | 8.0   |   |
| Other consumer                        | 1       | 0.1   | 3         | 0.8   |   |
| Unallocated                           | 30      | 1.8   | -         | -     |   |
| Total                                 | \$1,690 | 100.0 | % \$1,786 | 100.0 | % |

The percentage of the allowance for loan loss associated with real estate investor loans is only 1.8%, or \$52,000, despite total charge-offs of \$315,000 and \$1.8 million during fiscal 2018 and 2017 because a large portion of the investor charge-offs were associated with acquired loans from Fairmount. These loans, at acquisition, were not considered to have deteriorated credit quality and were accounted for in accordance with ASC Topic 310-20. Under ASC Topic 310-20, the difference between the loan's principal balance at the time of purchase and the fair value is recognized as an adjustment of yield over the life of the loan. The fair value is comprised of two parts, including a credit mark used to measure credit quality and an interest rate mark to adjust the contractual rate to a current market rate. At March 31, 2018, the credit mark remaining with respect to the Fairmount portfolio was \$1.1 million. This amount acts as a type of reserve and is analyzed in conjunction with the allowance for loan losses with respect to determining reserves that need to be set aside for a specific loan segment.

Table of Contents**Market Risk Management**

**General.** Our most significant form of market risk is interest rate risk because, as a financial institution, the majority of our assets and liabilities are sensitive to changes in interest rates. Therefore, a principal part of our operations is to manage interest rate risk and limit the exposure of our financial condition and results of operations to changes in market interest rates. Our Asset-Liability Management Committee (ALCO) is responsible for evaluating the interest rate risk inherent in our assets and liabilities, for determining the level of risk that is appropriate, given our business strategy, operating environment, capital, liquidity and performance objectives, and for managing this risk consistent with the policy and guidelines approved by our board of directors.

Historically, we have operated as a traditional thrift institution. A significant portion of our assets consist of longer-term, fixed-rate residential mortgage loans and securities, which we have funded primarily with time deposits. Since 2009, in an effort to improve our earnings and to decrease our exposure to interest rate risk, we have generally sold all newly originated residential mortgage loans with terms of over ten years into the secondary market and shifted our focus to originating commercial real estate and commercial business loans. Such loans generally have shorter maturities than one-to-four family residential mortgage loans. However, due to the recent acquisitions and increased volume, the normal run-off associated with our residential real estate loan portfolio has exceeded our new originations within this same loan segment. As a result, we have begun to portfolio some of our newly originated, longer-term residential real estate loans versus selling them in the secondary market to assist in slowing down the decline within this loan segment.

**Net Interest Income Analysis.** We analyze our sensitivity to changes in interest rates through our net interest income simulation model which is provided to us by an independent third party. Net interest income is the difference between the interest income we earn on our interest-earning assets, such as loans and securities, and the interest we pay on our interest-bearing liabilities, such as deposits and borrowings. We estimate what our net interest income would be for a one-year period based on current interest rates. We then calculate what the net interest income would be for the same period under different interest rate assumptions. We also estimate this impact over a five-year time horizon. The following table shows the estimated impact on net interest income for the one-year period beginning March 31, 2018 resulting from potential changes in interest rates. These estimates require certain assumptions to be made, including loan and mortgage-related investment prepayment speeds, reinvestment rates, and deposit maturities and decay rates. These assumptions are inherently uncertain. As a result, no simulation model can precisely predict the impact of changes in interest rates on our net interest income. Although the net interest income table below provides an indication of our interest rate risk exposure at a particular point in time, such estimates are not intended to, and do not, provide a precise forecast of the effect of changes in market interest rates on our net interest income and will differ from actual results.

| <b>Net Interest Income</b> | <b>Year 1<br/>Change</b> |
|----------------------------|--------------------------|
|----------------------------|--------------------------|

| <b>Rate Shift<br/>(1)</b> | <b>Year 1 Forecast</b>        | <b>from Level</b> |
|---------------------------|-------------------------------|-------------------|
|                           | <b>(Dollars in thousands)</b> |                   |
| +400                      | \$ 13,519                     | (4.4)%            |
| +300                      | \$ 13,880                     | (1.8)%            |
| +200                      | \$ 14,149                     | 0.1%              |
| +100                      | \$ 14,253                     | 0.8%              |
| Level                     | \$ 14,140                     | —                 |
| -100                      | \$ 13,792                     | (2.5)%            |
| -200                      | \$ 13,189                     | (6.7)%            |
| -300                      | \$ 13,048                     | (7.7)%            |

(1) The calculated changes assume an immediate shock of the static yield curve.

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**Economic Value of Equity Analysis.** We also analyze the sensitivity of our financial condition to changes in interest rates through our economic value of equity model, which is also provided to us by the same independent third party as the net interest income analysis. This analysis measures the difference between predicted changes in the present value of our assets and predicted changes in the present value of our liabilities assuming various changes in current interest rates. As with the net interest income simulation model, the estimates of changes in the economic value of our equity require certain assumptions to be made. These assumptions include loan and mortgage-related investment prepayment speeds, reinvestment rates, and deposit maturities and decay rates. These assumptions are inherently uncertain and, as a result, we cannot precisely predict the impact of changes in interest rates on the economic value of our equity. Although our economic value of equity analysis provides an indication of our interest rate risk exposure at a particular point in time, such estimates are not intended to, and do not, provide a precise forecast of the effect of changes in market interest rates on the economic value of our equity and will differ from actual results.

| <b>Rate Shift (1)</b>         | <b>Economic Value of Equity</b> | <b>%<br/>Change<br/>In<br/>Equity<br/>from<br/>Level</b> |
|-------------------------------|---------------------------------|--|
| <b>(Dollars in thousands)</b> |                                 |  |
| +400                          | \$ 39,348                       | (31.8) %   |
| +300                          | \$ 47,165                       | (19.7) %   |
| +200                          | \$ 54,316                       | (9.0) %  |
| +100                          | \$ 59,289                       | (1.9) %  |
| Level                         | \$ 61,178                       | —  |
| -100                          | \$ 59,172                       | (4.5) %  |
| -200                          | \$ 55,696                       | (11.5) %   |
| -300                          | \$ 53,844                       | (15.6) %   |

(1) The calculated changes assume an immediate shock of the static yield curve.

**Liquidity and Capital Management**

Liquidity describes our ability to meet the financial obligations that arise in the ordinary course of business. Liquidity is primarily needed to meet the borrowing and deposit withdrawal requirements of our customers and to fund current and planned expenditures. Our primary sources of funds are deposits, scheduled amortization and prepayments of loan principal and mortgage-backed securities, maturities and calls of investment securities and funds provided by our operations. While maturities and scheduled amortization of loans and securities are predictable sources of funds, deposit flows and mortgage prepayments are greatly influenced by general interest rates, economic conditions, and competition. We regularly adjust our investments in liquid assets available to meet short-term liquidity needs based upon our assessment of (i) expected loan demand, (ii) expected deposit flows, (iii) yields available on interest-earning

deposits and securities, and (iv) the objectives of our asset/liability management policy.

We also have the ability to borrow from the Federal Home Loan Bank of Atlanta (FHLB) to meet our funding and liquidity needs. At March 31, 2018, we had \$60.6 million in borrowings from the FHLB, of which \$13.0 million was assumed through acquisitions, and the capacity to borrow approximately \$68.3 million more, subject to our pledging of sufficient assets.

Hamilton Bank may also borrow up to \$5.0 million from a correspondent bank under a secured federal funds line of credit, and \$1.0 million under an unsecured line of credit. We would be required to pledge investment securities to draw upon the secured line of credit.

We normally carry balances with correspondent banks that exceed the federally insured limit. We currently conduct a quarterly review of each correspondent bank's financial information, including the bank's capital ratios, balance sheet, income statement and allowance for loan losses, to determine if the bank is financially stable.

Our primary investing activities are the origination of one-to-four family real estate loans, commercial real estate, commercial business, construction and consumer loans, and the purchase of securities. For the year ended March 31, 2018, loan originations (including original commitment amount) totaled \$53.5 million, compared to \$68.1 million for the year ended March 31, 2017. Purchases of investment and mortgage-backed securities totaled \$1.2 million for the year ended March 31, 2018 and \$50.6 million for the year ended March 31, 2017.

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Our most liquid assets are cash and cash equivalents and interest-bearing deposits. The level of these assets depends on our operating, financing, lending, and investing activities during any given period. At March 31, 2018, cash and cash equivalents totaled \$23.4 million, while securities classified as available-for-sale amounted to \$75.4 million.

Total deposits decreased \$7.7 million during the year ended March 31, 2018, while total deposits decreased \$9.7 million, excluding those acquired in the Fairmount acquisition, during the year ended March 31, 2017. Deposit flows are affected by the level of interest rates, the interest rates and products offered by competitors and other factors. In the first quarter of fiscal 2017, we made an increased effort to grow our lower costing core deposits (considered to be all deposits other than certificates of deposit) and retain maturing certificates of deposits through various promotions to assist in funding organic loan growth and potential loan purchases. Certificates of deposit allowed us to lock in those funds for an extended period based upon current interest rates. At March 31, 2018, certificates of deposit scheduled to mature within one year totaled \$123.8 million, 50.1% of certificates of deposit. The percentage of certificates of deposit that mature within one year reflects customers' hesitancy to invest their funds for longer periods due to the current low interest rate environment, expectation of rising rates, and local competitive pressures. Whether we retain these deposits will be determined in part by the interest rates we are willing to pay on such deposits. If these maturing deposits do not remain with us, we will be required to seek other sources of funds, including other certificates of deposit and borrowings. Depending on market conditions, we may be required to pay higher rates on such deposits or other borrowings than we currently pay on certificates of deposit due on or before March 31, 2019.

In the normal course of operations, we engage in a variety of financial transactions that, in accordance with generally accepted accounting principles, are not recorded in our financial statements. These transactions involve, to varying degrees, elements of credit, interest rate and liquidity risk. Such transactions are used primarily to manage customers' requests for funding and take the form of loan commitments, unused lines of credit and letters of credit. At March 31, 2018, we had \$50.7 million in commitments to extend credit outstanding. These commitments consisted of unused lines of credits, approved loan settlements, and standby letters of credit.

We are committed to maintaining a strong liquidity position. We monitor our liquidity position on a daily basis. We anticipate that we will have sufficient funds to meet our current funding commitments. Based on our deposit retention experience and current pricing strategy, we anticipate that a significant portion of maturing time deposits will be retained.

At March 31, 2018 and 2017, we exceeded all of the applicable regulatory capital requirements for the Bank, including the new requirements under Basel III to obtain a minimum common equity core (Tier 1) capital to risk-weighted assets ratio of 4.5%. To be classified as a well-capitalized bank, we must have a common equity core (Tier 1) capital to risk-weighted assets ratio of at least 6.5%. For the year ended March 31, 2018, the Bank's common equity to Tier 1 capital was \$39.1 million, or 10.61%, of total risk-weighted assets compared to \$40.1 million, or 12.13% of total risk-weighted assets for the year ended March 31, 2017.



Our core (Tier 1) capital was \$39.1 million and \$40.1 million, or 7.64% and 8.28% of adjusted total assets, at March 31, 2018 and 2017, respectively. In order to be classified as “well-capitalized” under federal banking regulations, we were required to have core capital of at least \$25.6 million, or 5.0% of adjusted assets, as of March 31, 2018. To be classified as a well-capitalized bank, we must also have a ratio of total risk-based capital to risk-weighted assets of at least 10.0%, and a Tier 1 risk-based capital to risk-weighted assets of at least 8%. At March 31, 2018 and 2017, we had total risk-based capital ratios of 11.39% and 12.81%, respectively, and Tier 1 risk-based capital ratios of 10.61% and 12.13%, respectively. Our regulatory risk weighted capital ratios decreased during fiscal 2018 as a result of our risk-weighted assets increasing due to the increase in loans associated with organic growth and loan purchases throughout the year.

### **Off-Balance Sheet Arrangements and Aggregate Contractual Obligations**

**Commitments.** As a financial services provider, we routinely are a party to various financial instruments with off-balance-sheet risks, such as commitments to extend credit and unused lines of credit. While these contractual obligations represent our future cash requirements, a significant portion of commitments to extend credit may expire without being drawn upon. Such commitments are subject to the same credit policies and approval process accorded to loans we make.

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**Contractual Obligations.** In the ordinary course of our operations, we enter into certain contractual obligations. Such obligations include data processing services, operating leases for premises and equipment, agreements with respect to borrowed funds and deposit liabilities.

**Recent Accounting Pronouncements**

The information required by this item is included in Note 2 to the consolidated financial statements included in this annual report.

**Effect of Inflation and Changing Prices**

The consolidated financial statements and related consolidated financial data presented herein regarding Hamilton Bank have been prepared in accordance with accounting principles generally accepted in the United States of America, which generally require the measurement of financial position and operating results in terms of historical dollars, without considering changes in relative purchasing power over time due to inflation. Unlike most industrial companies, virtually all of Hamilton Bank's assets and liabilities are monetary in nature. As a result, interest rates generally have a more significant impact on Hamilton Bank's performance than does the effect of inflation. Interest rates do not necessarily move in the same direction or in the same magnitude as the prices of goods and services, because such prices are affected by inflation to a larger extent than interest rates.

**ITEM 7A. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK**

The information required by this item is incorporated herein by reference to Part II, Item 7, "*Management's Discussion and Analysis of Financial Condition and Results of Operation.*"

**ITEM 8. FINANCIAL STATEMENTS AND SUPPLEMENTARY DATA**

The Consolidated Financial Statements, including supplemental data, of Hamilton Bancorp, Inc. begin on page F-1 of this Annual Report.

**ITEM 9. CHANGES IN AND DISAGREEMENTS WITH ACCOUNTANTS ON ACCOUNTING AND FINANCIAL DISCLOSURE**

None.

## **ITEM 9A. CONTROLS AND PROCEDURES**

### **Evaluation of Disclosure Controls and Procedures.**

The Company's President and Chief Executive Officer, its Chief Financial Officer, and other members of its senior management team have evaluated the effectiveness of the Company's disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) or 15d-15(e)), as of March 31, 2018. Based on such evaluation, the President and Chief Executive Officer and Chief Financial Officer have concluded that the Company's disclosure controls and procedures, as of the end of the period covered by this report, were adequate and effective to provide reasonable assurance that information required to be disclosed by the Company, including Hamilton Bank, in reports that are filed or submitted under the Exchange Act, is recorded, processed, summarized and reported, within the time periods specified in the Commission's rules and forms.

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**Managements Report and Changes in Internal Controls Over Financial Reporting.**

There have been no changes in the Company's internal control over financial reporting during the quarter ended March 31, 2018 that have materially affected, or are reasonably likely to materially affect, the Company's internal control over financial reporting.

The management of the Company is responsible for establishing and maintaining adequate internal control over financial reporting. The internal control process has been designed under our supervision to provide reasonable assurance regarding the reliability of financial reporting and the preparation of the Company's financial statements for external reporting purposes in accordance with accounting principles generally accepted in the United States of America.

Management conducted an assessment of the effectiveness of the Company's internal control over financial reporting as of March 31, 2018, utilizing the framework established in Internal Control — Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO) in 1992 and revised in 2013. Based on this assessment, management has determined that the Company's internal control over financial reporting as of March 31, 2018 is effective.

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

All internal control systems, no matter how well designed, have inherent limitations. Therefore, even those systems determined to be effective can provide only reasonable assurance with respect to financial statement preparation and presentation. Also, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

Management's report on internal control was not subject to attestation by the Company's registered public accounting firm in accordance with rules of the Securities and Exchange Commission.

**ITEM 9B. OTHER INFORMATION**

Not applicable.

**PART III**

**ITEM 10. DIRECTORS, EXECUTIVE OFFICERS AND CORPORATE GOVERNANCE**

Information relating to the directors and officers of the Company, information regarding compliance with Section 16(a) of the Exchange Act, information regarding any changes in procedures for stockholders to recommend director nominees, and information regarding the audit committee and audit committee financial expert is incorporated herein by reference to the Company's Proxy Statement for the Annual Meeting of Stockholders to be held on August 20, 2018 (the "Proxy Statement") under the captions "Proposal 1—Election of Directors," "Executive Officers," "Section 16(a) Beneficial Ownership Reporting Compliance," "Nominating Committee Procedures—Procedures to be Followed by Stockholders," "Corporate Governance and Board Matters—Committees of the Board of Directors" and "Corporate Governance and Board Matters—Committees of the Board of Directors."

The Company has adopted a code of ethics that applies to its principal executive officer, the principal financial officer and principal accounting officer. The Code of Ethics is posted on the Company's Internet Web site.

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**ITEM 11. EXECUTIVE COMPENSATION**

Information regarding executive and director compensation is incorporated herein by reference to the Proxy Statement under the captions “Executive Officers—Executive Compensation” and “Director Compensation.”

**ITEM 12. SECURITY OWNERSHIP OF CERTAIN BENEFICIAL OWNERS AND MANAGEMENT AND RELATED STOCKHOLDERS MATTERS**

(a) Security Ownership of Certain Beneficial Owners

Information required by this item is incorporated herein by reference to the section captioned “Stock Ownership—Stock Ownership of Certain Beneficial Owners” in the Proxy Statement.

(b) Security Ownership of Management

Information required by this item is incorporated herein by reference to the section captioned “Stock Ownership—Stock Ownership of Management” in the Proxy Statement.

(c) Changes in Control

Management of the Company knows of no arrangements, including any pledge by any person or securities of the Company, the operation of which may at a subsequent date result in a change in control of the registrant.

(d) Equity Compensation Plan Information

The following table sets forth information as of March 31, 2018 about Company common stock that may be issued upon the exercise of options under the Hamilton Bancorp, Inc. 2013 Equity Incentive Plan. The plan was approved by the Company’s stockholders.

| Plan Category  | Number of securities to be issued upon the exercise of outstanding options, warrants and rights | Weighted-average exercise price of outstanding options, warrants and rights | Number of securities remaining available for future issuance under equity compensation plans (excluding securities reflected in the first column) |
|--|---|---|---|
| Equity compensation plans approved by security holders     | <b>242,350</b>  | <b>\$13.84</b>  | <b>178,920</b>  |
| Equity compensation plans not approved by security holders | N/A   | N/A   | N/A   |
| Total  | <b>242,350</b>  | <b>\$13.84</b>  | <b>178,920</b>  |

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**ITEM 13. CERTAIN RELATIONSHIPS AND RELATED TRANSACTIONS, AND DIRECTOR INDEPENDENCE**

The information relating to certain relationships and related transactions and director independence is incorporated herein by reference to the Proxy Statement under the captions “Transactions with Related Persons” and “Proposal 1 — Election of Directors.”

**ITEM 14. PRINCIPAL ACCOUNTING FEES AND SERVICES**

The information relating to the principal accounting fees and expenses is incorporated herein by reference to the Proxy Statement under the captions “Proposal 2—Ratification of Independent Registered Public Accounting Firm—Audit Fees” and “—Pre-Approval of Services by the Independent Registered Public Accounting Firm.”

**PART IV**

**ITEM 15. EXHIBITS AND FINANCIAL STATEMENT SCHEDULES**

(1) The financial statements required in response to this item are incorporated by reference from Item 8 of this report.

(2) All financial statement schedules are omitted because they are not required or applicable, or the required information is shown in the consolidated financial statements or the notes thereto.

(3) Exhibits

Articles of Incorporation of Hamilton Bancorp, Inc. (Incorporated by reference to Exhibit 3.1 to the Company’s 3.1 Registration Statement on Form S-1 (File No. 333-182151), as amended, initially filed with the SEC on June 15, 2012).

3.2 Bylaws of Hamilton Bancorp, Inc. (Incorporated by reference to Exhibit 3.2 to the Company’s Registration Statement on Form S-1 (File No. 333-182151), as amended, initially filed with the SEC on June 15, 2012).



Form of Common Stock Certificate of Hamilton Bancorp, Inc. Bylaws of Hamilton Bancorp, Inc. (Incorporated by reference to Exhibit 4 to the Company's Registration Statement on Form S-1 (File No. 333-182151), as amended, initially filed with the SEC on June 15, 2012).

10.1 Employment Agreement between Hamilton Bank and Robert A. DeAlmeida (Incorporated by reference to Exhibit 10.1 to the Company's Form 8-K (File No. 001-35693) filed with the SEC on October 15, 2012).

10.2 Employment Agreement between Hamilton Bancorp, Inc. and Robert A. DeAlmeida (Incorporated by reference to Exhibit 10.2 to the Company's Form 8-K (File No. 001-35693) filed with the SEC on October 15, 2012).

10.3 Change in Control Agreement of John P. Marzullo (Incorporated by reference to Exhibit 10.4 to the Company's Form 8-K (File No. 001-35693) filed with the SEC on October 15, 2012).

10.4 Hamilton Bank Non-Qualified Supplemental Employee Stock Ownership Plan (Incorporated by reference to Exhibit 10.5 to the Company's Form 8-K (File No. 001-35693) filed with the SEC on October 15, 2012).

10.5 Hamilton Bank Executive Split Dollar Agreement with Robert A. DeAlmeida (Incorporated by reference to Exhibit 10.6 to the Company's Registration Statement on Form S-1 (File No. 333-182151), as amended, initially filed with the SEC on June 15, 2012).

10.6 Hamilton Bank Agreement for Deferred Compensation of Salaries (Incorporated by reference to Exhibit 10.8 to the Company's Registration Statement on Form S-1 (File No. 333-182151), as amended, initially filed with the SEC on June 15, 2012).

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Hamilton Bank Agreement for Deferred Compensation of Board Fees (Incorporated by reference to Exhibit 10.9 10.7 to the Company's Registration Statement on Form S-1 (File No. 333-182151), as amended, initially filed with the SEC on June 15, 2012).

10.8 Hamilton Bancorp, Inc. 2013 Equity Incentive Plan (Incorporated by reference to Appendix A of the Proxy Statement for the 2013 Annual Meeting of Stockholders (File No. 1-35693), filed October 18, 2013).

10.9 Change in Control Agreement of Ellen R. Fish (Incorporated by reference to Exhibit 10.9 to the Company's Annual Report on Form 10-K for the year ended March 31, 2014 (File No. 001-35693), filed with the SEC on June 26, 2015).

21.0 Subsidiaries of Registrant

23.0 Consent of Dixon Hughes Goodman, LLP

31.1 Rule 13a-14(a)/15d-14(a) Certification of Chief Executive Officer

31.2 Rule 13a-14(a)/15d-14(a) Certification of Chief Financial Officer

32.0 Section 1350 Certifications

The following materials from the Company's Annual Report on Form 10-K for the year ended March 31, 2018, formatted in XBRL (Extensible Business Reporting Language): (i) Consolidated Statements of Financial Condition; (ii) Consolidated Statements of Operations; (iii) Consolidated Statements of Changes in Shareholders' Equity; (iv) Consolidated Statements of Cash Flows; and (v) the Notes to the Consolidated Financial Statements.

**ITEM 16. Form 10-K Summary.**

None.

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**SIGNATURES**

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

**HAMILTON BANCORP, INC.**

Date: June 29, 2018

By: /s/ Robert A. DeAlmeida  
Robert A. DeAlmeida  
President and Chief Executive Officer

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

| <u>Signatures</u>                                 | <u>Title</u>  | <u>Date</u>      |
|---|---|------------------|
| /s/ Robert A.<br>DeAlmeida<br>Robert A. DeAlmeida | President and Chief Executive Officer (Principal Executive Officer)                                       | June 29,<br>2018 |
| /s/ John P. Marzullo<br>John P. Marzullo          | Senior Vice President, Chief Financial Officer and Treasurer (Principal Financial and Accounting Officer) | June 29,<br>2018 |
| /s/ Carol L. Coughlin<br>Carol L. Coughlin        | Chairperson of the Board  | June 29,<br>2018 |
| /s/ Joseph J. Bouffard<br>Joseph J. Bouffard      | Director  | June 29,<br>2018 |
| /s/ William E. Ballard                            | Director  | June 29,<br>2018 |

William E. Ballard

/s/ Jenny G. Morgan Director  
Jenny G. Morgan

June 29,  
2018

/s/ William W. Furr Director  
William W. Furr

June 29,  
2018

/s/ Bobbi R.  
Macdonald Director  
Bobbi R. Macdonald

June 29,  
2018

/s/ James R. Farnum,  
Jr. Director  
James R. Farnum, Jr.

June 29,  
2018

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**Report of Independent Registered Public Accounting Firm**

The Board of Directors and Shareholders

Hamilton Bancorp, Inc.

Towson, Maryland

***Opinion on the Consolidated Financial Statements***

We have audited the accompanying consolidated statements of financial condition of Hamilton Bancorp, Inc. and Subsidiary (the “Company”) as of March 31, 2018 and 2017 and the related consolidated statements of operations, comprehensive (loss) income, changes in shareholders’ equity, and cash flows for the years then ended, and the related notes (collectively referred to as the “financial statements”). In our opinion, the financial statements present fairly, in all material respects, the financial position of the Company as of March 31, 2018 and 2017, and the results of their operations and their cash flows for the years then ended, in conformity with U.S. generally accepted accounting policies.

***Basis for Opinion***

These financial statements are the responsibility of the Company’s management. Our responsibility is to express an opinion on these consolidated financial statements based on our audits. We are a public accounting firm registered with the Public Company Accounting Oversight Board (United States) (“PCAOB”) and are required to be independent with respect to the Company in accordance with the U.S. federal securities laws and the applicable rules and regulations of the Securities and Exchange Commission and the PCAOB.

We conducted our audits in accordance with the standards of the PCAOB. Those standards require that we plan and perform the audits to obtain reasonable assurance about whether the financial statements are free of material misstatement, whether due to error or fraud. The Company is not required to have, nor were we engaged to perform, an audit of its internal control over financial reporting. As part of our audits we are required to obtain an understanding of internal control over financial reporting but not for the purpose of expressing an opinion on the effectiveness of the Company’s internal control over financial reporting. Accordingly, we express no such opinion.

Our audits also included performing procedures to assess the risks of material misstatement of the financial statements, whether due to error or fraud, and performing procedures that respond to those risks. Such procedures included examining, on a test basis, evidence regarding the amounts and disclosures in the financial statements. Our audits also included evaluating the accounting principles used and significant estimates made by management, as well as evaluating the overall presentation of the financial statement. We believe that our audits provide a reasonable basis for our opinion.

/s/ Dixon Hughes Goodman LLP

We have served as the Company's auditor since 2016.

**Baltimore, Maryland**

**June 29, 2018**

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Table of Contents**HAMILTON BANCORP, INC. AND SUBSIDIARY****Consolidated Statements of Financial Condition****March 31, 2018 and March 31, 2017**

|   | <b>March 31,<br/>2018</b> | March 31,<br>2017 |
|---|---------------------------|-------------------|
| <b>Assets</b>                                 |                           |                   |
| <b>Assets</b>                                 |                           |                   |
| Cash and due from banks                       | <b>\$ 15,488,396</b>      | \$ 24,436,793     |
| Federal funds sold                            | <b>7,880,019</b>          | 4,917,128         |
| Cash and cash equivalents                     | <b>23,368,415</b>         | 29,353,921        |
| Certificates of deposit held as investment    | <b>499,189</b>            | 499,280           |
| Securities available for sale, at fair value  | <b>75,404,136</b>         | 102,429,128       |
| Federal Home Loan Bank stock, at cost         | <b>3,122,400</b>          | 2,020,200         |
| Loans   | <b>390,420,885</b>        | 338,933,198       |
| Allowance for loan losses                     | <b>(2,821,903 )</b>       | (2,194,815 )      |
| Net loans and leases                          | <b>387,598,982</b>        | 336,738,383       |
| Premises and equipment, net                   | <b>3,945,825</b>          | 3,674,280         |
| Premises and equipment held for sale          | -                         | 547,884           |
| Foreclosed real estate                        | <b>457,778</b>            | 503,094           |
| Accrued interest receivable                   | <b>1,468,382</b>          | 1,310,080         |
| Bank-owned life insurance                     | <b>17,455,850</b>         | 18,253,348        |
| Deferred income taxes                         | -                         | 7,976,850         |
| Income taxes refundable                       | <b>40,000</b>             | -                 |
| Goodwill and other intangible assets          | <b>9,176,764</b>          | 9,302,828         |
| Other assets                                  | <b>2,995,741</b>          | 1,920,740         |
| <b>Total Assets</b>                           | <b>\$ 525,533,462</b>     | \$ 514,530,016    |
| <b>Liabilities and Shareholders' Equity</b>   |                           |                   |
| <b>Liabilities</b>                            |                           |                   |
| Noninterest-bearing deposits                  | <b>\$ 29,557,943</b>      | \$ 30,401,454     |
| Interest-bearing deposits                     | <b>375,585,032</b>        | 382,454,320       |
| Total deposits                                | <b>405,142,975</b>        | 412,855,774       |
| Borrowings                                    | <b>60,672,140</b>         | 36,124,899        |
| Advances by borrowers for taxes and insurance | <b>1,962,665</b>          | 1,868,110         |
| Other liabilities                             | <b>3,679,550</b>          | 3,890,003         |
| Total liabilities                             | <b>471,457,330</b>        | 454,738,786       |
| Commitments and contingencies                 | -                         | -                 |
| <b>Shareholders' Equity</b>                   | <b>34,076</b>             | 34,111            |

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Common stock, \$.01 par value, 100,000,000 shares authorized. Issued and outstanding: 3,407,613 shares at March 31, 2018 and 3,411,075 shares at March 31, 2017

|   |                      |               |
|---|----------------------|---------------|
| Additional paid in capital                        | <b>32,113,534</b>    | 31,656,235    |
| Retained earnings                                 | <b>25,920,490</b>    | 31,730,673    |
| Unearned ESOP shares                              | <b>(2,073,680 )</b>  | (2,221,800 )  |
| Accumulated other comprehensive loss              | <b>(1,918,288 )</b>  | (1,407,989 )  |
| Total shareholders' equity                        | <b>54,076,132</b>    | 59,791,230    |
| <b>Total Liabilities and Shareholders' Equity</b> | <b>\$525,533,462</b> | \$514,530,016 |

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

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Table of Contents**HAMILTON BANCORP, INC. AND SUBSIDIARY****Consolidated Statements of Operations****Years Ended March 31, 2018 and 2017**

|  | <b>2018</b>         | <b>2017</b>  |
|--|---------------------|--------------|
| <b>Interest revenue</b>                                    |                     |              |
| Loans, including fees                                      | <b>\$16,088,774</b> | \$14,834,648 |
| U.S. treasuries, government agencies and FHLB stock        | <b>188,600</b>      | 214,441      |
| Municipal and corporate bonds                              | <b>420,737</b>      | 338,916      |
| Mortgage-backed securities                                 | <b>1,246,963</b>    | 1,183,227    |
| Federal funds sold and other bank deposits                 | <b>134,542</b>      | 190,374      |
| Total interest revenue                                     | <b>18,079,616</b>   | 16,761,606   |
| <b>Interest expense</b>                                    |                     |              |
| Deposits   | <b>2,836,925</b>    | 2,599,901    |
| Borrowed funds   | <b>750,092</b>      | 271,205      |
| Total interest expense                                     | <b>3,587,017</b>    | 2,871,106    |
| <b>Net interest income</b>                                 | <b>14,492,599</b>   | 13,890,500   |
| Provision for loan losses                                  | <b>1,575,000</b>    | 3,395,006    |
| <b>Net interest income after provision for loan losses</b> | <b>12,917,599</b>   | 10,495,494   |
| <b>Noninterest revenue</b>                                 |                     |              |
| Service charges  | <b>459,688</b>      | 420,234      |
| (Loss) gain on sale of investment securities               | <b>(2,354)</b>      | 23,720       |
| Gain on sale of loans held for sale                        | <b>-</b>            | 23,087       |
| Gain (loss) on sale of property and equipment              | <b>97,604</b>       | (5,046)      |
| Earnings on bank-owned life insurance                      | <b>484,030</b>      | 485,400      |
| Earnings on death benefit from bank-owned life insurance   | <b>834,610</b>      | -            |
| Other  | <b>122,770</b>      | 107,152      |
| Total noninterest revenue                                  | <b>1,996,348</b>    | 1,054,547    |
| <b>Noninterest expenses</b>                                |                     |              |
| Salaries   | <b>5,733,065</b>    | 5,283,578    |
| Employee benefits  | <b>1,535,442</b>    | 1,472,466    |
| Occupancy  | <b>1,045,589</b>    | 984,767      |
| Advertising  | <b>86,865</b>       | 122,093      |
| Furniture and equipment                                    | <b>343,624</b>      | 377,232      |
| Data processing  | <b>716,458</b>      | 777,554      |
| Legal services   | <b>491,900</b>      | 291,550      |
| Other professional services                                | <b>851,660</b>      | 1,046,450    |
| Merger related expenses                                    | <b>-</b>            | 219,417      |
| Branch consolidation expense                               | <b>-</b>            | 494,977      |

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|   |                       |              |
|---|-----------------------|--------------|
| Deposit insurance premiums                | <b>324,325</b>        | 318,132      |
| Foreclosed real estate expense and losses | <b>44,197</b>         | 7,468        |
| Other operating                           | <b>1,737,727</b>      | 1,841,144    |
| Total noninterest expense                 | <b>12,910,852</b>     | 13,236,828   |
| <b>Income (loss) before income taxes</b>  | <b>2,003,095</b>      | (1,686,787 ) |
| <b>Income tax expense (benefit)</b>       | <b>8,052,038</b>      | (758,005 )   |
| <b>Net loss</b>                           | <b>\$(6,048,942 )</b> | \$(928,782 ) |
| <b>Net loss per common share:</b>         |                       |              |
| <b>Basic</b>                              | <b>\$(1.90 )</b>      | \$(0.29 )    |
| <b>Diluted</b>                            | <b>\$(1.90 )</b>      | \$(0.29 )    |

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

Table of Contents**HAMILTON BANCORP, INC. AND SUBSIDIARY****Consolidated Statements of Comprehensive (Loss) Income****Years Ended March 31, 2018 and 2017**

|   | <b>2018</b>          | 2017          |
|---|----------------------|---------------|
| <b>Net loss</b>   | <b>\$(6,048,942)</b> | \$(928,782 )  |
| <b>Other comprehensive income (loss):</b>   |                      |               |
| Unrealized loss on investment securities available for sale   | <b>(678,270 )</b>    | (2,127,277)   |
| Reclassification adjustment for realized loss (gain) on investment securities available for sale included in net income | <b>2,354</b>         | (23,720 )     |
| Total unrealized loss on investment securities available for sale   | <b>(675,916 )</b>    | (2,150,997)   |
| Unrealized gain (loss) on derivative transactions   | <b>300,023</b>       | (83,634 )     |
| Income tax benefit relating to investment securities available for sale and derivative transactions                     | <b>(104,353 )</b>    | (848,461 )    |
| Other comprehensive loss  | <b>(271,540 )</b>    | (1,386,170)   |
| <b>Total comprehensive loss</b>   | <b>\$(6,320,482)</b> | \$(2,314,952) |

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

Table of Contents**HAMILTON BANCORP, INC. AND SUBSIDIARY****Consolidated Statements of Changes in Shareholders' Equity****Years Ended March 31, 2018 and 2017**

|   | <b>Common<br/>stock</b> | <b>Additional<br/>paid-in<br/>capital</b> | <b>Retained<br/>earnings</b> | <b>Unearned<br/>ESOP<br/>shares</b> | <b>Accumulated<br/>other<br/>comprehensive<br/>loss</b> | <b>Total<br/>shareholders'<br/>equity</b> |
|---|-------------------------|---|------------------------------|-------------------------------------|---|---|
| <b>Balances at April 1, 2016</b>  | <b>\$ 34,136</b>        | <b>\$31,242,731</b>                       | <b>\$32,659,455</b>          | <b>\$(2,369,920)</b>                | <b>\$(21,819)</b>                                       | <b>) \$ 61,544,583</b>                    |
| Net loss  | -                       | -   | (928,782 )                   | -                                   | -   | (928,782 )                                |
| Unrealized loss on available<br>for sale securities, net of tax<br>effect of \$ (848,461) | -                       | -   | -                            | -                                   | (1,302,536 )  | (1,302,536 )                              |
| Unrealized loss on derivative<br>transactions   | -                       | -   | -                            | -                                   | (83,634 )   | (83,634 )                                 |
| Stock based compensation -<br>options   | -                       | 216,735                                   | -                            | -                                   | -   | 216,735                                   |
| Restricted stock -<br>compensation and activity   | (25 )                   | 158,649                                   | -                            | -                                   | -   | 158,624                                   |
| ESOP shares allocated for<br>release  | -                       | 38,120                                    | -                            | 148,120                             | -   | 186,240                                   |
| <b>Balances at March 31, 2017</b>   | <b>\$ 34,111</b>        | <b>\$31,656,235</b>                       | <b>\$31,730,673</b>          | <b>\$(2,221,800)</b>                | <b>\$(1,407,989)</b>                                    | <b>) \$ 59,791,230</b>                    |
| Net loss  | -                       | -   | (6,048,942 )                 | -                                   | -   | (6,048,942 )                              |
| Unrealized loss on available<br>for sale securities, net of tax<br>effect of \$ (156,640) | -                       | -   | -                            | -                                   | (519,276 )  | (519,276 )                                |
| Unrealized gain on derivative<br>transactions, net of tax effect<br>of \$ 52,287          | -                       | -   | -                            | -                                   | 247,736   | 247,736                                   |
| Reclassification of tax effect under<br>ASU 2018-02                                       | -                       | -   | 238,759                      | -                                   | (238,759 )  | -   |
| Stock based compensation -<br>options   | -                       | 229,569                                   | -                            | -                                   | -   | 229,569                                   |
| Restricted stock -<br>compensation and activity   | (35 )                   | 176,911                                   | -                            | -                                   | -   | 176,876                                   |
| ESOP shares allocated for<br>release  | -                       | 50,819                                    | -                            | 148,120                             | -   | 198,939                                   |
| <b>Balances at March 31, 2018</b>   | <b>\$ 34,076</b>        | <b>\$32,113,534</b>                       | <b>\$25,920,490</b>          | <b>\$(2,073,680)</b>                | <b>\$(1,918,288)</b>                                    | <b>) \$ 54,076,132</b>                    |

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

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Table of Contents**HAMILTON BANCORP, INC. AND SUBSIDIARY****Consolidated Statements of Cash Flows****Years Ended March 31, 2018 and 2017**

|  | 2018                | 2017         |
|--|---------------------|--------------|
| <b>Cash flows from operating activities</b>  |                     |              |
| Interest received  | <b>\$18,587,764</b> | \$16,415,596 |
| Fees and commissions received  | <b>583,757</b>      | 522,341      |
| Interest paid  | <b>(4,427,190 )</b> | (4,004,880 ) |
| Cash paid to suppliers and employees   | <b>(13,059,738)</b> | (11,216,410) |
| Origination of loans held for sale   | -                   | (2,017,697 ) |
| Proceeds from sale of loans held for sale  | -                   | 2,300,234    |
| Income taxes paid, net of refunds received   | <b>(10,835 )</b>    | (1,455,219 ) |
| Net cash provided by operating activities  | <b>1,673,758</b>    | 543,965      |
| <b>Cash flows from investing activities</b>  |                     |              |
| Acquisition, net of cash acquired  | -                   | (10,508,813) |
| Proceeds from sale of securities available for sale  | <b>11,608,699</b>   | 4,282,233    |
| Proceeds from maturing and called securities available for sale, including principal pay downs | <b>15,124,739</b>   | 28,963,565   |
| Proceeds from sale of certificates of deposit held for investment                              | -                   | 1,730,273    |
| Proceeds from maturing and called certificates of deposit                                      | -                   | 1,724,000    |
| Purchase of investment securities available for sale   | <b>(1,208,990 )</b> | (50,585,898) |
| Redemption of Federal Home Loan Bank stock   | -                   | 210,800      |
| Purchase of Federal Home Loan Bank stock   | <b>(1,102,200 )</b> | (405,900 )   |
| Proceeds from Bank Owned Life Insurance death benefit  | <b>2,116,138</b>    | -            |
| Loans made, net of principal repayments  | <b>2,256,439</b>    | (10,461,510) |
| Loans purchased  | <b>(54,556,249)</b> | -            |
| Purchase of premises and equipment   | <b>(719,105 )</b>   | (273,669 )   |
| Proceeds from sale of premises and equipment   | <b>767,728</b>      | 442,529      |
| Proceeds from sale of foreclosed real estate   | <b>35,896</b>       | 60,258       |
| Net cash used by investing activities  | <b>(25,676,905)</b> | (34,822,132) |
| <b>Cash flows from financing activities</b>  |                     |              |
| Net increase (decrease) in Deposits  | <b>(7,295,252 )</b> | (10,529,332) |
| Advances by borrowers for taxes and insurance  | <b>94,555</b>       | 788,316      |
| Proceeds from borrowings   | <b>40,000,000</b>   | 11,578,805   |
| Payments of borrowings   | <b>(15,027,250)</b> | (5,501,555 ) |
| Interest rate swap on FHLB borrowings  | <b>300,023</b>      | (83,634 )    |
| Issuance of restricted stock   | <b>(35 )</b>        | 20           |
| Redemption of restricted stock   | <b>(54,400 )</b>    | (69,068 )    |
| Net cash provided (used) by financing activities   | <b>18,017,641</b>   | (3,816,448 ) |

|  |                     |                     |
|--|---------------------|---------------------|
| <b>Net decrease in cash and cash equivalents</b>         | <b>(5,985,506 )</b> | <b>(38,094,615)</b> |
| Cash and cash equivalents at beginning of period         | <b>29,353,921</b>   | 67,448,536          |
| <b>Cash and cash equivalents at end of period</b>        | <b>\$23,368,415</b> | \$29,353,921        |
| <b>Supplemental disclosures of cash flow information</b> |                     |                     |
| Total cash consideration paid for Fraternity acquisition | \$-                 | \$25,704,871        |
| Less cash acquired                                       | -                   | 15,196,058          |
| Acquisition, net of cash acquired                        | \$-                 | \$10,508,813        |

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

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Table of Contents**HAMILTON BANCORP, INC. AND SUBSIDIARY****Consolidated Statements of Cash Flows****(Continued)**

|  | 2018                 | 2017         |
|--|----------------------|--------------|
| <b>Reconciliation of net loss to net cash provided by operating activities</b> |                      |              |
| Net loss   | <b>\$(6,048,942)</b> | \$(928,782 ) |
| Adjustments to reconcile net loss to net cash provided by operating activities |                      |              |
| Amortization of premiums on certificates of deposit                            | <b>91</b>            | 12,949       |
| Amortization of premiums on securities   | <b>822,270</b>       | 840,535      |
| Gain on sale of investment securities and certificates of deposit              | <b>2,354</b>         | (23,720 )    |
| Loss on sale of foreclosed real estate   | <b>1,299</b>         | 6,238        |
| Write-down of foreclosed real estate   | <b>31,955</b>        | -            |
| Loan discount accretion  | <b>(225,587 )</b>    | (841,329 )   |
| Deposit premium amortization   | <b>(417,547 )</b>    | (597,655 )   |
| Borrowing premium amortization   | <b>(425,509 )</b>    | (551,125 )   |
| Core deposit intangible asset amortization                                     | <b>126,064</b>       | 121,022      |
| Premises and equipment depreciation and amortization                           | <b>325,320</b>       | 334,210      |
| Gain on death benefit from bank-owned life insurance                           | <b>(834,610 )</b>    | -            |
| (Gain) loss on sale of premises and equipment                                  | <b>(97,604 )</b>     | 5,046        |
| Stock based compensation   | <b>460,880</b>       | 444,406      |
| Provision for loan losses  | <b>1,575,000</b>     | 3,395,006    |
| ESOP shares allocated for release  | <b>198,939</b>       | 186,240      |
| Decrease (increase) in   |                      |              |
| Accrued interest receivable  | <b>(158,302 )</b>    | (361,914 )   |
| Loans held for sale  | -                    | 259,450      |
| Cash surrender value of life insurance   | <b>(484,030 )</b>    | (485,399 )   |
| Income taxes refundable and deferred income taxes                              | <b>8,041,203</b>     | (2,213,224)  |
| Other assets   | <b>(1,074,989)</b>   | 2,565,464    |
| Increase (decrease) in   |                      |              |
| Accrued interest payable   | <b>2,883</b>         | 15,007       |
| Deferred loan origination fees   | <b>69,676</b>        | 3,748        |
| Other liabilities  | <b>(217,056 )</b>    | (1,642,208)  |
| Net cash provided by operating activities                                      | <b>\$1,673,758</b>   | \$543,965    |
| <b>Noncash investing activity</b>  |                      |              |
| Real estate acquired through foreclosure                                       | <b>\$23,835</b>      | \$126,575    |

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





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**HAMILTON BANCORP, INC. AND SUBSIDIARY**

**Form 10-K**

**Notes to Consolidated Financial Statements**

**March 31, 2018**

**Note 1: Nature of Operations and Summary of Significant Accounting Policies**

**Nature of Operations**

Hamilton Bancorp, Inc. (the “Company”) was incorporated on June 7, 2012 to serve as the stock holding company for Hamilton Bank (the “Bank”), a federally chartered savings bank. On October 10, 2012, the Bank converted from a mutual savings bank to a stock savings bank and became the wholly owned subsidiary of the Company. In connection with the conversion, the Company sold 3,703,000 shares of common stock at a price of \$10.00 per share, through which the Company received proceeds of approximately \$35,580,000, net of offering expenses of approximately \$1,450,000. The Bank’s employee stock ownership plan (the “ESOP”) purchased 8.0% of the shares sold in the offering, or 296,240 common shares. The purchase of shares by the ESOP was funded by a loan from the Company. The company’s common stock began trading on the NASDAQ Capital Market under the trading symbol “HBK” on October 12, 2012.

On December 21, 2017, the Bank converted its charter from a federal savings bank to a Maryland state-chartered commercial bank and now operates under the laws of the State of Maryland. In conjunction with the Bank’s charter conversion, Hamilton Bancorp converted from a savings and loan holding company to a bank holding company. The charter conversion is part of the Bank’s strategic plan which will allow it to continue to focus on growth opportunities in commercial, consumer and mortgage lending as well as small business and retail banking. The Maryland Office of the Commissioner of Financial Regulation will serve as the Bank’s primary regulator with federal oversight provided by the Federal Deposit Insurance Corporation. Hamilton Bancorp will continue to be regulated by the Federal Reserve Board.

On May 13, 2016, the Company completed its acquisition of Fraternity Community Bancorp, Inc. (“Fraternity”) through the merger of Fraternity, the parent company of Fraternity Federal Savings and Loan, with and into the Company pursuant to the Agreement and Plan of Merger dated as of October 12, 2015, by and between the Company and Fraternity. As a result of the merger, each shareholder of Fraternity received a cash payment equal to nineteen dollars and twenty-five cents (\$19.25) for each share of Fraternity common stock, or an aggregate of approximately \$25.7

million. Immediately following the merger of Fraternity into the Company, Fraternity Federal Savings and Loan was merged with and into the Bank, with the Bank as the surviving entity.

On September 11, 2015, the Company completed its acquisition of Fairmount Bancorp, Inc. (“Fairmount Bancorp”) through the merger of Fairmount Bancorp, the parent company of Fairmount Bank, with and into the Company pursuant to the Agreement and Plan of Merger dated as of April 15, 2015, by and between the Company and Fairmount Bancorp. As a result of the merger, each shareholder of Fairmount Bancorp received a cash payment equal to thirty dollars (\$30.00) for each share of Fairmount Bancorp common stock, or an aggregate of approximately \$15.4 million. Immediately following the merger of Fairmount Bancorp into the Company, Fairmount Bank was merged with and into the Bank, with the Bank as the surviving entity.

Hamilton Bancorp is a holding company that operates a community bank with seven branches in the Baltimore-metropolitan area. Its primary deposit products are certificates of deposit and demand, savings, NOW, and money market accounts. Its primary lending products consist of real estate mortgages, along with commercial and consumer loans. Hamilton Bancorp’s primary source of revenue is derived from loans to customers, who are predominately small and middle-market businesses and middle-income individuals.

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HAMILTON BANCORP, INC. AND SUBSIDIARY

Notes to Consolidated Financial Statements (Continued)

**Summary of Significant Accounting Policies**

The accounting and reporting policies of Hamilton Bancorp, Inc. and Subsidiary (“Hamilton”) conform to accounting principles generally accepted in the United States of America (“U.S. GAAP”) and to general practices in the banking industry. The more significant policies follow:

***Principles of Consolidation.*** The accompanying consolidated financial statements include the accounts of the parent company and its wholly owned subsidiary, Hamilton Bank. All significant intercompany balances and transactions have been eliminated in consolidation.

***Reclassifications.*** There were no reclassifications to prior year amounts in order to conform to current period classifications.

***Use of Estimates.*** The preparation of financial statements in conformity with U.S. GAAP requires management to make estimates and assumptions that affect the amounts reported in the financial statements and the accompanying notes. Actual results could differ significantly from those estimates. Material estimates that are particularly susceptible to significant change in the near term relate to the determination of the allowance for loan losses, deferred income tax valuation allowances, the fair value of derivatives and investment securities, and other than temporary impairment of investment securities.

***Cash and Cash Equivalents.*** For purposes of reporting cash flows, cash and cash equivalents include cash on hand, amounts due from banks with original maturities of less than 90 days, brokerage money market accounts, and federal funds sold. Generally, federal funds are sold as overnight investments.

***Investment Securities.*** Management determines the appropriate classification of investment securities at the time of purchase. Securities that may be sold before maturity are classified as available for sale and carried at fair value. Investment securities that management has the intent and ability to hold to maturity are classified as held to maturity and carried at amortized cost. All investment securities held by Hamilton at March 31, 2018 and 2017 are classified as available for sale.

Investment securities designated as available for sale are stated at estimated fair value based on quoted market prices. They represent those securities which management may sell as part of its asset/liability strategy or that may be sold in response to changing interest rates or liquidity needs. Changes in unrealized gains and losses, net of related deferred taxes, for available for sale securities are recorded in other comprehensive income. Realized gains (losses) on available-for-sale securities are included in noninterest revenue and, when applicable, are reported as a reclassification adjustment in other comprehensive income. Realized gains and losses on the sale of available for sale securities are recorded on the trade date and are determined by the specific identification method. The amortization of premiums and the accretion of discounts are recognized in interest revenue using methods approximating the interest method over the term of the security.

In estimating other-than-temporary impairment losses, management considers the length of time and the extent to which the fair value has been less than cost, the financial condition and near-term prospects of the issuer, and the intent and ability of the Bank to retain its investment in the issuer for a period of time sufficient to allow for any anticipated recovery in fair value.

***Federal Home Loan Bank Stock.*** Federal Home Loan Bank of Atlanta (the “FHLB”) stock is an equity interest in the FHLB, which does not have a readily determinable fair value for purposes of generally accepted accounting principles, because its ownership is restricted and it lacks a market. FHLB stock is carried at cost, which approximates fair value and can be sold back only at par value of \$100 per share and only to the FHLB or another member institution. As a member of the FHLB, the Bank is required to purchase stock based on its total assets. Additional stock is purchased and redeemed based on the outstanding FHLB advances to the Bank. As of March 31, 2018 and 2017, the Company owned shares totaling \$3,122,400 and \$2,020,200, respectively.

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HAMILTON BANCORP, INC. AND SUBSIDIARY

Notes to Consolidated Financial Statements (Continued)

**Loans Held For Sale.** Mortgage loans originated and intended for sale are carried at the lower of aggregate cost or estimated fair value. Fair value is determined based on outstanding investor commitments, or in the absence of such commitments, based on current investor yield requirements. Gains and losses on loan sales are determined by the specific-identification method.

**Loans Receivable.** The Bank makes mortgage, commercial, and consumer loans to customers. A substantial portion of the loan portfolio is represented by mortgage loans throughout the Baltimore metropolitan area. The ability of the Bank's debtors to repay their loans is dependent upon the real estate and general economic conditions in this area.

Loans are reported at their outstanding unpaid principal balance adjusted for the allowance for loan loss, premiums on loans acquired, and/or any deferred fees or costs on originated loans. Interest revenue is accrued on the unpaid principal balance. Loan origination fees and the direct costs of underwriting and closing loans are recognized over the life of the related loan as an adjustment to yield using a method that approximates the interest method. Any differences that arise from prepayment will result in a recalculation of the effective yield.

Loans are generally placed on nonaccrual status when they are 90 days past due. Past due status is based on contractual terms of the loan. In all cases, loans are placed on nonaccrual status at an earlier date if the collection of principal or interest is considered doubtful. All interest accrued but not collected for loans that are placed on nonaccrual status are reversed against interest revenue. The interest on nonaccrual loans is accounted for on the cash basis method, until the loans qualify for return to accrual status. Loans are returned to accrual status when all the principal and interest amounts contractually due are brought current and, in management's judgment, future payments are reasonably assured.

Loans are considered impaired when, based on current information, management considers it unlikely that collection of principal and interest payments will be made according to contractual terms. If collection of principal is evaluated as doubtful, all payments are applied to principal. Impaired loans are measured: (i) at the present value of expected cash flows discounted at the loan's effective interest rate; (ii) at the observable market price; or (iii) at the fair value of the collateral if the loan is collateral dependent. If the measure of the impaired loan is less than the recorded investment in the loan, an impairment is recognized through an allocation of the allowance for loan losses and corresponding provision for loan losses. Generally, identified impairments are charged-off against the allowance for loan losses.

Troubled debt restructurings are loans for which Hamilton, for legal or economic reasons related to a debtor's financial difficulties, has granted a concession to the debtor that it otherwise would not have considered. Concessions that result in the categorization of a loan as a troubled debt restructuring include:

Reduction of the stated interest rate;

Extension of the maturity date or dates at a stated interest rate lower than the current market rate for new debt with similar risk;

Reduction of the face amount or maturity amount of the debt as stated in the instrument or other agreement; or

Reduction of accrued interest

***Accounting for Certain Loans or Debt Securities Acquired in a Transfer.*** The loans acquired from the Company's acquisition of Fraternity on May 13, 2016 (see Note 3 "Acquisition") and Fairmount on September 11, 2015 were recorded at fair value at the acquisition date and no separate valuation allowance was established. The initial fair values were determined by management, with the assistance of an independent valuation specialist, based on estimated expected cash flows discounted at appropriate rates. The discount rates were based on market rates for new originations of comparable loans and did not include a separate factor for loan losses as that was included in the estimated cash flows.

Accounting Standards Codification ("ASC") Topic 310-30, *Loans and Debt Securities Acquired with Deteriorated Credit Quality*, applies to loans acquired in a transfer with evidence of deterioration of credit quality for which it is probable, at acquisition, that the investor will be unable to collect all contractually required payments receivable. If both conditions exist, the Company determines whether to account for each loan individually or whether such loans will be assembled into pools based on common risk characteristics such as credit score, loan type, and origination date.

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HAMILTON BANCORP, INC. AND SUBSIDIARY

Notes to Consolidated Financial Statements (Continued)

The Company considered expected prepayments and estimated the total expected cash flows, which included undiscounted expected principal and interest. The excess of that amount over the fair value of the loan is referred to as accretable yield. Accretable yield is recognized as interest income on a constant yield basis over the expected life of the loan. The excess of the contractual cash flows over expected cash flows is referred to as nonaccretable difference and is not accreted into income. Over the life of the loan, the Company continues to estimate expected cash flows. Subsequent decreases in expected cash flows are recognized as impairments in the current period through the allowance for loan losses. Subsequent increases in cash flows to be collected are first used to reverse any existing valuation allowance and any remaining increase are recognized prospectively through an adjustment of the loan's yield over its remaining life.

ASC Topic 310-20, *Nonrefundable Fees and Other Costs*, was applied to loans not considered to have deteriorated credit quality at acquisition. Under ASC Topic 310-20, the difference between the loan's principal balance at the time of purchase and the fair value is recognized as an adjustment of yield over the life of the loan.

***Allowance for Loan Losses.*** The allowance for loan losses represents an amount which, in management's judgment, will be adequate to absorb probable future losses on existing loans. The allowance for loan losses is established, as loan losses are estimated to have occurred, through a provision for loan losses charged to earnings. Loan losses are charged against the allowance when management believes the uncollectability of a loan balance is confirmed. Recoveries on previously charged-off loans are credited to the allowance for loan losses.

The allowance for loan losses is increased by provisions charged to income and reduced by charge-offs, net of recoveries. Management's periodic evaluation of the adequacy of the allowance is based on the Bank's past loan loss experience, known and inherent risks in the loan portfolio, adverse situations that may affect the borrower's ability to repay, estimated value of any underlying collateral and current economic conditions. The look back period for historical losses consists of using both a 36 month and 48 month look back period for net charge-offs. Both of these periods are used individually to develop a range in which the allowance for loan loss should be within.

Management considers a number of factors in estimating the required level of the allowance. These factors include: historical loss experience in the loan portfolios; the levels and trends in past-due and nonaccrual loans; the status of nonaccrual loans and other loans identified as having the potential for further deterioration; credit risk and industry concentrations; trends in loan volume; the effects of any changes in lending policies and procedures or underwriting standards; and a continuing evaluation of the economic environment. Management modified the analysis during the quarter ended September 30, 2016 by keeping our net charge-off history as a percentage of loans, as it pertains to each loan segment, constant across all risk ratings and altering our qualitative factors either up or down based upon the



respective risk rating for each loan segment. The change in methodology did not have a material impact on the amount of the allowance for loan and lease losses at September 30, 2016, the date of the change, as compared to the prior methodology.

***Bank-Owned Life Insurance (BOLI).*** The Bank purchased single premium life insurance policies on certain employees of the Bank. The net cash surrender value of those policies is included in the accompanying statement of financial position. Appreciation in the value of the insurance policies is recognized as noninterest revenue and is nontaxable. Upon the death of an employee covered under one or more BOLI policies, the full amount of the insurance policy is paid-out to the Bank and the difference between the policy amount and the cash surrender value of the policy or policies is recognized as noninterest revenue. This income is also nontaxable.

***Premises and Equipment.*** Land is carried at cost. Buildings, land improvements, leasehold improvements, and furniture and equipment are stated at cost less accumulated depreciation and amortization. Depreciation is computed primarily by the straight-line method over the estimated useful lives of the assets. Leasehold improvements are amortized over the lesser of the lease term or the useful lives of the improvements. Maintenance and normal repairs are charged to noninterest expense as incurred, while additions and improvements to buildings and furniture and equipment are capitalized. Gains and losses on disposition of assets are reflected in earnings.

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HAMILTON BANCORP, INC. AND SUBSIDIARY

Notes to Consolidated Financial Statements (Continued)

**Foreclosed Real Estate.** Real estate acquired through foreclosure or other means is recorded at the lower of its carrying value or the fair value of the related real estate collateral less estimated selling costs. Losses in estimated fair value incurred at the time of acquisition of the property are charged to the allowance for loan losses. Subsequent reductions in the estimated fair value of the property are included in noninterest expense. Costs to maintain foreclosed real estate are expensed as incurred.

**Goodwill and Other Intangible Assets.** Goodwill represents the excess of the cost of an acquisition over the fair value of the net assets acquired. Intangible assets, consisting of core deposit intangibles, represent purchased assets that also lack physical substance but can be distinguished from goodwill because of contractual or other legal rights or because the asset may be sold or exchanged on its own or in combination with a related contract, asset, or liability. Core deposit intangibles are amortized on an accelerated basis over an eight-year period. Goodwill is not amortized but is evaluated on an annual basis to determine impairment, if any. Any impairment of goodwill would be recognized against income in the period of impairment.

**Derivative Financial Instruments and Hedging Activities.** Derivatives are initially recognized at fair value on the date a derivative contract is entered into and are subsequently re-measured at their fair value. The accounting for changes in the fair value of a derivative depends on the intended use of the derivative and the resulting designation. The Company documents at the inception of the transaction the relationship between hedging instruments and hedged items, as well as its risk management objective and strategy for undertaking various hedge transactions.

For derivatives qualifying as cash flow hedges, the Company also documents its assessment, both at hedge inception and on an ongoing basis, of whether the derivatives that are used in hedging transactions are highly effective in offsetting changes in fair values or cash flows of hedged items. The effective portion of changes in fair value of derivatives that are designated and qualify as cash flow hedges is recognized in the consolidated statement of comprehensive (loss) income. The gain or loss relating to the ineffective portion is recognized immediately in the consolidated statement of operations as a gain or loss. When a hedging instrument expires or is sold, or when a hedge no longer meets the criteria for hedge accounting, any cumulative gain or loss existing in equity at that time remains in equity and is recognized when the forecast transaction is ultimately recognized in the consolidated statement of operations. When a forecast transaction is no longer expected to occur, the cumulative gain or loss that was reported in equity is immediately transferred to the consolidated statement of operations as a gain or loss to income.

For derivative instruments designated as fair-value hedges, the change in fair value of the derivative is recognized in the consolidated statement of operations under the same heading as the change in fair value of the hedged item for the portion attributable to the hedged risk. For accounting purposes, if the derivative is highly effective, the change in fair

values relating to the asset or liability and the hedged item will offset one another and result in no impact to overall income.

Gains (losses) on derivatives representing either hedge components excluded from the assessment of effectiveness or hedge ineffectiveness are recognized in earnings.

***Off-Balance-Sheet Credit-Related Financial Instruments.*** In the ordinary course of business, the Bank enters into commitments to extend credit, including commitments under standby letters of credit. Such financial instruments are recorded when they are funded or otherwise required to be recognized.

***Advertising Costs.*** Advertising costs are expensed as incurred and included in non-interest expenses.

***Stock Based Compensation.*** Compensation cost is recognized for stock options and restricted stock awards issued to employees and directors, based on the fair value of these awards at the date of grant. A Black-Scholes model is utilized to estimate the fair value of stock options, while the market price of the Company's common stock at the date of grant is used for restricted stock awards. Compensation cost is recognized over the required service period, generally defined as the vesting period. For awards with graded vesting, compensation cost is recognized on a straight-line basis over the requisite service period for the entire award.

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HAMILTON BANCORP, INC. AND SUBSIDIARY

Notes to Consolidated Financial Statements (Continued)

**Income Taxes.** The Bank recognizes income taxes under the asset and liability method. Under this method, 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. 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. Deferred tax assets and liabilities are reduced by a valuation allowance when, in the opinion of management, it is more-likely-than-not that all or some portion of the deferred tax assets will not be realized.

**Earnings Per Common Share.** Basic earnings per share represents income available to common shareholders divided by the weighted-average number of common shares outstanding during the period. Weighted average shares exclude unallocated ESOP shares. Diluted earnings per share includes additional common shares that would have been outstanding if dilutive potential common shares had been issued, as well as any adjustment to income that would result from the assumed issuance. Potential common shares relate to outstanding stock options, restricted stock, and warrants and are determined using the treasury stock method.

**Note 2: New Accounting Pronouncements**

**Recent Accounting Pronouncements**

*ASU No. 2017-12, Targeted Improvements to Accounting for Hedging Activities.* This ASU's objectives are to: (1) improve the transparency and understandability of information conveyed to financial statement users about an entity's risk management activities by better aligning the entity's financial reporting for hedging relationships with those risk management activities; and (2) reduce the complexity of and simplify the application of hedge accounting by preparers. The ASU is effective for interim and annual reporting periods beginning after December 15, 2018; early adoption is permitted. The Company does not expect the adoption of ASU 2017-12 to have a material impact on its consolidated financial statements.

*ASU 2017-04, Simplifying the Test for Goodwill Impairment.* This update removes the requirement to compare the implied fair value of goodwill with its carrying amount as part of step 2 of the goodwill impairment test. As a result, under the ASU, an entity should perform its annual, or interim, goodwill impairment test by comparing the fair value

of a reporting unit with its carrying amount and should recognize an impairment charge for the amount by which the carrying amount exceeds the reporting unit's fair value; however, the loss recognized should not exceed the total amount of goodwill allocated to that reporting unit. The ASU is effective for annual and interim goodwill impairment tests in fiscal years beginning after December 15, 2019. Early adoption is permitted for interim or annual goodwill impairment tests performed on testing dates after January 1, 2017. The Company does not expect the adoption of ASU 2017-04 to have a material impact on its consolidated financial statements.

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HAMILTON BANCORP, INC. AND SUBSIDIARY

Notes to Consolidated Financial Statements (Continued)

*ASU No. 2017-01, Business Combinations (Topic 805): Clarifying the Definition of a Business.* This guidance clarifies the definition of a business and assists entities with evaluating whether transactions should be accounted for as acquisitions (or disposals) of assets or businesses. Under this guidance, when substantially all of the fair value of gross assets acquired is concentrated in a single asset (or group of similar assets), the assets acquired would not represent a business. In addition, in order to be considered a business, an acquisition would have to include at a minimum an input and a substantive process that together significantly contribute to the ability to create an output. The amended guidance also narrows the definition of outputs by more closely aligning it with how outputs are described in FASB guidance for revenue recognition. This guidance is effective for annual periods beginning after December 15, 2017, including interim periods within those fiscal years, with early adoption permitted. The Company does not expect the adoption of this guidance to have a material impact on its consolidated financial statements.

*ASU No. 2016-15, Statement of Cash Flows (Topic 230): Classification of Certain Cash Receipts and Cash Payments.* This update addresses diversity on how certain cash receipts and payments are reflected in the statement of cash flows. The update made the following changes that may affect the Company: (1) Debt Prepayment or Debt Extinguishment Costs: Cash payments for debt prepayment or debt extinguishment costs should be classified as cash flows for financing activities. (2) Proceeds from the settlement of Bank-Owned Life Insurance Policies: Cash proceeds received from the settlement of bank-owned life insurance policies should be classified as cash flows from investing activities. The cash payments for premiums on bank-owned policies may be classified as cash flows from investing activities, operating activities, or a combination of investing and operating activities. The amendments in this Update will be effective for public business entities for fiscal years beginning after December 15, 2017, and interim periods within those fiscal years. The guidance requires application using a retrospective transition method. The Company does not expect the guidance to have a significant impact on its consolidated statement of cash flows.

*ASU 2016-13, Financial Instruments – Credit Losses.* The main objective of this update is to provide financial statement users with more decision-useful information about the expected credit losses on financial instruments and other commitments to extend credit held by a reporting entity at each reporting date. To achieve this objective, the guidance in this update replaces the incurred loss impairment methodology in current GAAP with a methodology that reflects expected credit losses and requires consideration of a broader range of reasonable and supportable information to estimate credit losses. The measurement of expected credit losses is based on relevant information about past events, including historical experience, current conditions, and reasonable and supportable forecasts that affect the collectability of the reported amount. An entity must use judgment in determining the relevant information and estimation methods that are appropriate in its circumstances. The guidance in this update for public business entities is effective for fiscal years beginning after December 15, 2019, including interim periods within those fiscal years. Hamilton Bancorp is in the process of implementing a committee and has begun to gather loan information and consider acceptable methodologies to comply with this ASU. The implementation team will meet periodically to discuss the latest developments and updates via webcasts, publications, and conferences. Hamilton Bancorp's evaluation indicates that the provisions of ASU No. 2016-13 are expected to impact its consolidated financial statements, in particular the level of the reserve for loan losses. We are, however, continuing to evaluate the extent of

the potential impact.

*ASU 2016-09, Improvements to Employee Share-Based Payment Accounting (Topic 718)*. This ASU includes provisions intended to simplify various aspects related to how share-based payments are accounted for and presented in the financial statements. Some of the key provisions of this new ASU include: (1) companies will no longer record excess tax benefits and certain tax deficiencies in additional paid-in capital (“APIC”). Instead, they will record all excess tax benefits and tax deficiencies as income tax expense or benefit in the income statement, and APIC pools will be eliminated. The guidance also eliminates the requirement that excess tax benefits be realized before companies can recognize them. In addition, the guidance requires companies to present excess tax benefits as an operating activity on the statement of cash flows rather than as a financing activity; (2) increase the amount an employer can withhold to cover income taxes on awards and still qualify for the exception to liability classification for shares used to satisfy the employer’s statutory income tax withholding obligation. The new guidance will also require an employer to classify the cash paid to a tax authority when shares are withheld to satisfy its statutory income tax withholding obligation as a financing activity on its statement of cash flows (current guidance did not specify how these cash flows should be classified); and (3) permit companies to make an accounting policy election for the impact of forfeitures on the recognition of expense for share-based payment awards. Forfeitures can be estimated, as required today, or recognized when they occur. ASU No. 2016-09 became effective for the Company on April 1, 2017 and was not material to the consolidated financial statements.

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HAMILTON BANCORP, INC. AND SUBSIDIARY

Notes to Consolidated Financial Statements (Continued)

*ASU 2016-02, Leases (Topic 842)*. From the lessee's perspective, the new ASU standard establishes a right-of-use (ROU) model that requires a lessee to record a ROU asset and a lease liability on the balance sheet for all leases with terms longer than 12 months. Leases will be classified as either finance or operating, with classification affecting the pattern of expense recognition in the income statement for lessees. The guidance also eliminates the current real estate-specific provision and changes the guidance on sale-leaseback transactions, initial direct costs and lease executory costs. With respect to lessors, the guidance modifies the classification criteria and the accounting for sales-type and direct financing leases. All entities will classify leases to determine how to recognize lease-related revenue and expense. In applying this guidance entities will also need to determine whether an arrangement contains a lease or service agreement. Disclosures are required by lessees and lessors to meet the objective of enabling users of financials statements to assess the amount, timing, and uncertainty of cash flows arising from leases. For public entities, this guidance is effective for the first interim or annual period beginning after December 15, 2018. Early adoption is permitted. Entities are required to use a modified retrospective approach for leases that exist or are entered into after the beginning of the earliest comparative period in the financial statements. The Company is assessing this guidance to determine its impact on the Company's financial position, results of operations and cash flows.

*ASU No. 2016-01, Financial Instruments – Recognition and Measurement of Financial Assets and Liabilities*. This ASU requires equity investments to be measured at fair value with changes in fair value recognized in net income, excluding equity investments that are consolidated or accounted for under the equity method of accounting. The amendment allows equity investments without readily determinable fair values to be measured at cost minus impairment, with a qualitative assessment required to identify impairment. The amendment also requires public companies to use exit prices to measure the fair value of financial instruments purposes; requiring separate presentation of financial assets and financial liabilities by measurement category and form of financial asset on the balance sheet or the accompanying notes to the financial statement; it eliminates the disclosure requirements related to measurement assumptions for the fair value of instruments measured at amortized cost. In addition, for liabilities measured at fair value under the fair value option, to present in other comprehensive income changes in fair value due to changes in instrument specific credit risk. This ASU will be effective for us in our first quarter of fiscal 2018. The Company's management has engaged a third-party expert in the field of valuation and reporting and is creating a process to ensure adequate documentation of financial controls and analysis performed in its review of "exit pricing" of the fair values of loans, deposits, and other financial instruments. ASU 2016-01 is effective for public companies for fiscal years beginning after December 31, 2017 and interim periods within those fiscal years. This ASU will be effective for us in our first quarter ending June 30, 2018 and will not have a significant impact on the Company's consolidated financial statements.

*ASU 2014-09, Revenue from Contracts with Customers (Topic 606)*. ASU 2014-09 implements a common revenue standard that clarifies the principles for recognizing revenue. The core principle of ASU 2014-09 is that an entity should recognize revenue to depict the transfer of promised goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods or services. To achieve that core principle, an entity should apply the following steps: (i) identify the contract(s) with a customer, (ii) identify the



performance obligations in the contract, (iii) determine the transaction price, (iv) allocate the transaction price to the performance obligations in the contract and (v) recognize revenue when (or as) the entity satisfies a performance obligation.

The guidance in this ASU affects any entity that either enters into contracts with customers to transfer goods or services or enters into contracts for the transfer of nonfinancial assets. This ASU does not apply to revenue associated with financial instruments including loans and securities that are accounted for under U.S. GAAP. Consequently, adoption of the ASU is not expected to have a significant impact on the Company's consolidated financial statements and related disclosures since the primary source of revenue is derived from interest and dividends earned on loans, investment securities and other financial instruments that are outside the scope of the ASU. However, the Company has assessed its revenue streams and reviewed its contracts with customers that are potentially affected by the new guidance. This includes fees on deposits, gains and sales on the sale of foreclosed real estate, credit and debit card interchange fees, merchant card services, and administrative services for customer deposit account such as ATM and wire transfer transactions. The Company's revenue recognition pattern for revenue streams within the scope of the ASU has not change significantly from current practice and is immaterial to our financial statements. ASU 2014-09 is effective for fiscal years beginning after December 31, 2017 and interim periods within those fiscal years. This ASU will be effective for us in our first quarter ending June 30, 2018 and will not have a significant impact on the Company's consolidated financial statements.

*ASU 2018-02, Reclassification of Certain Tax Effects from Accumulated Other Comprehensive Income (Topic 220).* ASU 2018-02 allows an entity to elect a reclassification from accumulated other comprehensive income ("AOCI") to retained earnings for stranded tax effects resulting from the *Tax Cuts and Jobs Act* that changed our federal income tax rate from 35% to 21%. The amount of that reclassification should include the effect of changes in the tax rate on the deferred tax amount in AOCI. The ASU requires an entity to state if an election to reclassify the tax effect to retained earnings is made along with the description of other income tax effects that are reclassified from AOCI. ASU 2018-02 is effective for fiscal years beginning after December 15, 2018 and interim periods within those fiscal years with early adoption permitted. Hamilton Bancorp early adopted ASU 2018-02 in the last quarter of fiscal 2018. The change in accounting principal was accounted for as a cumulative effect adjustment to the balance sheet resulting in a reclassification of \$238,759 from AOCI to retained earnings during the last quarter of fiscal 2018.

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## HAMILTON BANCORP, INC. AND SUBSIDIARY

## Notes to Consolidated Financial Statements (Continued)

**Note 3: Acquisition****Fraternity Community Bancorp, Inc.**

On May 13, 2016, Hamilton Bancorp acquired Fraternity Community Bancorp, Inc. (“Fraternity”), the parent company of Fraternity Federal Savings and Loan. Under the terms of the Merger Agreement, shareholders of Fraternity received a cash payment equal to nineteen dollars and twenty-five cents (\$19.25) for each share of Fraternity common stock. The total merger consideration was \$25.7 million.

In connection with the acquisition, Fraternity Federal Savings and Loan was merged with and into Hamilton Bank, with Hamilton Bank as the surviving bank. The results of the Fraternity acquisition are included with Hamilton’s results as of and from May 13, 2016.

As required by the acquisition method of accounting, we have adjusted the acquired assets and liabilities of Fraternity to their estimated fair value on the date of acquisition and added them to those of Hamilton Bancorp. Based on management’s preliminary valuation of the fair value of tangible and intangible assets acquired and liabilities assumed, which we have based on level 3 valuation estimates and assumptions that were subject to change through the measurement date of May 2017, we have allocated the purchase price for Fraternity as follows:

|  | As recorded<br>by<br>Fraternity<br>Community<br>Bancorp, Inc. | Fair Value<br>Adjustments | As recorded<br>by<br>Hamilton<br>Bancorp, Inc. |
|--|---|---------------------------|--|
| Identifiable assets:                     |   |                           |  |
| Cash and cash equivalents                | \$15,196,058  | \$-                       | \$15,196,058                                   |
| Investment securities available for sale | 17,570,712  | -                         | 17,570,712                                     |
| FHLB Bank Stock                          | 782,600   | -                         | 782,600  |
| Loans                                    | 108,872,041   | (67,858 )A                | 108,804,183                                    |

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|   |               |             |   |               |
|---|---------------|-------------|---|---------------|
| Allowance For Loan Loss                   | (1,550,000 )  | 1,550,000   | A | -             |
| Premises and equipment                    | 691,095       | 78,711      | B | 769,806       |
| Bank-Owned Life Insurance                 | 5,058,041     | -           |   | 5,058,041     |
| Deferred income taxes                     | 2,743,481     | (410,377 )  | C | 2,333,104     |
| Other assets                              | 2,877,665     | -           |   | 2,877,665     |
| Total identifiable assets                 | \$152,241,693 | \$1,150,476 |   | \$153,392,169 |
| Identifiable liabilities:                 |               |             |   |               |
| Non-interest bearing deposits             | 1,242,187     | -           |   | 1,242,187     |
| Interest bearing deposits                 | 107,648,792   | 1,098,131   | D | 108,746,923   |
| Borrowings                                | 15,000,000    | 793,537     | E | 15,793,537    |
| Other liabilities                         | 4,023,914     | -           |   | 4,023,914     |
| Total identifiable liabilities            | \$127,914,893 | \$1,891,668 |   | \$129,806,561 |
| Net tangible assets acquired              | 24,326,800    | (741,192 )  |   | 23,585,608    |
| Definite lived intangible assets acquired | -             | 242,020     |   | 242,020       |
| Goodwill                                  | -             | 1,877,243   |   | 1,877,243     |
| Net intangible assets acquired            | -             | 2,119,263   |   | 2,119,263     |
| Total cash consideration                  | \$24,326,800  | \$1,378,071 |   | \$25,704,871  |

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## HAMILTON BANCORP, INC. AND SUBSIDIARY

## Notes to Consolidated Financial Statements (Continued)

Explanation of fair value adjustments:

- A - Adjustment reflects the fair value adjustments based on Hamilton Bancorp's evaluation of the acquired loan portfolio and excludes the allowance for losses recorded by Fraternity Community Bancorp, Inc.
- B - Adjustment reflects the fair value adjustments based on Hamilton Bancorp's evaluation of the acquired premises and equipment.
- C - Adjustment to record deferred tax asset related to fair value adjustments at 39.45% income tax rate; the statutory income tax rate of the Company on the acquisition date.
- D - Adjustment arises since the rates on interest-bearing deposits are higher than rates available on similar deposits as of the acquisition date.
- E - Adjustment reflects the fair value of Fraternity's borrowings acquired on acquisition date.

Prior to the end of the May 13, 2016 measurement period, if information became available which indicated the purchase price allocations require adjustments, we included such adjustments in the purchase price allocation retrospectively.

Of the total estimated purchase price, we have allocated \$23.6 million to net tangible assets acquired and we have allocated \$242,020 to the core deposit intangible which is a definite lived intangible asset. We have allocated the remaining purchase price to goodwill. We will amortize the core deposit intangible on a straight-line basis over its estimated useful life of eight years. We will evaluate goodwill annually for impairment.

The following table outlines the contractually required payments receivable, cash flows we expect to receive, non-accretable credit adjustments and the accretable yield for all Fraternity loans as of the acquisition date.

|                           | <b>Contractually<br/>Required<br/>Payments<br/>Receivable</b> | <b>Non-Accretable<br/>Credit<br/>Adjustments</b> | <b>Cash Flows<br/>Expected To<br/>Be<br/>Collected</b> | <b>Accretable<br/>FMV<br/>Adjustments</b> | <b>Carrying<br/>Value<br/>of Loans<br/>Receivable</b> |
|---------------------------|---|--|--|---|---|
| Performing loans acquired | \$ 107,474,993  | \$ -   | \$ 107,474,993   | \$ 301,672                                | \$ 107,776,665  |

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|                         |                       |                    |          |                       |                   |          |                       |
|-------------------------|-----------------------|--------------------|----------|-----------------------|-------------------|----------|-----------------------|
| Impaired loans acquired | 1,397,048             | (314,484           | )        | 1,082,564             | (55,046           | )        | 1,027,518             |
| Total                   | <b>\$ 108,872,041</b> | <b>\$ (314,484</b> | <b>)</b> | <b>\$ 108,557,557</b> | <b>\$ 246,626</b> | <b>)</b> | <b>\$ 108,804,183</b> |

At our acquisition of Fraternity, we recorded all loans acquired at the estimated fair value on the purchase date with no carryover of the related allowance for loan losses. On the acquisition date, we segregated the loan portfolio into two loan pools, performing and nonperforming loans, to be retained in our portfolio.

We had an independent third party assist us to determine the fair value of cash flows on \$107,474,993 of performing loans. The valuation took into consideration the loans' underlying characteristics, including account types, remaining terms, annual interest rates, interest types, past delinquencies, timing of principal and interest payments, current market rates, loan to value ratios, loss exposures, and remaining balances. These performing loans were segregated into pools based on loan and payment type and in some cases, risk grade. The effect of this fair valuation process was a net accretable premium adjustment of \$301,672 at acquisition.

We also individually evaluated 23 impaired loans totaling \$1,397,048 to determine the fair value as of the May 13, 2016 measurement date. In determining the fair value for each individually evaluated impaired loan, we considered a number of factors including the remaining life of the acquired loans, estimated prepayments, estimated loss ratios, estimated value of the underlying collateral and net present value of cash flows we expect to receive, among others.

We established a credit risk related non-accretable difference of \$314,484 relating to these acquired, credit impaired loans, reflected in the recorded net fair value. We further estimated the timing and amount of expected cash flows in excess of the estimated fair value and established an accretable discount adjustment of \$55,046 at acquisition relating to these impaired loans.

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## HAMILTON BANCORP, INC. AND SUBSIDIARY

## Notes to Consolidated Financial Statements (Continued)

**Fraternity Pro forma Condensed Combined Financial Information.** The consolidated statements of operations data for the unaudited pro forma results for the fiscal year periods ending March 31, 2018 and 2017 as if the Fraternity acquisition had occurred at the beginning of these fiscal periods are deemed immaterial and not presented. Due to the fact the acquisition of Fraternity occurred on May 13, 2016, the fiscal year period ending March 31, 2018, as reported in this 10-K, already include the impact of Fraternity in the consolidated statements of operations as though the acquisition occurred at the beginning of fiscal 2018. The fiscal period ending March 31, 2017 does not reflect the full impact to the consolidated statements of operations for those twelve months since the acquisition occurred in May 2016 or close to the beginning of that respective fiscal period, however, that amount is deemed to be immaterial to the consolidated statement of operations for that period.

**Fraternity acquisition expenses.** In connection with the acquisition of Fraternity, the Company incurred merger related costs in fiscal 2017. These expenses were primarily related to legal, other professional services and system conversions. The following table details the expenses included in the consolidated statements of operations for the period shown.

|                               | Fiscal<br>Year<br>Ending<br>March<br>31, 2017 |
|-------------------------------|---|
| Legal                         | \$55,500                                      |
| Professional services         | 157,567                                       |
| Data processing               | -   |
| Advertising                   | -   |
| Other                         | 6,350   |
| Total merger related expenses | \$219,417                                     |

In addition, included in other professional service expense in the Consolidated Statements of Operations for the period ended March 31, 2018 and 2017 is \$305,000 and \$532,000 relating to the amortization of non-compete agreements that have been paid to former executives in the acquisition. The non-compete agreements are for a term of one and two years that end or ended in April 2017 and 2018.

**Note 4: Earnings per Share**

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Basic earnings per share is computed by dividing net income available to common shareholders by the weighted average number of common shares outstanding for the period. Weighted average shares exclude unallocated ESOP shares. Diluted earnings per share reflects the potential dilution that could occur if securities or other contracts to issue common stock were exercised or converted into common stock or resulted in the issuance of common stock that then shared in the earnings of the entity.

Both the basic and diluted earnings per share for the years ended March 31, 2018 and 2017 are summarized below:

|  | <b>Year<br/>Ended<br/>March 31,<br/>2018</b> | Year<br>Ended<br>March 31,<br>2017 |
|--|--|------------------------------------|
| Net loss   | <b>\$(6,048,942)</b>                         | \$(928,782 )                       |
| Weighted average common shares outstanding - basic   | <b>3,192,011</b>                             | 3,180,292                          |
| Weighted average common shares outstanding - diluted | <b>3,192,011</b>                             | 3,180,292                          |
| Loss per common share - basic and diluted            | <b>\$(1.90 )</b>                             | \$(0.29 )                          |
| Anti-dilutive shares                                 | <b>175,177</b>                               | 118,911                            |

During the years ended March 31, 2018 and 2017, none of the common stock equivalents were dilutive due to the loss reported for each period.

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## HAMILTON BANCORP, INC. AND SUBSIDIARY

## Notes to Consolidated Financial Statements (Continued)

**Note 5: Cash and Due From Banks**

Regulation D of the Federal Reserve Act requires that banks maintain reserve balances with the Federal Reserve Bank based principally on the type and amount of their deposits. During fiscal years 2018 and 2017, the Company maintained balances at the Federal Reserve (in addition to vault cash) to meet the reserve requirements, as well as balances to partially compensate for services. Additionally, the Company maintained balances with the Federal Home Loan Bank and other domestic correspondent financial institutions as partial compensation for services they provided to the Company. The Bank normally carries balances with other correspondent financial institutions that exceed the federally insured limit.

**Note 6: Investment Securities Available for Sale**

The amortized cost and fair value of securities at March 31, 2018 and 2017, is summarized as follows:

|                              | Amortized<br>cost | Gross<br>unrealized<br>gains | Gross<br>unrealized<br>losses | Fair<br>value |
|------------------------------|-------------------|------------------------------|-------------------------------|---------------|
| <b><u>March 31, 2018</u></b> |                   |                              |                               |               |
| U.S. government agencies     | \$2,753,346       | \$ -                         | \$34,697                      | \$2,718,649   |
| Municipal bonds              | 12,435,068        | -                            | 729,077                       | 11,705,991    |
| Corporate bonds              | 2,000,000         | -                            | 45,924                        | 1,954,076     |
| Mortgage-backed securities   | 61,078,665        | 12,993                       | 2,066,238                     | 59,025,420    |
|                              | \$78,267,079      | \$ 12,993                    | \$2,875,936                   | \$75,404,136  |

|                              | Amortized<br>cost | Gross<br>unrealized<br>gains | Gross<br>unrealized<br>losses | Fair<br>value |
|------------------------------|-------------------|------------------------------|-------------------------------|---------------|
| <b><u>March 31, 2017</u></b> |                   |                              |                               |               |
| U.S. government agencies     | \$3,525,373       | \$ 323                       | \$13,393                      | \$3,512,303   |



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|                            |               |           |             |               |
|----------------------------|---------------|-----------|-------------|---------------|
| Municipal bonds            | 17,096,477    | 21,858    | 950,496     | 16,167,839    |
| Corporate bonds            | 2,000,000     | -         | 83,478      | 1,916,522     |
| Mortgage-backed securities | 81,994,305    | 65,094    | 1,226,935   | 80,832,464    |
|                            | \$104,616,155 | \$ 87,275 | \$2,274,302 | \$102,429,128 |

Proceeds from sales of investment securities were \$11,608,699 and \$4,273,234 during the years ended March 31, 2018 and 2017, respectively, with gains of \$57,099 and losses of \$59,455 for the year ended March 31, 2018 and gains of \$35,441 and losses of \$9,995 for the year ended March 31, 2017. During fiscal 2017, we also sold certificates of deposits that were held as investments. Proceeds associated with those certificates of deposits were \$1,730,273 with losses of \$1,726.

As of March 31, 2018 and 2017, all mortgage-backed securities are backed by U.S. Government- Sponsored Enterprises (GSE), except one private label mortgage-backed security that was acquired in the Fraternity acquisition in May 2016 with a book value of \$75,645 and fair value of \$76,803 as of March 31, 2018.

As of March 31, 2018 and 2017, the Company had pledged one security to the Federal Reserve Bank with a book value of \$744,186 and \$744,186 and a fair value of \$723,023 and \$736,412, respectively.

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## HAMILTON BANCORP, INC. AND SUBSIDIARY

## Notes to Consolidated Financial Statements (Continued)

The amortized cost and estimated fair value of debt securities by contractual maturity at March 31, 2018 and 2017 follow. Actual maturities may differ from contractual maturities because borrowers may have the right to call or prepay obligations.

|  | Available for Sale  |                     | March 31, 2017 |               |
|--|---------------------|---------------------|----------------|---------------|
|  | Amortized cost      | Fair value          | Amortized cost | Fair value    |
| Maturing                                 |                     |                     |                |               |
| Within one year                          | <b>\$2,009,160</b>  | <b>\$1,995,625</b>  | \$-            | \$-           |
| Over one to five years                   | <b>1,231,928</b>    | <b>1,196,368</b>    | 4,234,642      | 4,240,740     |
| Over five to ten years                   | <b>3,578,827</b>    | <b>3,500,641</b>    | 5,538,313      | 5,404,810     |
| Over ten years                           | <b>10,368,499</b>   | <b>9,686,082</b>    | 12,848,895     | 11,951,114    |
| Mortgage-backed, in monthly installments | <b>61,078,665</b>   | <b>59,025,420</b>   | 81,994,305     | 80,832,464    |
|  | <b>\$78,267,079</b> | <b>\$75,404,136</b> | \$104,616,155  | \$102,429,128 |

The following table presents the Company's investments' gross unrealized losses and the corresponding fair values by investment category and length of time that the securities have been in a continuous unrealized loss position at March 31, 2018 and 2017.

|                            | Less than 12 months     |                     | 12 months or longer     |                     | Total                   |                     |
|----------------------------|-------------------------|---------------------|-------------------------|---------------------|-------------------------|---------------------|
|                            | Gross unrealized losses | Fair value          | Gross unrealized losses | Fair value          | Gross unrealized losses | Fair value          |
| <u>March 31, 2018</u>      |                         |                     |                         |                     |                         |                     |
| U.S. government agencies   | <b>\$21,163</b>         | <b>\$723,023</b>    | <b>\$13,534</b>         | <b>\$1,995,625</b>  | <b>\$34,697</b>         | <b>\$2,718,648</b>  |
| Municipal bonds            | -                       | -                   | <b>729,077</b>          | <b>11,705,991</b>   | <b>729,077</b>          | <b>11,705,991</b>   |
| Corporate bonds            | -                       | -                   | <b>45,924</b>           | <b>1,954,076</b>    | <b>45,924</b>           | <b>1,954,076</b>    |
| Mortgage-backed securities | <b>383,987</b>          | <b>15,880,948</b>   | <b>1,682,251</b>        | <b>40,684,836</b>   | <b>2,066,238</b>        | <b>56,565,784</b>   |
|                            | <b>\$405,150</b>        | <b>\$16,603,971</b> | <b>\$2,470,786</b>      | <b>\$56,340,528</b> | <b>\$2,875,936</b>      | <b>\$72,944,499</b> |

|                       | Less than 12 months     |            | 12 months or longer     |            | Total                   |            |
|-----------------------|-------------------------|------------|-------------------------|------------|-------------------------|------------|
|                       | Gross unrealized losses | Fair value | Gross unrealized losses | Fair value | Gross unrealized losses | Fair value |
| <u>March 31, 2017</u> |                         |            |                         |            |                         |            |

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|                            |             |              |           |             |             |              |
|----------------------------|-------------|--------------|-----------|-------------|-------------|--------------|
| U.S. government agencies   | \$13,393    | \$3,256,964  | \$-       | \$-         | \$13,393    | \$3,256,964  |
| Municipal bonds            | 950,496     | 13,982,251   | -         | -           | 950,496     | 13,982,251   |
| Corporate bonds            | -           | -            | 83,478    | 1,916,522   | 83,478      | 1,916,522    |
| Mortgage-backed securities | 941,183     | 66,953,532   | 285,752   | 7,016,746   | 1,226,935   | 73,970,278   |
|                            | \$1,905,072 | \$84,192,747 | \$369,230 | \$8,933,268 | \$2,274,302 | \$93,126,015 |

The unrealized losses that exist are a result of market changes in interest rates since the original purchase. Management systematically evaluates investment securities for other-than-temporary declines in fair value on an annual basis from the date of purchase if the respective security is in a loss position. This analysis requires management to consider various factors, which include (1) duration and magnitude of the decline in value, (2) the financial condition of the issuer or issuers and (3) structure of the security.

An impairment loss is recognized in earnings if any of the following are true: (1) the Company intends to sell the debt security; (2) it is more likely than not that the Company will be required to sell the security before recovery of its amortized cost basis; or (3) the Company does not expect to recover the entire amortized cost basis of the security. In situations where the Company intends to sell or when it is more likely than not that the Company will be required to sell the security, the entire impairment loss must be recognized in earnings. In all other situations, only the portion of the impairment loss representing the credit loss must be recognized in earnings, with the remaining portion being recognized in shareholders' equity as a component of other comprehensive income, net of deferred tax.

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## HAMILTON BANCORP, INC. AND SUBSIDIARY

## Notes to Consolidated Financial Statements (Continued)

**Note 7: Loans Receivable and Allowance for Loan Losses**

Loans receivable at March 31, 2018 and March 31, 2017, consisted of the following:

|  | March 31, 2018 |               |               |            | March 31, 2017 |               |               |            |
|--|----------------|---------------|---------------|------------|----------------|---------------|---------------|------------|
|  | Legacy (1)     | Acquired      | Total Loans   | % of Total | Legacy (1)     | Acquired      | Total Loans   | % of Total |
| Real estate loans:                           |                |               |               |            |                |               |               |            |
| One-to four-family:                          |                |               |               |            |                |               |               |            |
| Residential (2)                              | \$85,248,184   | \$72,749,066  | \$157,997,250 | 40 %       | \$67,126,677   | \$83,892,389  | \$151,019,066 | 44 %       |
| Residential construction                     | 5,450,827      | -             | 5,450,827     | 1 %        | 6,426,076      | -             | 6,426,076     | 2 %        |
| Investor (3)                                 | 9,275,031      | 17,460,809    | 26,735,840    | 7 %        | 6,742,469      | 18,779,644    | 25,522,113    | 8 %        |
| Commercial                                   | 100,403,769    | 11,762,485    | 112,166,254   | 29 %       | 92,665,689     | 14,898,523    | 107,564,212   | 32 %       |
| Commercial construction                      | 5,763,784      | 1,352,019     | 7,115,803     | 2 %        | 1,881,541      | 1,308,652     | 3,190,193     | 1 %        |
| Total real estate loans                      | 206,141,595    | 103,324,379   | 309,465,974   | 80 %       | 174,842,452    | 118,879,208   | 293,721,660   | 87 %       |
| Commercial business (4)                      | 38,302,739     | 1,841,226     | 40,143,965    | 10 %       | 19,518,029     | 2,019,337     | 21,537,366    | 6 %        |
| Home equity loans                            | 13,956,327     | 6,039,462     | 19,995,789    | 5 %        | 13,278,229     | 7,266,141     | 20,544,370    | 6 %        |
| Consumer (5)                                 | 18,849,448     | 766,063       | 19,615,511    | 5 %        | 2,258,836      | 937,600       | 3,196,436     | 1 %        |
| Total Loans                                  | 277,250,109    | 111,971,130   | 389,221,239   | 100%       | 209,897,546    | 129,102,286   | 338,999,832   | 100%       |
| Net deferred loan origination fees and costs | (212,746 )     | -             | (212,746 )    |            | (143,070 )     | -             | (143,070 )    |            |
| Loan premium (discount)                      | 1,922,428      | (510,036 )    | 1,412,392     |            | 619,846        | (543,410 )    | 76,436        |            |
|  | \$278,959,791  | \$111,461,094 | \$390,420,885 |            | \$210,374,322  | \$128,558,876 | \$338,933,198 |            |

- As a result of the acquisition of Fraternity Community Bancorp, Inc., the parent company of Fraternity Federal Savings and Loan, in May 2016 and Fairmount Bancorp, Inc., the parent company of Fairmount Bank, in September 2015, we have segmented the portfolio into two components, loans originated by Hamilton Bank "Legacy" and loans acquired from Fraternity Community Bancorp, Inc. and Fairmount Bancorp, Inc. "Acquired".
- (1) "Legacy" one-to four-family residential real estate loans at March 31, 2018 and 2017 includes \$19.2 million and \$23.4 million of purchased loan pools, respectively.
  - (2) "Investor" loans are residential mortgage loans secured by non-owner occupied one-to four-family properties.
  - (3) "Legacy" commercial business loans at March 31, 2018 includes a \$15.5 million pool of commercial lease loans purchased in June 2017 and \$3.2 million in guaranteed SBA loans purchased in last half of fiscal 2018.
  - (4) "Legacy" consumer loans at March 31, 2018 includes \$19.9 million of purchased loan pools consisting of recreational vehicles that were purchased in August and December 2017.
  - (5)

Residential lending is generally considered to involve less risk than other forms of lending, although payment experience on these loans is dependent on economic and market conditions in the Bank's lending area. Construction loan repayments are generally dependent on the related properties or the financial condition of its borrower or guarantor. Accordingly, repayment of such loans can be more susceptible to adverse conditions in the real estate market and the regional economy.

A substantial portion of the Bank's loan portfolio is real estate loans secured by residential and commercial real estate properties located in the Baltimore metropolitan area. Loans are extended only after evaluation of a customer's creditworthiness and other relevant factors on a case-by-case basis. The Bank generally does not lend more than 75% - 95% of the appraised value of a property, depending on the type of loan, and requires private mortgage insurance on residential mortgages with loan-to-value ratios in excess of 80%. In addition, the Bank generally obtains personal guarantees of repayment from borrowers and/or others for construction loans and disburses the proceeds of those and similar loans only as work progresses on the related projects.

Commercial business loans are made to provide funds for equipment and general corporate needs. Repayment of a loan primarily uses the funds obtained from the operation of the borrower's business. Commercial loans also include lines of credit that are utilized to finance a borrower's short-term credit needs and/or to finance a percentage of eligible receivables and inventory. The Company's loan portfolio also includes equipment leases, which consists of leases for essential commercial equipment used by small to medium sized businesses.

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## HAMILTON BANCORP, INC. AND SUBSIDIARY

## Notes to Consolidated Financial Statements (Continued)

The home equity loans consist of both conforming loans and revolving lines of credit to consumers which are secured by residential real estate. These loans are typically secured with second mortgages on the homes. Consumer loans include share loans, installment loans and, to a lesser extent, personal lines of credit. Share loans represent loans that are collateralized by a certificate of deposit or other deposit product. Installment loans are used by customers to purchase primarily automobiles, but may be used to also purchase boats and recreational vehicles.

The following tables detail activity in the allowance for loan losses by portfolio segment for the fiscal years ended March 31, 2018 and 2017. The allowance for loan losses allocated to each portfolio segment is not necessarily indicative of future losses in any particular portfolio segment and does not restrict the use of the allowance to absorb losses in other portfolio segments.

|                                       | <b>March 31, 2018</b> |                 |                    |                     |                   |               |                 |              |
|---------------------------------------|-----------------------|-----------------|--------------------|---------------------|-------------------|---------------|-----------------|--------------|
|                                       | <b>Residential</b>    | <b>Investor</b> | <b>Commercial</b>  | <b>Commercial</b>   | <b>Commercial</b> | <b>Home</b>   | <b>Consumer</b> | <b>Total</b> |
|                                       | <b>Real</b>           | <b>Real</b>     | <b>Real Estate</b> | <b>Construction</b> | <b>Business</b>   | <b>Equity</b> |                 |              |
|                                       | <b>Estate</b>         | <b>Estate</b>   |                    |                     |                   |               |                 |              |
| <b>Allowance for credit losses:</b>   |                       |                 |                    |                     |                   |               |                 |              |
| Beginning balance                     | \$553,539             | \$35,275        | \$1,375,894        | \$9,031             | \$149,461         | \$70,071      | \$1,544         | \$2,194,815  |
| Charge-offs                           | (19,868)              | (315,663)       | (244,014)          | -                   | (378,694)         | -             | (17,013)        | (975,252)    |
| Recoveries                            | 3,937                 | 18,129          | -                  | -                   | 770               | -             | 4,504           | 27,340       |
| Provision for credit losses           | 71,115                | 313,949         | 121,503            | 24,399              | 902,445           | (612)         | 142,201         | 1,575,000    |
| Ending balance                        | \$608,723             | \$51,690        | \$1,253,383        | \$33,430            | \$673,982         | \$69,459      | \$131,236       | \$2,821,903  |
| <b>Allowance allocated to:</b>        |                       |                 |                    |                     |                   |               |                 |              |
| <u>Legacy Loans:</u>                  |                       |                 |                    |                     |                   |               |                 |              |
| Individually evaluated for impairment | \$266,256             | \$-             | \$-                | \$-                 | \$-               | \$-           | \$-             | \$266,256    |
| Collectively evaluated for impairment | 342,467               | 51,690          | 1,253,383          | 33,430              | 673,982           | 69,459        | 131,236         | 2,555,647    |
| <u>Acquired Loans:</u>                |                       |                 |                    |                     |                   |               |                 |              |
|                                       | \$-                   | \$-             | \$-                | \$-                 | \$-               | \$-           | \$-             | \$-          |

Individually  
evaluated for  
impairment  
Collectively  
evaluated for  
impairment

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## HAMILTON BANCORP, INC. AND SUBSIDIARY

## Notes to Consolidated Financial Statements (Continued)

|                                       | March 31, 2017 |                      |              |              |            |          |           |              |
|---------------------------------------|----------------|----------------------|--------------|--------------|------------|----------|-----------|--------------|
|                                       | Residential    |                      | Commercial   | Commercial   | Commercial | Home     | Consumer  | Total        |
|                                       | Real Estate    | Investor Real Estate | Real Estate  | Construction | Business   | Equity   |           |              |
| Allowance for credit losses:          |                |                      |              |              |            |          |           |              |
| Beginning balance                     | \$259,895      | \$168,132            | \$901,768    | \$42,377     | \$228,199  | \$82,012 | \$19,982  | \$1,702,365  |
| Charge-offs                           | (34,578 )      | (1,801,438 )         | (1,111,320 ) | -            | (1,521 )   | -        | (4,073 )  | (2,952,930 ) |
| Recoveries                            | -              | 11,599               | -            | -            | 29,257     | -        | 9,518     | 50,374       |
| Provision for credit losses           | 328,222        | 1,656,982            | 1,585,446    | (33,346 )    | (106,474 ) | (11,941) | (23,883 ) | 3,395,006    |
| Ending balance                        | \$553,539      | \$35,275             | \$1,375,894  | \$9,031      | \$149,461  | \$70,071 | \$1,544   | \$2,194,815  |
| Allowance allocated to:               |                |                      |              |              |            |          |           |              |
| <u>Legacy</u>                         |                |                      |              |              |            |          |           |              |
| <u>Loans:</u>                         |                |                      |              |              |            |          |           |              |
| Individually evaluated for impairment | \$284,177      | \$-                  | \$-          | \$-          | \$-        | \$-      | \$-       | \$284,177    |
| Collectively evaluated for impairment | 269,362        | 34,093               | 1,375,894    | 9,031        | 149,461    | 70,071   | 1,544     | 1,909,456    |
| <u>Acquired</u>                       |                |                      |              |              |            |          |           |              |
| <u>Loans:</u>                         |                |                      |              |              |            |          |           |              |
| Individually evaluated for impairment | \$-            | \$1,182              | \$-          | \$-          | \$-        | \$-      | \$-       | \$1,182      |
| Collectively evaluated for impairment | -              | -                    | -            | -            | -          | -        | -         | -            |

Our recorded investment in loans at March 31, 2018 and 2017 related to each balance in the allowance for probable loan losses by portfolio segment and disaggregated on the basis of our impairment methodology was as follows:



| March 31, 2018                                 |                            |                         |                           |                            |                        |                |              |               |
|--|----------------------------|-------------------------|---------------------------|----------------------------|------------------------|----------------|--------------|---------------|
|  | Residential<br>Real Estate | Investor<br>Real Estate | Commercial<br>Real Estate | Commercial<br>Construction | Commercial<br>Business | Home<br>Equity | Consumer     | Total         |
| <b>Loans:</b>                                  |                            |                         |                           |                            |                        |                |              |               |
| <u>Legacy</u>                                  |                            |                         |                           |                            |                        |                |              |               |
| <u>Loans:</u>                                  |                            |                         |                           |                            |                        |                |              |               |
| Individually<br>evaluated<br>for<br>impairment | \$1,827,040                | \$60,949                | \$4,356,264               | \$-                        | \$795,410              | \$20,595       | \$34,266     | \$7,094,524   |
| Collectively<br>evaluated<br>for<br>impairment | 88,871,971                 | 9,214,082               | 96,047,505                | 5,763,784                  | 37,507,329             | 13,935,732     | 18,815,182   | 270,155,505   |
| Ending<br>balance                              | \$90,699,011               | \$9,275,031             | \$100,403,769             | \$5,763,784                | \$38,302,739           | \$13,956,327   | \$18,849,448 | \$277,250,105 |
| <u>Acquired</u>                                |                            |                         |                           |                            |                        |                |              |               |
| <u>Loans:</u>                                  |                            |                         |                           |                            |                        |                |              |               |
| individually<br>evaluated<br>for<br>impairment | \$922,252                  | \$444,254               | \$198,938                 | \$-                        | \$-                    | \$-            | \$60,011     | \$1,625,455   |
| collectively<br>evaluated<br>for<br>impairment | 71,826,814                 | 17,016,555              | 11,563,547                | 1,352,019                  | 1,841,226              | 6,039,462      | 706,052      | 110,345,615   |
| Ending<br>balance                              | \$72,749,066               | \$17,460,809            | \$11,762,485              | \$1,352,019                | \$1,841,226            | \$6,039,462    | \$766,063    | \$111,971,109 |
| March 31, 2017                                 |                            |                         |                           |                            |                        |                |              |               |
|  | Residential<br>Real Estate | Investor<br>Real Estate | Commercial<br>Real Estate | Commercial<br>Construction | Commercial<br>Business | Home<br>Equity | Consumer     | Total         |
| <b>Loans:</b>                                  |                            |                         |                           |                            |                        |                |              |               |
| <u>Legacy</u>                                  |                            |                         |                           |                            |                        |                |              |               |
| <u>Loans:</u>                                  |                            |                         |                           |                            |                        |                |              |               |
| Individually<br>evaluated<br>for<br>impairment | \$1,762,417                | \$16,919                | \$1,546,812               | \$-                        | \$753,375              | \$12,040       | \$-          | \$4,091,563   |
| Collectively<br>evaluated<br>for<br>impairment | 71,790,336                 | 6,725,550               | 91,118,877                | 1,881,541                  | 18,764,654             | 13,266,189     | 2,258,836    | 205,805,983   |
| Ending<br>balance                              | \$73,552,753               | \$6,742,469             | \$92,665,689              | \$1,881,541                | \$19,518,029           | \$13,278,229   | \$2,258,836  | \$209,897,546 |

Acquired

Loans:

individually  
evaluated  
for

|             |           |           |     |     |     |          |             |
|-------------|-----------|-----------|-----|-----|-----|----------|-------------|
| \$1,133,646 | \$186,888 | \$204,844 | \$- | \$- | \$- | \$40,107 | \$1,565,485 |
|-------------|-----------|-----------|-----|-----|-----|----------|-------------|

impairment  
collectively

evaluated  
for

|            |            |            |           |           |           |         |             |
|------------|------------|------------|-----------|-----------|-----------|---------|-------------|
| 82,758,743 | 18,592,756 | 14,693,679 | 1,308,652 | 2,019,337 | 7,266,141 | 897,493 | 127,536,801 |
|------------|------------|------------|-----------|-----------|-----------|---------|-------------|

impairment

Ending  
balance

|              |              |              |             |             |             |           |               |
|--------------|--------------|--------------|-------------|-------------|-------------|-----------|---------------|
| \$83,892,389 | \$18,779,644 | \$14,898,523 | \$1,308,652 | \$2,019,337 | \$7,266,141 | \$937,600 | \$129,102,286 |
|--------------|--------------|--------------|-------------|-------------|-------------|-----------|---------------|

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## HAMILTON BANCORP, INC. AND SUBSIDIARY

## Notes to Consolidated Financial Statements (Continued)

Past due loans, segregated by age and class of loans, as March 31, 2018 and 2017, were as follows:

|                           | March 31, 2018 |               |               | March 31, 2017 |               |               |
|---------------------------|----------------|---------------|---------------|----------------|---------------|---------------|
|                           | Legacy         | Acquired      | Total         | Legacy         | Acquired      | Total         |
| Current                   | \$270,807,643  | \$109,972,473 | \$380,780,116 | \$207,328,184  | \$128,769,860 | \$336,098,044 |
| Accruing past due loans:  |                |               |               |                |               |               |
| 30-59 days past due:      |                |               |               |                |               |               |
| Real estate loans:        |                |               |               |                |               |               |
| Residential               | 63,618         | 689,364       | 752,982       | 69,618         | -             | 69,618        |
| Investor                  | -              | -             | -             | 320,971        | -             | 320,971       |
| Commercial                | -              | -             | -             | -              | -             | -             |
| Commercial construction   | -              | -             | -             | 113,603        | -             | 113,603       |
| Commercial business       | 135,502        | -             | 135,502       | -              | -             | -             |
| Home equity loans         | -              | -             | -             | -              | -             | -             |
| Consumer                  | 148,876        | -             | 148,876       | -              | -             | -             |
| Total 30-59 days past due | 347,996        | 689,364       | 1,037,360     | 504,192        | -             | 504,192       |
| 60-89 days past due:      |                |               |               |                |               |               |
| Real estate loans:        |                |               |               |                |               |               |
| Residential               | 70,291         | -             | 70,291        | 74,631         | -             | 74,631        |
| Investor                  | -              | -             | -             | -              | -             | -             |
| Commercial                | -              | -             | -             | -              | -             | -             |
| Commercial construction   | -              | -             | -             | -              | -             | -             |
| Commercial business       | 134,524        | -             | 134,524       | -              | -             | -             |
| Home equity loans         | -              | -             | -             | -              | -             | -             |
| Consumer                  | 28,300         | -             | 28,300        | -              | -             | -             |
| Total 60-89 days past due | 233,115        | -             | 233,115       | 74,631         | -             | 74,631        |
| 90 or more days past due: |                |               |               |                |               |               |
| Real estate loans:        |                |               |               |                |               |               |
| Residential               | -              | -             | -             | -              | -             | -             |
| Investor                  | 734,818        | 471,423       | 1,206,241     | -              | 21,030        | 21,030        |
| Commercial                | -              | -             | -             | -              | -             | -             |
|                           | -              | -             | -             | -              | -             | -             |

|                                       |                      |                      |                      |                      |                      |                      |
|---------------------------------------|----------------------|----------------------|----------------------|----------------------|----------------------|----------------------|
| Commercial construction               | -                    | -                    | -                    | -                    | -                    | -                    |
| Commercial business                   | -                    | -                    | -                    | -                    | -                    | -                    |
| Home equity loans                     | -                    | -                    | -                    | -                    | -                    | -                    |
| Consumer                              | -                    | -                    | -                    | -                    | -                    | -                    |
| Total 90 or more days past due        | <b>734,818</b>       | <b>471,423</b>       | <b>1,206,241</b>     | -                    | <b>21,030</b>        | <b>21,030</b>        |
| Total accruing past due loans         | <b>1,315,929</b>     | <b>1,160,787</b>     | <b>2,476,716</b>     | <b>578,823</b>       | <b>21,030</b>        | <b>599,853</b>       |
| Non-accruing loans:                   |                      |                      |                      |                      |                      |                      |
| Real estate loans:                    |                      |                      |                      |                      |                      |                      |
| Residential                           | <b>526,584</b>       | <b>338,060</b>       | <b>864,644</b>       | <b>426,354</b>       | <b>248,663</b>       | <b>675,017</b>       |
| Investor                              | <b>60,949</b>        | <b>300,872</b>       | <b>361,821</b>       | <b>13,976</b>        | <b>57,131</b>        | <b>71,107</b>        |
| Commercial                            | <b>4,356,264</b>     | <b>198,938</b>       | <b>4,555,202</b>     | <b>1,546,812</b>     | -                    | <b>1,546,812</b>     |
| Commercial construction               | -                    | -                    | -                    | -                    | -                    | -                    |
| Commercial business                   | <b>165,285</b>       | -                    | <b>165,285</b>       | -                    | -                    | -                    |
| Home equity loans                     | <b>12,605</b>        | -                    | <b>12,605</b>        | <b>3,397</b>         | -                    | <b>3,397</b>         |
| Consumer                              | <b>4,850</b>         | -                    | <b>4,850</b>         | -                    | <b>5,602</b>         | <b>5,602</b>         |
| Non-accruing loans:                   | <b>5,126,537</b>     | <b>837,870</b>       | <b>5,964,407</b>     | <b>1,990,539</b>     | <b>311,396</b>       | <b>2,301,935</b>     |
| Total Loans                           | <b>\$277,250,109</b> | <b>\$111,971,130</b> | <b>\$389,221,239</b> | <b>\$209,897,546</b> | <b>\$129,102,286</b> | <b>\$338,999,832</b> |
| Nonaccrual interest not accrued:      |                      |                      |                      |                      |                      |                      |
| Real estate loans:                    |                      |                      |                      |                      |                      |                      |
| Residential                           | <b>\$8,250</b>       | <b>\$53,120</b>      | <b>\$61,370</b>      | <b>\$6,460</b>       | <b>\$35,177</b>      | <b>\$41,637</b>      |
| Investor                              | <b>8,513</b>         | <b>15,604</b>        | <b>24,117</b>        | <b>6,982</b>         | <b>23,293</b>        | <b>30,275</b>        |
| Commercial                            | <b>294,619</b>       | -                    | <b>294,619</b>       | <b>109,818</b>       | -                    | <b>109,818</b>       |
| Commercial construction               | -                    | -                    | -                    | -                    | -                    | -                    |
| Commercial business                   | <b>12,891</b>        | -                    | <b>12,891</b>        | -                    | -                    | -                    |
| Home equity loans                     | <b>436</b>           | -                    | <b>436</b>           | <b>66</b>            | -                    | <b>66</b>            |
| Consumer                              | <b>385</b>           | -                    | <b>385</b>           | -                    | <b>317</b>           | <b>317</b>           |
| Total nonaccrual interest not accrued | <b>\$325,094</b>     | <b>\$68,724</b>      | <b>\$393,818</b>     | <b>\$123,326</b>     | <b>\$58,787</b>      | <b>\$182,113</b>     |

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## HAMILTON BANCORP, INC. AND SUBSIDIARY

## Notes to Consolidated Financial Statements (Continued)

Impaired Loans as of March 31, 2018 and 2017 were as follows:

|                                     | <b>Impaired Loans at March 31, 2018</b> |            |           |            |            |
|-------------------------------------|---|------------|-----------|------------|------------|
|                                     | Unpaid                                  |            |           | Average    | Interest   |
|                                     | Contractual                             | Recorded   | Related   | Recorded   | Income     |
| <b>Legacy:</b>                      | Principal                               | Investment | Allowance | Investment | Recognized |
|                                     | Balance                                 |            |           |            |            |
| With no related allowance recorded: |   |            |           |            |            |
| Real estate loans:                  |   |            |           |            |            |
| Residential                         | \$665,051                               | \$517,600  | \$-       | \$548,636  | \$ 9,257   |
| Investor                            | 126,389                                 | 60,949     | -         | 118,175    | 3,772      |
| Commercial                          | 6,487,088                               | 4,356,264  | -         | 4,634,504  | 1,077      |
| Commercial construction             | -                                       | -          | -         | -          | -          |
| Commercial business                 | 1,562,756                               | 795,410    | -         | 1,082,773  | 103,474    |
| Home equity loans                   | 47,650                                  | 20,595     | -         | 22,604     | 392        |
| Consumer                            | 48,115                                  | 34,266     | -         | 38,514     | 1,576      |
| With an allowance recorded:         |   |            |           |            |            |
| Real estate loans:                  |   |            |           |            |            |
| Residential                         | 1,336,078                               | 1,309,440  | 266,256   | 1,328,919  | 51,928     |
| Investor                            | -                                       | -          | -         | -          | -          |
| Commercial                          | -                                       | -          | -         | -          | -          |
| Commercial construction             | -                                       | -          | -         | -          | -          |
| Commercial business                 | -                                       | -          | -         | -          | -          |
| Home equity loans                   | -                                       | -          | -         | -          | -          |
| Consumer                            | -                                       | -          | -         | -          | -          |
| Total legacy impaired               | 10,273,127                              | 7,094,524  | 266,256   | 7,774,125  | 171,476    |
| <b>Acquired (1):</b>                |   |            |           |            |            |
| With no related allowance recorded: |   |            |           |            |            |
| Real estate loans:                  |   |            |           |            |            |
| Residential                         | 1,082,484                               | 922,252    | -         | 945,602    | 26,437     |
| Investor                            | 682,045                                 | 444,254    | -         | 659,246    | 37,368     |
| Commercial                          | 248,938                                 | 198,938    | -         | 201,519    | 7,336      |
| Commercial construction             | -                                       | -          | -         | -          | -          |
| Commercial business                 | -                                       | -          | -         | -          | -          |
| Home equity loans                   | 40,473                                  | -          | -         | -          | 1,329      |
| Consumer                            | 95,986                                  | 60,371     | -         | 64,013     | 6,062      |
| With an allowance recorded:         |   |            |           |            |            |
| Real estate loans:                  |   |            |           |            |            |
| Residential                         | -                                       | -          | -         | -          | -          |

|                         |                     |                    |                  |                    |                  |
|-------------------------|---------------------|--------------------|------------------|--------------------|------------------|
| Investor                | -                   | -                  | -                | -                  | -                |
| Commercial              | -                   | -                  | -                | -                  | -                |
| Commercial construction | -                   | -                  | -                | -                  | -                |
| Commercial business     | -                   | -                  | -                | -                  | -                |
| Home equity loans       | -                   | -                  | -                | -                  | -                |
| Consumer                | -                   | -                  | -                | -                  | -                |
| Total acquired impaired | <b>2,149,926</b>    | <b>1,625,815</b>   | -                | <b>1,870,380</b>   | <b>78,532</b>    |
| Total impaired          | <b>\$12,423,053</b> | <b>\$8,720,339</b> | <b>\$266,256</b> | <b>\$9,644,505</b> | <b>\$250,008</b> |

(1) Generally accepted accounting principles require that we record acquired loans at fair value at acquisition, which includes a discount for loans with credit impairment. These purchased credit impaired loans are not performing according to their contractual terms and meet the definition of an impaired loan. Although we do not accrue interest income at the contractual rate on these loans, we do recognize an accretable

yield as  
interest  
income to  
the extent  
such yield is  
supported by  
cash flow  
analysis of  
the  
underlying  
loans.

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## HAMILTON BANCORP, INC. AND SUBSIDIARY

## Notes to Consolidated Financial Statements (Continued)

**Impaired Loans at March 31, 2017**

|                                     | Unpaid Contractual |            |           | Average    | Interest   |
|-------------------------------------|--------------------|------------|-----------|------------|------------|
|                                     | Principal          | Recorded   | Related   | Recorded   | Income     |
| <b>Legacy:</b>                      | Balance            | Investment | Allowance | Investment | Recognized |
| With no related allowance recorded: |                    |            |           |            |            |
| Real estate loans:                  |                    |            |           |            |            |
| Residential                         | \$491,249          | \$360,590  | \$-       | \$373,618  | \$ 11,901  |
| Investor                            | 107,710            | 16,919     | -         | 16,306     | -          |
| Commercial                          | 3,433,621          | 1,546,812  | -         | 2,485,299  | 987        |
| Commercial construction             | -                  | -          | -         | -          | -          |
| Commercial business                 | 1,177,632          | 753,375    | -         | 832,437    | 107,063    |
| Home equity loans                   | 37,365             | 12,040     | -         | 14,102     | 257        |
| Consumer                            | -                  | -          | -         | -          | -          |
| With an allowance recorded:         |                    |            |           |            |            |
| Real estate loans:                  |                    |            |           |            |            |
| Residential                         | 1,432,212          | 1,401,827  | 284,177   | 1,428,128  | 54,121     |
| Investor                            | -                  | -          | -         | -          | -          |
| Commercial                          | -                  | -          | -         | -          | -          |
| Commercial construction             | -                  | -          | -         | -          | -          |
| Commercial business                 | -                  | -          | -         | -          | -          |
| Home equity loans                   | -                  | -          | -         | -          | -          |
| Consumer                            | -                  | -          | -         | -          | -          |
| Total legacy impaired               | 6,679,789          | 4,091,563  | 284,177   | 5,149,890  | 174,329    |
| <b>Acquired (1):</b>                |                    |            |           |            |            |
| With no related allowance recorded: |                    |            |           |            |            |
| Real estate loans:                  |                    |            |           |            |            |
| Residential                         | 1,320,985          | 1,133,646  | -         | 1,017,399  | 51,442     |
| Investor                            | 503,920            | 148,506    | -         | 230,757    | 12,229     |
| Commercial                          | 254,844            | 204,844    | -         | 208,057    | 7,770      |
| Commercial construction             | -                  | -          | -         | -          | -          |
| Commercial business                 | -                  | -          | -         | -          | -          |
| Home equity loans                   | -                  | -          | -         | -          | -          |
| Consumer                            | 88,276             | 40,107     | -         | 44,079     | 6,049      |
| With an allowance recorded:         |                    |            |           |            |            |
| Real estate loans:                  |                    |            |           |            |            |
| Residential                         | -                  | -          | -         | -          | -          |
| Investor                            | 66,446             | 38,382     | 1,182     | 34,448     | -          |
| Commercial                          | -                  | -          | -         | -          | -          |
| Commercial construction             | -                  | -          | -         | -          | -          |
| Commercial business                 | -                  | -          | -         | -          | -          |



|                         |                    |                    |                  |                    |                  |
|-------------------------|--------------------|--------------------|------------------|--------------------|------------------|
| Home equity loans       | -                  | -                  | -                | -                  | -                |
| Consumer                | -                  | -                  | -                | -                  | -                |
| Total acquired impaired | <b>2,234,471</b>   | <b>1,565,485</b>   | <b>1,182</b>     | <b>1,534,740</b>   | <b>77,490</b>    |
| Total impaired          | <b>\$8,914,260</b> | <b>\$5,657,048</b> | <b>\$285,359</b> | <b>\$6,684,630</b> | <b>\$251,819</b> |

(1) Generally accepted accounting principles require that we record acquired loans at fair value at acquisition, which includes a discount for loans with credit impairment. These purchased credit impaired loans are not performing according to their contractual terms and meet the definition of an impaired loan. Although we do not accrue interest income at the contractual rate on these loans, we do recognize an accretable yield as interest income to the extent

such yield is supported by cash flow analysis of the underlying loans.

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## HAMILTON BANCORP, INC. AND SUBSIDIARY

## Notes to Consolidated Financial Statements (Continued)

The following table documents changes in the carrying amount of acquired impaired loans (Purchase Credit Impaired of "PCI") for the years ended March 31, along with the outstanding balance at the end of the period:

|  | 2018         | 2017         |
|--|--------------|--------------|
| Recorded investment at beginning of period     | \$ 1,341,935 | \$ 919,729   |
| Fair value of loans acquired during the year   | -            | 1,027,518    |
| Accretion                                      | 27,744       | 28,036       |
| Reductions for payments                        | (348,255 )   | (633,348 )   |
| Recorded investment at end of period           | \$ 1,021,424 | \$ 1,341,935 |
| Outstanding principal balance at end of period | \$ 1,274,022 | \$ 1,691,004 |

A summary of changes in the accretable yield for PCI loans for the years ended March 31, is as follows:

|  | 2018      | 2017      |
|--|-----------|-----------|
| Accretable yield, beginning of period          | \$ 59,639 | \$ 32,629 |
| Addition from acquisition                      | -         | 55,046    |
| Accretion                                      | (27,744)  | (28,036)  |
| Reclassification from nonaccretable difference | -         | -         |
| Other changes, net                             | -         | -         |
| Accretable yield, end of period                | \$ 31,895 | \$ 59,639 |

Impaired loans also include certain loans that have been modified in troubled debt restructurings (TDRs) where economic concessions have been granted to borrowers who have experienced or are expected to experience financial difficulties. These concessions typically result from the Bank's loss mitigation activities and could include reductions in the interest rate, payment extensions, forgiveness of principal, forbearance or other actions. Generally, nonaccrual loans that are modified and considered TDRs are classified as nonperforming at the time of restructure and may only be returned to performing status after considering the borrower's sustained repayment performance for a reasonable period, generally six months.

A summary of TDRs at March 31, 2018 and 2017 follows:

|                         | Number<br>of<br>contracts | Performing         | Nonperforming       | Total              |
|-------------------------|---------------------------|--------------------|---------------------|--------------------|
| <b>March 31, 2018</b>   |                           |                    |                     |                    |
| Real estate loans:      |                           |                    |                     |                    |
| Residential             | <b>15</b>                 | <b>\$1,230,166</b> | <b>\$ 312,964</b>   | <b>\$1,543,130</b> |
| Investor                | -                         | -                  | -                   | -                  |
| Commercial              | <b>2</b>                  | -                  | <b>1,195,421</b>    | <b>1,195,421</b>   |
| Commercial construction | -                         | -                  | -                   | -                  |
| Commercial business     | <b>1</b>                  | <b>605,488</b>     | -                   | <b>605,488</b>     |
| Home equity loans       | -                         | -                  | -                   | -                  |
| Consumer                | -                         | -                  | -                   | -                  |
|                         | <b>18</b>                 | <b>\$1,835,654</b> | <b>\$ 1,508,385</b> | <b>\$3,344,039</b> |

|                         | Number<br>of<br>contracts | Performing         | Nonperforming       | Total              |
|-------------------------|---------------------------|--------------------|---------------------|--------------------|
| <b>March 31, 2017</b>   |                           |                    |                     |                    |
| Real estate loans:      |                           |                    |                     |                    |
| Residential             | <b>13</b>                 | <b>\$1,261,603</b> | <b>\$ 294,968</b>   | <b>\$1,556,571</b> |
| Investor                | -                         | -                  | -                   | -                  |
| Commercial              | <b>2</b>                  | -                  | <b>1,546,812</b>    | <b>1,546,812</b>   |
| Commercial construction | -                         | -                  | -                   | -                  |
| Commercial business     | <b>1</b>                  | <b>643,999</b>     | -                   | <b>643,999</b>     |
| Home equity loans       | -                         | -                  | -                   | -                  |
| Consumer                | -                         | -                  | -                   | -                  |
|                         | <b>16</b>                 | <b>\$1,905,602</b> | <b>\$ 1,841,780</b> | <b>\$3,747,382</b> |

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## HAMILTON BANCORP, INC. AND SUBSIDIARY

## Notes to Consolidated Financial Statements (Continued)

The following table presents the number of contracts and the dollar amount of TDRs that were added during the years ended March 31, 2018 and 2017. The amount shown reflects the outstanding loan balance at the time of the modification.

|  | <b>Loans Modified as a TDR for the fiscal year ended</b> |                                     |
|--|--|-------------------------------------|
|  | <b>March 31, 2018</b>                                    | <b>March 31, 2017</b>               |
| <b>Number of recorded Troubled Debt Restructurings contracts</b> | <b>Number of recorded contracts</b>                      | <b>Number of recorded contracts</b> |
|  | <b>Investment</b>  | <b>Investment</b>                   |
| Real estate loans:   |  |                                     |
| Residential  | <b>3 \$ 52,363</b>                                       | <b>3 \$ 97,401</b>                  |

There are no TDRs outstanding that defaulted over the twelve-month period ended March 31, 2018 and 2017. Earlier in fiscal 2017, there were 11 newly added TDR loans to one borrower for non-owner occupied residential real estate properties that had subsequently defaulted within twelve months. However, these loans were sold as part of a larger pool of loans in October 2016 and are no longer being reflected in these financial statements. Payment default under a TDR is defined as any TDR that is 90 days or more past due following the time that the loan was modified or the inability of the TDR to make the required payment subsequent to the modification. There are no commitments to extend credit under existing TDRs as of March 31, 2018.

In calculating the allowance for loan losses, individual TDRs are evaluated for impairment. TDRs are evaluated for impairment based upon either the present value of cash flows or, if collateral dependent, the lower of cost or fair value of the underlying collateral. If it is determined that the cash flows or underlying collateral is less than the carrying amount of the loan, the difference in value will be charged-off through earnings, unless the TDR is performing, in which case a specific reserve may be set-up for that TDR.

***Credit quality indicators***

As part of the ongoing monitoring of the credit quality of the Bank's loan portfolio, management tracks certain credit quality indicators including trends related to the risk grade of loans, the level of classified loans, net charge offs, nonperforming loans, and the general economic conditions in the Bank's market.

The Bank utilizes a risk grading matrix to assign a risk grade to each of its loans. A description of the general characteristics of loans characterized as watch list or classified is as follows:

***Pass***

A pass loan is considered of sufficient quality to preclude a special mention or an adverse rating. Pass assets generally are well protected by the current net worth and paying capacity of the obligor or by the value of the asset or underlying collateral.

***Special Mention***

A special mention loan has potential weaknesses that deserve management's close attention. If left uncorrected, these potential weaknesses may result in deterioration of the repayment prospects for the loan or in the Bank's credit position at some future date. Special mention loans are not adversely classified and do not expose the Bank to sufficient risk to warrant adverse classification.

Loans that would primarily fall into this notational category could have been previously classified adversely, but the deficiencies have since been corrected. Management should closely monitor recent payment history of the loan and value of the collateral.

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HAMILTON BANCORP, INC. AND SUBSIDIARY

Notes to Consolidated Financial Statements (Continued)

Borrowers may exhibit poor liquidity and leverage positions resulting from generally negative cash flow or negative trends in earnings. Access to alternative financing may be limited to finance companies for business borrowers and may be unavailable for commercial real estate borrowers.

***Substandard***

A substandard loan is inadequately protected by the current sound worth and paying capacity of the obligor or of the collateral pledged, if any. Substandard loans have a well-defined weakness, or weaknesses, that jeopardize the collection or liquidation of the debt. They are characterized by the distinct possibility that the Bank will sustain some loss if the deficiencies are not corrected. This will be the measurement for determining if a loan is impaired.

Borrowers may exhibit recent or unexpected unprofitable operations, an inadequate debt service coverage ratio, or marginal liquidity and capitalization. These loans require more intense supervision by Bank management.

***Doubtful***

A doubtful loan has all the weaknesses inherent as a substandard loan 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. A loan classified as doubtful exhibits loss potential. However, there is still sufficient reason to permit the loan to remain on the books. A doubtful classification could reflect the deterioration of the primary source of repayment and serious doubt exists as to the quality of the secondary source of repayment.

Doubtful classifications should be used only when a distinct and known possibility of loss exists. When identified, adequate loss should be recorded for the specific assets. The entire asset should not be classified as doubtful if a partial recovery is expected, such as liquidation of the collateral or the probability of a private mortgage insurance payment is likely.

***Loss***

Loans classified as loss are considered uncollectable and of such little value that their continuance as loans is unjustified. A loss classification does not mean a loan has absolutely no value; partial recoveries may be received in the future. When loans or portions of a loan are considered a loss, it will be the policy of the Bank to write-off the amount designated as a loss. Recoveries will be treated as additions to the allowance for loan losses.

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## HAMILTON BANCORP, INC. AND SUBSIDIARY

## Notes to Consolidated Financial Statements (Continued)

The following tables present the March 31, 2018 and 2017 balances of classified loans based on the risk grade. Classified loans include Special Mention, Substandard, Doubtful, and Loss loans. The Bank had no loans classified as Doubtful or Loss as of March 31, 2018 or 2017.

|                           | March 31, 2018 |              |               | March 31, 2017 |              |               |
|---------------------------|----------------|--------------|---------------|----------------|--------------|---------------|
|                           | LEGACY         | ACQUIRED     | TOTAL         | LEGACY         | ACQUIRED     | TOTAL         |
| <u>Risk Rating:</u>       |                |              |               |                |              |               |
| Rating - Pass:            |                |              |               |                |              |               |
| Real estate loans:        |                |              |               |                |              |               |
| Residential               | \$87,863,805   | \$70,901,293 | \$158,765,098 | \$71,721,341   | \$81,228,457 | \$152,949,798 |
| Investor                  | 9,214,082      | 16,719,346   | 25,933,428    | 6,728,493      | 18,151,533   | 24,880,026    |
| Commercial                | 92,955,370     | 11,563,547   | 104,518,917   | 84,789,748     | 13,387,987   | 98,177,735    |
| Commercial construction   | 5,763,784      | 1,352,019    | 7,115,803     | 1,881,541      | 1,308,652    | 3,190,193     |
| Commercial Business       | 37,978,293     | 1,841,226    | 39,819,519    | 19,376,763     | 2,019,337    | 21,396,100    |
| Home Equity               | 13,935,732     | 5,928,787    | 19,864,519    | 13,269,478     | 7,133,164    | 20,402,642    |
| Consumer                  | 18,733,489     | 733,669      | 19,467,158    | 2,258,836      | 896,022      | 3,154,858     |
| Total Pass                | 266,444,555    | 109,039,887  | 375,484,442   | 200,026,200    | 124,125,152  | 324,151,352   |
| Rating - Special Mention: |                |              |               |                |              |               |
| Real estate loans:        |                |              |               |                |              |               |
| Residential               | 2,365,652      | 925,521      | 3,291,173     | 1,499,436      | 1,724,987    | 3,224,423     |
| Investor                  | -              | 297,209      | 297,209       | -              | 408,803      | 408,803       |
| Commercial                | 3,092,135      | -            | 3,092,135     | 6,329,129      | 1,305,692    | 7,634,821     |
| Commercial construction   | -              | -            | -             | -              | -            | -             |
| Commercial Business       | 134,524        | -            | 134,524       | -              | -            | -             |
| Home Equity               | -              | 110,675      | 110,675       | -              | 132,977      | 132,977       |
| Consumer                  | 96,474         | -            | 96,474        | -              | 788          | 788           |
| Total Special Mention     | 5,688,785      | 1,333,405    | 7,022,190     | 7,828,565      | 3,573,247    | 11,401,812    |
| Rating - Substandard:     |                |              |               |                |              |               |
| Real estate loans:        |                |              |               |                |              |               |
| Residential               | 469,554        | 922,252      | 1,391,806     | 331,976        | 938,945      | 1,270,921     |
| Investor                  | 60,949         | 444,254      | 505,203       | 13,976         | 219,308      | 233,284       |
| Commercial                | 4,356,264      | 198,938      | 4,555,202     | 1,546,812      | 204,844      | 1,751,656     |
| Commercial construction   | -              | -            | -             | -              | -            | -             |
| Commercial Business       | 189,922        | -            | 189,922       | 141,266        | -            | 141,266       |

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|                     |                      |                      |                      |                      |                      |                      |
|---------------------|----------------------|----------------------|----------------------|----------------------|----------------------|----------------------|
| Home Equity         | <b>20,595</b>        | -                    | <b>20,595</b>        | <b>8,751</b>         | -                    | <b>8,751</b>         |
| Consumer            | <b>19,485</b>        | <b>32,394</b>        | <b>51,879</b>        | -                    | <b>40,790</b>        | <b>40,790</b>        |
| Total - Substandard | <b>5,116,769</b>     | <b>1,597,838</b>     | <b>6,714,607</b>     | <b>2,042,781</b>     | <b>1,403,887</b>     | <b>3,446,668</b>     |
| Rating - Doubtful   | -                    | -                    | -                    | -                    | -                    | -                    |
| Rating - Loss       | -                    | -                    | -                    | -                    | -                    | -                    |
| <b>TOTAL LOANS</b>  | <b>\$277,250,109</b> | <b>\$111,971,130</b> | <b>\$389,221,239</b> | <b>\$209,897,546</b> | <b>\$129,102,286</b> | <b>\$338,999,832</b> |

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## HAMILTON BANCORP, INC. AND SUBSIDIARY

## Notes to Consolidated Financial Statements (Continued)

In the normal course of business, the Bank has various outstanding commitments and contingent liabilities that are not reflected in the accompanying financial statements. Loan commitments and lines of credit are agreements to lend to a customer as long as there is no violation of any condition to the contract. Mortgage loan commitments generally have fixed interest rates, fixed expiration dates, and may require payment of a fee. Other loan commitments generally have fixed interest rates. Lines of credit generally have variable interest rates. Such lines do not represent future cash requirements because it is unlikely that all customers will draw upon their lines in full at any time.

The Bank's maximum exposure to credit loss in the event of nonperformance by the customer is the contractual amount of the credit commitment. Loan commitments, lines of credit, and letters of credit are made on the same terms, including collateral, as outstanding loans. The Bank has established an off-balance sheet reserve for potential losses associated with any outstanding commitment or unused line of credit. The off-balance sheet reserve is a percentage of the outstanding commitment or unused line of credit that is based upon a discounted charge-off history associated with each respective loan segment. The reserve at March 31, 2018 and 2017 totaled \$50,200 and \$55,200, respectively. At March 31, 2018, management is not aware of any accounting loss to be incurred by funding these loan commitments at this time.

The Bank had the following outstanding commitments and unused lines of credit as of March 31, 2018 and 2017:

|   | <b>March 31,<br/>2018</b> | <b>March 31,<br/>2017</b> |
|---|---------------------------|---------------------------|
| Unused commercial lines of credit         | <b>\$9,187,810</b>        | <b>\$10,733,345</b>       |
| Unused home equity lines of credit        | <b>22,560,376</b>         | <b>22,993,289</b>         |
| Unused consumer lines of credit           | <b>29,331</b>             | <b>1,110,155</b>          |
| Residential construction loan commitments | <b>4,234,076</b>          | <b>8,047,156</b>          |
| Commercial construction loan commitments  | <b>8,968,416</b>          | <b>7,091,564</b>          |
| Home equity loan commitments              | <b>389,600</b>            | <b>84,000</b>             |
| Commercial loan commitments               | <b>5,125,000</b>          | <b>1,089,218</b>          |
| Standby letter of credit                  | <b>250,224</b>            | <b>472,354</b>            |

**Note 8: Related Party Transactions**

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The officers and directors of the Bank enter into loan transactions with the Bank in the ordinary course of business. The terms of these transactions are similar to the terms provided to other borrowers entering into similar loan transactions. All related party loans are subject to review by management and the board of directors.

Activity in these loans during the years ended March 31, 2018 and 2017 was as follows:

|  | <b>2018</b>      | 2017      |
|--|------------------|-----------|
| Balance - Beginning of year            | <b>\$345,314</b> | \$381,948 |
| New loans and lines of credit advances | <b>1,600</b>     | 7,500     |
| Principal repayments                   | <b>(216,960)</b> | (44,134 ) |
| Balance - End of year                  | <b>\$129,954</b> | \$345,314 |

At March 31, 2018 there were no new loans made to related parties during the fiscal year and \$6,150 of credit available under certain lines of credit. At March 31, 2017 there were \$7,500 of new loans made to related parties during the fiscal year and \$6,150 of credit available under lines of credit. Deposits from officers and directors of the Bank totaled \$1,033,558 and \$1,122,872 at March 31, 2018 and 2017, respectively.

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## HAMILTON BANCORP, INC. AND SUBSIDIARY

## Notes to Consolidated Financial Statements (Continued)

**Note 9: Premises and Equipment and Premises and Equipment Held For Sale**

A summary of premises and equipment, excluding premises and equipment held for sale, and the related depreciation and amortization as of March 31, is as follows:

|   | Estimated<br>Useful<br>Life (in<br>years) | 2018               | 2017        |
|---|---|--------------------|-------------|
| Land                                      |   | <b>\$1,064,046</b> | \$1,064,044 |
| Office buildings and improvements         | 3 - 39                                    | <b>3,899,584</b>   | 3,800,195   |
| Furniture and equipment                   | 3 - 7                                     | <b>2,711,893</b>   | 2,602,749   |
| Automobiles                               | 5   | <b>43,505</b>      | 43,505      |
| Assets not in service                     |   | <b>8,448</b>       | 30,900      |
|   |   | <b>7,727,476</b>   | 7,541,393   |
| Accumulated depreciation and amortization |   | <b>(3,781,651)</b> | (3,867,113) |
| Net premises and equipment                |   | <b>\$3,945,825</b> | \$3,674,280 |
| Depreciation and amortization expense     |   | <b>\$325,320</b>   | \$334,210   |

At March 31, 2018, the Bank had four operating leases that include three branches acquired from Fraternity and the administrative office lease in Baltimore County. The administrative office lease was renewed under a five-year option in December 2016, while two of the acquired branches have new leases due to relocation during fiscal 2018. Each of the lease agreements have options to renew at the end of the lease term. Rental expense under the four leases for the year ended March 31, 2018 was \$511,884 compared to lease expense of \$1,002,477 for March 31, 2017. The prior year lease expense includes the \$495,000 in lease expense that is associated with closing one of our branches and the inability to get out of a respective lease agreement. The minimum future rental commitment under the current lease agreements at March 31, 2018 is as follows:

| Year ending March 31, | Payments       |
|-----------------------|----------------|
| 2019                  | <b>521,642</b> |
| 2020                  | <b>543,727</b> |
| 2021                  | <b>480,779</b> |
| 2022                  | <b>353,841</b> |

|            |                    |
|------------|--------------------|
| 2023       | <b>67,054</b>      |
| Thereafter | <b>25,879</b>      |
|            | <b>\$1,992,922</b> |

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## HAMILTON BANCORP, INC. AND SUBSIDIARY

## Notes to Consolidated Financial Statements (Continued)

**Note 10: Goodwill and Other Intangible Assets**

The Company's intangible assets (goodwill and core deposit intangible) at March 31, 2018 consists of assets recorded in December 2009 associated with the acquisition of a branch office in Pasadena, Maryland and the acquisition of Fairmount in September 2015 and the acquisition of Fraternity in May 2016. Only the goodwill related to the branch office acquisition in the amount of \$2.7 million is deductible for tax purposes. We conducted our annual impairment test of goodwill as of December 31, 2017. In addition, due to the significant increase in tax expense resulting from the recording of a valuation allowance on our net deferred tax assets in the fourth quarter of fiscal 2018, we concluded that a triggering event had occurred. Therefore, we performed an additional goodwill impairment analysis during the quarter ending March 31, 2018. Based upon the impairment tests performed as of December 31, 2017 and March 31, 2018, the fair values exceeded the carrying values of our only reporting unit. As a result, no impairment to goodwill was recorded for the period ended March 31, 2018. The core deposit intangible asset is being amortized straight-line over a life of eight years.

The following table presents the changes in net book value of intangible assets for the years ended March 31, 2018 and 2017:

|                               | Goodwill           | Core<br>deposit<br>intangible |
|-------------------------------|--------------------|-------------------------------|
| <b>Balance April 1, 2016</b>  | \$6,767,811        | \$618,300                     |
| Additions (1)                 | 1,877,243          | 242,020                       |
| Post acquisition adjustments  | (81,524 )          | -                             |
| Amortization                  | -                  | (121,022)                     |
| <b>Balance March 31, 2017</b> | <b>8,563,530</b>   | <b>739,298</b>                |
| Amortization                  | -                  | (126,064)                     |
| <b>Balance March 31, 2018</b> | <b>\$8,563,530</b> | <b>\$613,234</b>              |

(1) -  
Additions to  
intangible  
assets are  
related to

the  
acquisition  
of Fraternity  
Community  
Bancorp,  
Inc.

The post-acquisition adjustment to goodwill shown in the table above was recorded in the first quarter of fiscal 2017. The adjustment represents a \$451,000 write-down of several owner-occupied residential investor loans to one borrower that were acquired in the Fairmount acquisition and recording of an increase to the deferred tax asset related to a \$533,000 net operating loss (NOL) from Fairmount's final tax return. With regards to the investor loans, information we were not aware of at the time of the acquisition became available during the quarter ended June 30, 2016. Had we known this information at the time of the acquisition, we would have deemed these loans as impaired and valued them accordingly.

At March 31, 2018, future expected annual amortization associated with the core deposit intangible is as follows:

| Year ending March 31, | Amount           |
|-----------------------|------------------|
| 2019                  | <b>126,070</b>   |
| 2020                  | <b>123,737</b>   |
| 2021                  | <b>98,070</b>    |
| 2022                  | <b>98,070</b>    |
| 2023                  | <b>98,070</b>    |
| 2024                  | <b>64,174</b>    |
| 2025                  | <b>5,043</b>     |
|                       | <b>\$613,234</b> |

#### **Note 11: Derivative – Interest Rate Swap Agreements**

The Company utilizes interest rate swap agreements as part of its asset liability management strategy to help manage its interest rate risk position. The notional amount of the interest rate swaps does not represent amounts exchanged by the parties. The amount exchanged is determined by reference to the notional amount and the other terms of the individual interest rate swap agreements. The Company posted \$751,000 and \$392,000 under collateral arrangements as of March 31, 2018 and 2017, respectively, to satisfy collateral requirements associated with the risk exposure associated with all interest rate swap agreements.

#### *Interest Rate SWAPS Designated as Cash Flow Hedges*



During fiscal 2017, the Company entered into several interest rate swaps that were designated as cash flow hedges. The interest rate swaps have notional amounts totaling \$11.6 million as of March 31, 2018 and were designated as cash flow hedges of certain Federal Home Loan Bank advances. The purpose of the cash flow hedges is to match-fund longer-term assets with longer-term borrowings to reduce potential interest rate risk and cost by swapping a variable rate borrowing for a fixed rate borrowing. The aggregate fair value of the swaps is recorded in other assets (liabilities) with changes in fair value associated with the effective portion recorded in other comprehensive income (loss) and the ineffective portion recorded in other non-interest income. The cash flow hedges were determined to be ineffective during the quarter ended September 30, 2017. As such, a total of \$1,075 of ineffectiveness has been reported in net income for the period ending March 31, 2018.

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## HAMILTON BANCORP, INC. AND SUBSIDIARY

## Notes to Consolidated Financial Statements (Continued)

Summary information about the interest-rate swaps designated as cash flow hedges as of year-end is as follows:

| Interest Rate Swap    | Notional<br>Amount | Effective<br>Start Date | Maturity Date  | Pay           | Receive       |
|-----------------------|--------------------|-------------------------|----------------|---------------|---------------|
|                       |                    |                         |                | Fixed<br>Rate | Floating Rate |
| FHLB Advance Swap 1   | \$ 1,850,000       | March 9, 2017           | March 9, 2022  | 2.24 %        | 3-Month LIBOR |
| FHLB Advance Swap 2   | 1,850,000          | March 9, 2017           | March 9, 2024  | 2.41 %        | 3-Month LIBOR |
| FHLB Advance Swap 3   | 1,850,000          | March 9, 2017           | March 9, 2027  | 2.57 %        | 3-Month LIBOR |
| FHLB Advance Swap 4   | 2,000,000          | March 29, 2017          | March 29, 2022 | 2.08 %        | 3-Month LIBOR |
| FHLB Advance Swap 5   | 2,000,000          | March 29, 2017          | March 29, 2024 | 2.24 %        | 3-Month LIBOR |
| FHLB Advance Swap 6   | 2,000,000          | March 29, 2017          | March 29, 2027 | 2.40 %        | 3-Month LIBOR |
| Total Notional Amount | \$ 11,550,000      |                         |                |               |               |

Interest expense recorded on the swap transactions totaled \$110,926 and \$4,800 for the fiscal years ending March 31, 2018 and 2017 and is reported as a component of interest expense relating to borrowed funds.

The following table reflects cash flow hedges included in the Consolidated Statements of Financial Condition as of March 31, 2018 and 2017:

|  | March 31, 2018     |               | March 31, 2017     |               |
|--|--------------------|---------------|--------------------|---------------|
|  | Notional<br>Amount | Fair<br>Value | Notional<br>Amount | Fair<br>Value |
| Included in assets:                          |                    |               |                    |               |
| Interest rate swaps related to FHLB Advances | \$ 11,550,000      | \$ 217,464    |                    |               |
| Included in liabilities:                     |                    |               |                    |               |
| Interest rate swaps related to FHLB Advances |                    |               | \$ 11,550,000      | \$ 83,634     |

The following tables present the net gains (losses) recorded in accumulated other comprehensive income (loss) and the Consolidated Statements of Operations relating to the cash flow derivative instruments for the fiscal year ended March 31, 2018:

**Fiscal Year Ended March 31, 2018**

| <b>Amount<br/>of Gain<br/>(Loss)<br/>Recognized<br/>in OCI<br/>(Effective<br/>Portion)</b> | <b>Amount of<br/>Gain<br/>(Loss)<br/>Reclassified<br/>from OCI to<br/>Interest<br/>Income</b> | <b>Amount of<br/>Gain<br/>(Loss)<br/>Recognized<br/>in<br/>Other<br/>Noninterest<br/>Income<br/>(Ineffective<br/>Portion)</b> |
|--|---|---|
|--|---|---|

|                         |           |      |             |
|-------------------------|-----------|------|-------------|
| Interest Rate Contracts | \$300,023 | \$ - | \$ (1,075 ) |
|-------------------------|-----------|------|-------------|

*Interest Rate SWAPS Designated as Fair Value Hedges*

The derivative position relates to a transaction in which the Bank entered into an interest rate swap with another financial institution using a fixed rate commercial real estate loan as an offset. The Bank agrees to pay the other financial institution a fixed interest rate on a notional amount based upon the commercial real estate loan and in return receive a variable interest rate on the same notional amount. This transaction allows the Bank to effectively convert a fixed rate loan to a variable rate. Because the terms of the swap with the other financial institution and the commercial real estate loan offset each other, with the only difference being credit risk associated with the loan, changes in the fair value of the underlying derivative contract and the commercial real estate loan are not materially different and do not significantly impact the Bank's results of operations.

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## HAMILTON BANCORP, INC. AND SUBSIDIARY

## Notes to Consolidated Financial Statements (Continued)

During the second quarter of fiscal 2016, the Company entered into the interest rate swap agreement with a \$3.3 million notional amount to convert a fixed rate commercial real estate loan at 3.99% into a variable rate for a term of approximately 10 years. The notional amount of the interest rate swap and the offsetting commercial real estate loan were \$3.1 and \$3.2 million at March 31, 2018 and 2017, respectively. The derivative is designated as a fair value hedge.

Credit risk arises from the possible inability of counterparties to meet the terms of their contracts. The Bank's exposure is limited to the replacement value of the contract rather than the notional amount, principal, or contract amount. There are provisions in the agreement with the counterparty that allow for certain unsecured credit exposure up to an agreed threshold. Exposures in excess of the agreed threshold are collateralized. In addition, the Bank minimizes credit risk through credit approvals, limits, and monitoring procedures.

The fair value hedge is summarized below:

|                                | March 31, 2018     |                     |             | March 31, 2017     |                     |             |
|--------------------------------|--------------------|---------------------|-------------|--------------------|---------------------|-------------|
|                                | Notional<br>Amount | Principal<br>Amount | Fair Value  | Notional<br>Amount | Principal<br>Amount | Fair Value  |
| Included in Loans and Leases:  |                    |                     |             |                    |                     |             |
| Commercial real estate loan    | \$-                | \$3,091,892         | \$3,022,744 | \$-                | \$3,175,044         | \$3,201,691 |
| Included in Other Assets:      |                    |                     |             |                    |                     |             |
| Interest Rate Swap             | \$3,091,892        | \$-                 | \$69,148    | \$-                | -                   | \$-         |
| Included in Other Liabilities: |                    |                     |             |                    |                     |             |
| Interest Rate Swap             | \$-                | -                   | \$-         | \$3,175,044        | -                   | \$26,647    |

No gain or loss was recognized in earnings for the years ended March 31, 2018 and 2017 related to the interest rate swap due to the fact the gain or increase in the fair value of the commercial real estate was offset by the loss or decrease in the fair value of interest rate swap.

**Note 12: Deposits**

The following table details the composition of deposits and the related percentage mix of total deposits, respectively:

|                              | <b>March 31, 2018</b> |              | March 31, 2017 |            |
|------------------------------|-----------------------|--------------|----------------|------------|
|                              | Amount                | % of Total   | Amount         | % of Total |
| Savings                      | <b>\$42,499,381</b>   | <b>11 %</b>  | \$44,614,415   | 11 %       |
| Noninterest-bearing checking | <b>29,557,943</b>     | <b>7 %</b>   | 30,401,454     | 7 %        |
| Interest-bearing checking    | <b>27,219,285</b>     | <b>7 %</b>   | 26,415,189     | 6 %        |
| Money market accounts        | <b>58,466,228</b>     | <b>14 %</b>  | 62,962,902     | 15 %       |
| Time deposits                | <b>246,988,613</b>    | <b>61 %</b>  | 247,632,742    | 60 %       |
|                              | <b>\$404,731,450</b>  | <b>100 %</b> | \$412,026,702  | 100 %      |
| Premium on deposits assumed  | <b>411,525</b>        |              | 829,072        |            |
| Total deposits               | <b>\$405,142,975</b>  |              | \$412,855,774  |            |

The aggregate amount of time deposits in denominations of \$250,000 or more is \$20,633,911 and \$21,594,387 at March 31, 2018 and 2017, respectively.

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## HAMILTON BANCORP, INC. AND SUBSIDIARY

## Notes to Consolidated Financial Statements (Continued)

A schedule of maturity of time deposits at March 31 is as follows:

| <u>Maturity period</u>              | <b>2018</b>          | 2017          |
|-------------------------------------|----------------------|---------------|
| Within one year                     | <b>\$125,075,179</b> | \$124,859,888 |
| Over one year through two years     | <b>64,229,103</b>    | 61,925,008    |
| Over two years through three years  | <b>26,460,307</b>    | 26,005,112    |
| Over three years through four years | <b>18,157,709</b>    | 17,427,002    |
| Over four years through five years  | <b>13,066,315</b>    | 17,393,621    |
| Greater than five years             | -                    | 22,111        |
|                                     | <b>\$246,988,613</b> | \$247,632,742 |

**Note 13: Federal Home Loan Bank Advances and Lines of Credit**

The Bank may borrow up to \$5,000,000 from a correspondent bank under a secured federal funds line of credit and \$1,000,000 under an unsecured federal funds line of credit. The Bank would be required to pledge investment securities to draw upon the secured line of credit. There were no borrowings under these lines of credit at March 31, 2018 and 2017. The Bank also maintained a note payable on an automobile purchased during fiscal 2017. The original amount of the note was \$28,805 with an interest rate of 1.95% for 36 months. The note was paid-off in January 2018.

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## HAMILTON BANCORP, INC. AND SUBSIDIARY

## Notes to Consolidated Financial Statements (Continued)

Borrowings consist of advances from the Federal Home Loan Bank (FHLB). The Bank may borrow up to 25 percent of its assets under a line of credit agreement with the FHLB. Advances under the line of credit are secured by certain loans owned by the Bank. As of March 31, 2018 and 2017, the Bank had \$68.3 million and \$88.2 million, respectively, of available credit from the FHLB. Advances are limited by the balance of loans available for pledge. The amount of loans that were deemed eligible to pledge as collateral totaled \$127.1 million at March 31, 2018 and \$159.1 million at March 31, 2017. As a condition of obtaining the line of credit from the FHLB, the FHLB also requires the Bank purchase shares of capital stock in the FHLB. Information relating to borrowings at March 31, 2018 and 2017 is presented below.

|                                  | March 31, 2018 |       |               | March 31, 2017 |       |               |
|----------------------------------|----------------|-------|---------------|----------------|-------|---------------|
|                                  | Amount         | Rate  | Maturity Date | Amount         | Rate  | Maturity Date |
| FHLB advance (1)                 | \$5,550,000    | 1.84% | 6/11/2018     | \$5,550,000    | 0.94% | 6/9/2017      |
| FHLB advance (2)                 | 6,000,000      | 1.90% | 6/29/2018     | 6,000,000      | 0.93% | 6/29/2017     |
| FHLB advance                     | 1,000,000      | 2.60% | 7/2/2018      | 1,000,000      | 4.24% | 7/31/2017     |
| FHLB advance                     | 1,000,000      | 3.05% | 7/3/2018      | 5,000,000      | 4.28% | 7/31/2017     |
| FHLB advance                     | 5,000,000      | 3.94% | 7/23/2018     | 1,000,000      | 4.01% | 8/21/2017     |
| FHLB advance                     | 1,000,000      | 1.74% | 7/31/2018     | 1,000,000      | 0.91% | 8/31/2017     |
| FHLB advance                     | 1,000,000      | 1.40% | 8/21/2018     | 1,500,000      | 3.23% | 11/24/2017    |
| FHLB advance                     | 4,000,000      | 1.94% | 8/27/2018     | 1,500,000      | 3.40% | 11/27/2017    |
| FHLB advance                     | 3,000,000      | 1.41% | 8/27/2018     | 1,000,000      | 2.60% | 7/2/2018      |
| FHLB advance                     | 5,000,000      | 3.38% | 9/19/2018     | 1,000,000      | 3.05% | 7/3/2018      |
| FHLB advance                     | 1,000,000      | 2.60% | 10/2/2018     | 5,000,000      | 3.94% | 7/23/2018     |
| FHLB advance                     | 1,000,000      | 1.95% | 12/31/2018    | 5,000,000      | 3.38% | 9/19/2018     |
| FHLB advance                     | 3,000,000      | 1.38% | 7/31/2019     | 1,000,000      | 2.60% | 10/2/2018     |
| FHLB advance                     | 3,000,000      | 1.96% | 8/26/2019     | -              | -     | -             |
| FHLB advance                     | 3,000,000      | 1.59% | 8/26/2019     | -              | -     | -             |
| FHLB advance                     | 3,000,000      | 1.42% | 8/26/2019     | -              | -     | -             |
| FHLB advance                     | 1,500,000      | 1.95% | 11/25/2019    | -              | -     | -             |
| FHLB advance                     | 1,500,000      | 1.78% | 11/27/2019    | -              | -     | -             |
| FHLB advance                     | 3,000,000      | 2.31% | 2/3/2020      | -              | -     | -             |
| FHLB advance                     | 1,000,000      | 2.15% | 11/30/2020    | -              | -     | -             |
| FHLB advance                     | 2,000,000      | 2.28% | 12/28/2020    | -              | -     | -             |
| FHLB advance                     | 2,000,000      | 2.49% | 2/1/2021      | -              | -     | -             |
| FHLB advance                     | 3,000,000      | 1.48% | 8/25/2021     | -              | -     | -             |
| Note payable - auto              | -              | -     | -             | 27,250         | 1.95% | 2/17/2020     |
|                                  | 60,550,000     |       |               | 35,577,250     |       |               |
| Premium on FHLB advances assumed | 122,140        |       |               | 547,649        |       |               |
| Total borrowings                 | \$60,672,140   |       |               | \$36,124,899   |       |               |

**FHLB**

Advance is tied to three derivative cash flow hedges in increments of \$1.85 million each. The three individual cash flow hedges are for a term of five, seven and ten years, respectively

(1) - and are tied to the 3-month LIBOR rate.

In order for the cash flow hedges to remain effective, the corresponding FHLB

Advance will have to be renewed every three months until the respective cash flow hedge matures.

(2) - **FHLB**

Advance is tied to three derivative cash flow hedges in increments of \$2.0 million each. The three individual cash flow hedges are for a term of five, seven and ten years, respectively and are tied to



the 3-month LIBOR rate. In order for the cash flow hedges to remain effective, the corresponding FHLB Advance will have to be renewed every three months until the respective cash flow hedge matures.

**Note 14: Income Taxes**

The provisions for income taxes for the years ended March 31, 2018 and 2017 consist of the following components:

|                             | Year Ended March 31, |             |
|-----------------------------|----------------------|-------------|
|                             | 2018                 | 2017        |
| Tax expense (benefit):      |                      |             |
| Current:                    |                      |             |
| Federal                     | <b>\$(22,566 )</b>   | \$(10,911 ) |
| State                       | <b>\$(6,599 )</b>    | (5,193 )    |
| Deferred tax                | <b>8,081,203</b>     | (741,901)   |
| Total tax expense (benefit) | <b>\$8,052,038</b>   | \$(758,005) |

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## HAMILTON BANCORP, INC. AND SUBSIDIARY

## Notes to Consolidated Financial Statements (Continued)

A reconciliation of the provision for taxes on income from the statutory federal income tax rate to the effective income tax rates follows:

|  | Year Ended March 31, |             |
|--|----------------------|-------------|
|  | 2018                 | 2017        |
| Tax at statutory federal income tax rate   | \$615,952            | \$(573,507) |
| Tax effect of:                             |                      |             |
| Tax-exempt income                          | (491,456 )           | (260,637)   |
| State income taxes, net of federal impact  | 42,442               | (90,427 )   |
| Valuation allowance on income tax benefits | 5,790,102            | -           |
| Impact of the Tax Act                      | 2,318,118            | -           |
| Nondeductible expenses and other           | 55,397               | 166,566     |
| Other                                      | (278,517 )           | -           |
| Income tax expense (benefit)               | \$8,052,038          | \$(758,005) |

The following is a summary of the tax effects of the temporary differences and tax attributes between financial and income tax accounting that give rise to deferred tax assets and deferred tax liabilities as of March 31:

|   | 2018        | 2017      |
|---|-------------|-----------|
| Deferred tax assets:  |             |           |
| Allowance for loan losses                                   | \$627,297   | \$887,510 |
| Nonaccrual interest   | 219,172     | 197,363   |
| Deferred compensation                                       | 547,968     | 822,939   |
| Foreclosed real estate write down and holding costs         | 162,973     | 221,010   |
| Deferred loan costs   | 34,870      | 42,285    |
| Capital loss carryforward                                   | -           | 48,872    |
| Charitable contribution carryforward                        | 28,272      | 42,098    |
| Net operating loss carryforward                             | 3,227,274   | 4,414,529 |
| Stock based payment awards                                  | 66,968      | 80,833    |
| Unrealized loss on investment securities available for sale | 728,266     | 862,673   |
| AMT credit carryover  | 245,260     | 225,294   |
| Acquisition activity  | 510,506     | 1,078,763 |
| Other   | 39,692      | -         |
|   | 6,438,518   | 8,924,169 |
| Valuation allowance on deferred tax asset                   | (5,790,102) | (42,364 ) |
|   | 648,416     | 8,881,805 |

|                                      |                |             |
|--------------------------------------|----------------|-------------|
| Deferred tax liabilities:            |                |             |
| FHLB stock dividends                 | <b>63,486</b>  | 91,004      |
| Goodwill and other intangible assets | <b>522,993</b> | 717,933     |
| Accumulated depreciation             | <b>61,937</b>  | 65,193      |
| Other                                | -              | 30,825      |
|                                      | <b>648,416</b> | 904,955     |
| Net deferred tax asset               | \$-            | \$7,976,850 |

Deferred income taxes reflect the impact of “temporary differences” between the amount of assets and liabilities for financial reporting purposes and such amounts as measured by tax laws and regulations. The largest component of our net deferred tax asset at March 31, 2018 was our net operating loss carryforwards and temporary differences related to the activity in our allowance for loan losses and unrealized loss on investment securities available for sale. The Company records a valuation allowance against deferred tax assets if, based on the weight of available evidence, it is more likely than not, that some or all of the deferred tax assets will not be realized. Due to the Company remaining in a cumulative loss position for three consecutive years, management has concluded that it is more likely-than-not that the Company will be unable to realize its deferred tax assets in the foreseeable future, and accordingly has established a full valuation allowance of \$5.8 million which equals 100% of the net deferred tax assets at March 31, 2018. If, in the future, the Company generates taxable income on a sustained basis sufficient to support the deferred tax assets, the need for a deferred tax valuation allowance could change, resulting in the reversal of all or a portion of the deferred tax asset valuation at that time.

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HAMILTON BANCORP, INC. AND SUBSIDIARY

Notes to Consolidated Financial Statements (Continued)

The Company has a federal net operating loss carryforward (NOL) of \$12.0 million as of March 31, 2018, which will expire within the period of the years ending March 31, 2030 through 2037, including \$4.9 million and \$1.9 million of federal NOL assumed in the acquisition of Fraternity and Fairmount, respectively. As a result of the change in ownership, the utilization of Fraternity and Fairmount's NOL carryforwards is subject to limitations imposed under Code Section 382 of the Internal Revenue Code. The state NOL for the Company is \$11.0 million and also expires within the same period as the federal NOL. In addition, other tax attributes consisted of charitable contribution carryforwards of \$102,742 and AMT credit carryovers of \$245,620 at March 31, 2018. Under the Tax Act, the AMT credit carryovers are refundable over a period beginning in 2018. Charitable contribution carryovers have a limited life of five years.

On December 22, 2017, the Tax Act was passed into law. The Tax Act included a broad range of tax reform including changes to tax rates and deductions that were effective January 1, 2018. The primary change for the Company was the lowering of the federal corporate income tax rate to 21% from maximum of 35%. The decrease in the enacted corporate tax rate expected to apply when the Company's temporary differences are realized or settled resulted in a revaluation of the Company's net deferred tax asset of \$2.3 million with a corresponding charge to income tax expense. Based on information available and our current interpretation of the Tax Act, the Company has made reasonable estimates of the impact from the reduction in the corporate tax rate on the remeasurement of applicable deferred tax assets and liabilities. However, certain deferred tax assets and liabilities will continue to be evaluated in the context of the Tax Act through the date of the filing of our March 31, 2018 federal income tax return, and may change as a result of evolving management interpretations, elections, and assumptions, as well as new guidance that may be issued by the Internal Revenue Service. Management expects to complete its analysis within the measurement period in accordance with SAB 118.

The Company's tax returns are subject to review and examination by federal and state taxing authorities. The Company's tax returns are currently open to audit under the applicable statutes of limitations by the Internal Revenue Service for the years ended March 31, 2015 through March 31, 2017. Years in which an NOL is created though are still open for examination. The establishment of a valuation allowance on our deferred tax assets for financial reporting purposes does not affect how the net operating loss carryforwards may be utilized on our subsequent income tax returns. The Company does not have any uncertain tax positions that are deemed material, and did not recognize any adjustments for unrecognized tax benefits.

**Note 15: Regulatory Capital Ratios**

Banks and bank holding companies are subject to various regulatory capital requirements administered by state and federal banking agencies. Capital adequacy guidelines and prompt corrective action regulations for banks, involve quantitative measures of assets, liabilities, and certain off-balance-sheet items calculated under regulatory accounting practices. Capital amounts and classifications are also subject to qualitative judgments by regulators about components, risk weighting and other factors.

The Basel III Capital Rules became effective for Hamilton Bank on January 1, 2015 (subject to a phase-in period for certain provisions). Quantitative measures established by the Basel III Capital Rules to ensure capital adequacy require the maintenance of minimum amounts and ratios (set forth in the table below) of Common Equity Tier 1 capital, Tier 1 capital and Total capital (as defined in the regulations) to risk-weighted assets (as defined), and of Tier 1 capital to adjusted quarterly average assets (as defined).

In connection with the adoption of the Basel III Capital Rules, we elected to opt-out of the requirement to include accumulated other comprehensive income in Common Equity Tier 1. Common Equity Tier 1 for Hamilton Bank is reduced by goodwill and other intangible assets, net of associated deferred tax liabilities and subject to transition provisions.

Under the revised prompt corrective action requirements, as of January 1, 2015, insured depository institutions are required to meet the following in order to qualify as “well capitalized:” (1) a common equity Tier 1 risk-based capital ratio of 6.5%; (2) a Tier 1 risk-based capital ratio of 8%; (3) a total risk-based capital ratio of 10% and (4) a Tier 1 leverage ratio of 5%. As of March 31, 2018, the Bank met all capital adequacy requirements under the Basel III Capital Rules to be considered “well capitalized” under prompt corrective action rules.

The implementation of the capital conservation buffer will begin on January 1, 2016 at the 0.625% level and be phased in over a four-year period (increasing by that amount on each subsequent January 1, until it reaches 2.5% on January 1, 2019). The Basel III Capital Rules also provide for a “countercyclical capital buffer” that is applicable to only certain covered institutions and does not have any current applicability to Hamilton Bank.

The aforementioned capital conservation buffer is designed to absorb losses during periods of economic stress. Banking institutions with a ratio of Common Equity Tier 1 capital to risk-weighted assets above the minimum but below the conservation buffer (or below the combined capital conservation buffer and countercyclical capital buffer, when the latter is applied) will face constraints on dividends, equity repurchases and compensation based on the amount of the shortfall.

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## HAMILTON BANCORP, INC. AND SUBSIDIARY

## Notes to Consolidated Financial Statements (Continued)

The following table presents actual and required capital ratios as of March 31, 2018 and March 31, 2017 for Hamilton Bank and the Company under the Basel III Capital Rules. The minimum required capital amounts presented include the minimum required capital levels as of January 1, 2018 based on the phase-in provisions of the Basel III Capital Rules and the minimum required capital levels as of January 1, 2019 when the Basel III Capital Rules have been fully phased-in. Capital levels required to be considered well capitalized are based upon prompt corrective action regulations, as amended to reflect the changes under the Basel III Capital Rules.

|  | Actual   |         | Minimum Capital Required - Basel III Phase-In Schedule |         | Minimum Capital Required - Basel III Fully Phased-In |         | To be well capitalized (1) |         |
|--|----------|---------|--|---------|--|---------|----------------------------|---------|
|  | Amount   | Ratio   | Amount   | Ratio   | Amount   | Ratio   | Amount                     | Ratio   |
|  |          |         | <i>(dollars in thousands)</i>                          |         | <i>(dollars in thousands)</i>                        |         |                            |         |
| <b>March 31, 2018</b>                                  |          |         |  |         |  |         |                            |         |
| Common equity tier 1 capital (to risk-weighted assets) |          |         |  |         |  |         |                            |         |
| Hamilton Bank  | \$39,126 | 10.61 % | \$23,498   | 6.375 % | \$25,802   | 7.00 %  | \$23,959                   | 6.50 %  |
| Hamilton Bancorp                                       | 47,308   | 12.79 % | 23,582   | 6.375 % | 25,894   | 7.00 %  | 24,044                     | 6.50 %  |
| Total risk-based capital (to risk-weighted assets)     |          |         |  |         |  |         |                            |         |
| Hamilton Bank  | 41,998   | 11.39 % | 36,399   | 9.875 % | 38,703   | 10.50 % | 36,860                     | 10.00 % |
| Hamilton Bancorp                                       | 50,180   | 13.57 % | 36,529   | 9.875 % | 38,841   | 10.50 % | 36,992                     | 10.00 % |
| Tier 1 capital (to risk-weighted assets)               |          |         |  |         |  |         |                            |         |
| Hamilton Bank  | 39,126   | 10.61 % | 29,027   | 7.875 % | 31,331   | 8.50 %  | 29,488                     | 8.00 %  |
| Hamilton Bancorp                                       | 47,308   | 12.79 % | 29,131   | 7.875 % | 31,443   | 8.50 %  | 29,593                     | 8.00 %  |
| Tier 1 capital (to adjusted total assets)              |          |         |  |         |  |         |                            |         |
| Hamilton Bank  | 39,126   | 7.64 %  | 20,497   | 4.000 % | 20,497   | 4.00 %  | 25,621                     | 5.00 %  |
| Hamilton Bancorp                                       | 47,308   | 8.15 %  | 20,674   | 4.000 % | 20,674   | 4.00 %  | 25,843                     | 5.00 %  |

March 31, 2017

Common equity tier 1 capital (to risk-weighted assets)

|               |          |         |          |         |          |        |          |        |
|---------------|----------|---------|----------|---------|----------|--------|----------|--------|
| Hamilton Bank | \$40,084 | 12.13 % | \$18,996 | 5.750 % | \$23,126 | 7.00 % | \$21,474 | 6.50 % |
|---------------|----------|---------|----------|---------|----------|--------|----------|--------|

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|  |        |         |        |         |        |         |          |         |
|--|--------|---------|--------|---------|--------|---------|----------|---------|
| Hamilton Bancorp                                   | 48,318 | 14.56 % | 19,078 | 5.750 % | 23,225 | 7.00 %  | \$21,566 | 6.50 %  |
| Total risk-based capital (to risk-weighted assets) |        |         |        |         |        |         |          |         |
| Hamilton Bank                                      | 42,334 | 12.81 % | 30,559 | 9.250 % | 34,689 | 10.50 % | 33,037   | 10.00 % |
| Hamilton Bancorp                                   | 50,568 | 15.24 % | 30,690 | 9.250 % | 34,838 | 10.50 % | 33,179   | 10.00 % |
| Tier 1 capital (to risk-weighted assets)           |        |         |        |         |        |         |          |         |
| Hamilton Bank                                      | 40,084 | 12.13 % | 23,952 | 7.250 % | 28,081 | 8.50 %  | 26,429   | 8.00 %  |
| Hamilton Bancorp                                   | 48,318 | 14.56 % | 24,055 | 7.250 % | 28,202 | 8.50 %  | 26,543   | 8.00 %  |
| Tier 1 capital (to adjusted total assets)          |        |         |        |         |        |         |          |         |
| Hamilton Bank                                      | 40,084 | 8.28 %  | 19,365 | 4.000 % | 19,365 | 4.00 %  | 24,207   | 5.00 %  |
| Hamilton Bancorp                                   | 48,318 | 9.96 %  | 19,402 | 4.000 % | 19,402 | 4.00 %  | 24,253   | 5.00 %  |

(1) - Under prompt corrective action

Tier 1 capital consists of total shareholders' equity less goodwill, intangible assets, and deferred tax net operating loss carryforwards. Total capital includes a limited amount of the allowance for loan losses and a portion of any unrealized gain on equity securities. In calculating risk-weighted assets, specified risk percentages are applied to each category of asset and off-balance-sheet items.

Failure to meet the capital requirements could affect, among other things, the Bank's ability to accept brokered deposits and may significantly affect the operations of the Bank. During the quarter ended December 31, 2016, the Company transferred \$3.0 million in cash down to the Bank as capital to increase the Bank's lending capacity and enhance the Bank's capital ratios after falling below the Bank's self-imposed internal minimum capital level in the prior quarter.

In its regulatory report filed as of March 31, 2018, the Bank exceeded all regulatory capital requirements and was considered "well capitalized" under regulatory guidelines. Management is not aware of any events that would have caused this classification to change. Management has no plans that should change the classification of the capital adequacy.

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HAMILTON BANCORP, INC. AND SUBSIDIARY

Notes to Consolidated Financial Statements (Continued)

**Note 16: Defined Contribution Retirement Plan**

The Bank offers a retirement plan qualifying under section 401(k) of the Internal Revenue Code to its employees. The Plan covers all full-time employees with one year of service who have reached 18 years of age. The Bank contributes three percent of each participant's eligible compensation to the Plan. The Bank may make elective deferrals as well, upon Board of Directors approval. During the years ended March 31, 2018 and 2017, the Bank recorded expense of \$174,065 and \$145,082, respectively, related to the 401(k) Plan.

**Note 17: Employee Stock Ownership Plan**

In connection with the conversion to stock form in October 2012, the Company established an Employee Stock Ownership Plan (ESOP) for the exclusive benefit of eligible employees. Eligible employees include all employees over the age of 21 that have completed 1,000 hours of service over a continuous twelve-month period. The ESOP borrowed funds from the Company in the amount of \$2,962,400, which was sufficient to purchase 296,240 shares or 8% of the Common Stock issued in the offering. The shares were acquired at a price of \$10.00 per share.

The loan is secured by the shares purchased with the loan proceeds and will be repaid by the ESOP over the 20-year term of the loan with funds from the Bank's contributions to the ESOP and dividends paid on the stock, if any. The interest rate on the ESOP loan is an adjustable rate equal to the lowest prime rate, as published in the *Wall Street Journal*. The interest rate will adjust annually and will be the prime rate on the first business day of the calendar year. The interest rate on the loan as of March 31, 2018 is 4.50%.

Shares purchased with the loan proceeds are held in a suspense account for allocation among participants as the loan is repaid. Contributions to the ESOP and shares released from the suspense account are allocated among participants in proportion to their annual salaried wages, relative to total salaried wages of all active participants. Participants will vest their accrued benefits under the employee stock ownership plan at a rate of 20% per year, such that the participants will be 100% vested upon completion of five years of credited service. Vesting is accelerated upon retirement, death, or disability of the participant, or a change in control of the Bank. Forfeitures will be reallocated to remaining plan participants. Benefits may be payable upon retirement, death, disability, separation of service, or termination of the ESOP. Participants may elect to receive benefits in cash in lieu of common stock.



The debt of the ESOP, in accordance with generally accepted accounting principles, is eliminated in consolidation and the shares pledged as collateral are reported as unearned ESOP shares in the Consolidated Statement of financial Condition. Contributions to the ESOP shall be sufficient to pay principal and interest currently due under the loan agreement. As shares are committed to be released from collateral, the Company reports compensation expense equal to the fair market price of the shares as they are committed to be released from the unallocated suspense account to participants' accounts. The shares allocated will then become outstanding shares for earnings per share computations. The ESOP compensation expense for the year ended March 31, 2018 and 2017 was \$224,481 and \$235,633, respectively.

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## HAMILTON BANCORP, INC. AND SUBSIDIARY

## Notes to Consolidated Financial Statements (Continued)

A summary of ESOP shares at March 31, 2018 and 2017 is as follows:

|                               | 2018               | 2017        |
|-------------------------------|--------------------|-------------|
| Shares allocated to employees | <b>88,872</b>      | 74,060      |
| Unearned shares               | <b>207,368</b>     | 222,180     |
| Total ESOP shares             | <b>296,240</b>     | 296,240     |
| Fair value of unearned shares | <b>\$2,954,994</b> | \$3,410,463 |

**Note 18: Stock Based Compensation**

In November 2013, the Company's shareholders approved a new Equity Incentive Plan (the "2013 Equity Incentive Plan"). The 2013 Equity Incentive Plan allows for up to 148,120 shares to be issued to employees, executive officers or Directors in the form of restricted stock, and up to 370,300 shares to be issued to employees, executive officers or Directors in the form of stock options. At March 31, 2018, there were 83,900 restricted stock awards issued and outstanding and 247,850 stock option awards granted under the 2013 Equity Incentive Plan.

Stock Options:

Under the above plan, the exercise price for stock options is the market price at date of grant. The maximum option term is ten years and the options granted shall vest in five equal annual installments of 20% with the first installment becoming exercisable on the first anniversary of the date of grant and succeeding installments on each anniversary thereafter. The Company plans to issue new shares to satisfy share option exercises. The total expense that has been incurred for the stock option plan was \$229,569 and \$216,735 for the years ended March 31, 2018 and 2017, respectively.

The fair value of each option award is estimated on the date of grant using a closed form option valuation (Black-Scholes) model that uses the assumptions noted in the table below. Expected volatilities are based on historical data. The Company uses historical data to estimate option exercise and post-vesting termination behavior. The expected term of options granted represents the period of time that options granted are expected to be outstanding, which takes into account that the options are not transferable. The risk-free interest rate for the expected term of the

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option is based on the U.S. Treasury rate equal to the expected term of the option in effect at the time of the grant.

The fair value of options granted to date was determined using the following weighted-average assumptions as of grant date.

| Grant Date       | Number of Options Granted | Risk Free Interest Rate | Expected Term (in years) | Expected Stock Price Volatility | Dividend Yield | Fair Value of Options Granted |
|------------------|---------------------------|-------------------------|--------------------------|---------------------------------|----------------|-------------------------------|
| February 3, 2014 | 225,150                   | 2.07 %                  | 7.0                      | 27.30 %                         | 0.00 %         | \$ 4.65                       |
| November 1, 2016 | 19,000                    | 1.61 %                  | 7.0                      | 27.17 %                         | 0.00 %         | \$ 4.35                       |
| February 3, 2017 | 3,700                     | 2.27 %                  | 7.0                      | 27.26 %                         | 0.00 %         | \$ 5.18                       |

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## HAMILTON BANCORP, INC. AND SUBSIDIARY

## Notes to Consolidated Financial Statements (Continued)

A summary of stock option activity for the year ended March 31, 2018 and 2017 is as follows:

| <u>March 31, 2018:</u>          | Shares         | Weighted<br>Average<br>Exercise<br>Price | Weighted<br>Average<br>Remaining<br>Contractual<br>Term (in<br>years) |
|---------------------------------|----------------|--|---|
| Outstanding at April 1, 2017    | <b>242,350</b> | <b>\$ 13.84</b>                          | 7.1   |
| Granted                         | -              | -  | -   |
| Exercised                       | -              | -  | -   |
| Forfeited, exchanged or expired | -              | -  | -   |
| Outstanding at March 31, 2018   | <b>242,350</b> | <b>\$ 13.84</b>                          | 6.1   |
| Vested at March 31, 2018        | <b>180,260</b> | <b>\$ 13.84</b>                          | 5.8   |

| <u>March 31, 2017:</u>          | Shares  | Weighted<br>Average<br>Exercise<br>Price | Weighted<br>Average<br>Remaining<br>Contractual<br>Term (in<br>years) |
|---------------------------------|---------|--|---|
| Outstanding at April 1, 2016    | 219,650 | \$ 13.85                                 | 7.8   |
| Granted                         | 22,700  | 13.78                                    | 10.0  |
| Exercised                       | -       | -  | -   |
| Forfeited, exchanged or expired | -       | -  | -   |
| Outstanding at March 31, 2017   | 242,350 | \$ 13.84                                 | 7.1   |
| Vested at March 31, 2017        | 131,790 | \$ 13.85                                 | 6.8   |

As of March 31, 2018, there was \$248,272 of total unrecognized compensation cost related to nonvested stock options granted under the Plan. The expense is expected to be recognized over a weighted-average period of 1.7 years. The intrinsic value of a stock option is the amount that the market value of the underlying stock exceeds the exercise price of the option. Based upon a fair market value of \$14.25 at March 31, 2018, the options outstanding had an intrinsic value of \$102,110.

Restricted Stock:

The specific terms of each restricted stock award are determined by the Compensation Committee at the date of the grant. Compensation expense is recognized over the vesting period of the awards based on the fair value of the stock at the grant date. Restricted stock awards granted shall vest in five equal annual installments of 20% with the first installment becoming vested on the first anniversary of the date of grant and succeeding installments on each anniversary thereafter.

A summary of changes in the Company's nonvested shares for the year is as follows:

| <u>March 31, 2018:</u>             | Shares           | Weighted-Average<br>Fair Value |
|------------------------------------|------------------|--------------------------------|
| Nonvested shares at April 1, 2017  | <b>36,220</b>    | <b>\$ 13.76</b>                |
| Granted                            | -                | -                              |
| Vested                             | <b>(16,780 )</b> | <b>13.78</b>                   |
| Forfeited                          | -                | -                              |
| Nonvested shares at March 31, 2018 | <b>19,440</b>    | <b>\$ 13.74</b>                |

Fair Value of shares vested at March 31, 2018 **\$918,555**

| <u>March 31, 2017:</u>             | Shares    | Weighted-Average<br>Fair Value |
|------------------------------------|-----------|--------------------------------|
| Nonvested shares at April 1, 2016  | 50,600    | \$ 13.76                       |
| Granted                            | 2,000     | 13.93                          |
| Vested                             | (16,380 ) | 13.78                          |
| Forfeited                          | -         | -                              |
| Nonvested shares at March 31, 2017 | 36,220    | \$ 13.76                       |

Fair Value of shares vested at March 31, 2017 \$731,888

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HAMILTON BANCORP, INC. AND SUBSIDIARY

Notes to Consolidated Financial Statements (Continued)

The following table outlines the vesting schedule of the nonvested restricted stock awards as of March 31, 2018:

| <b>Year Ending<br/>March 31,</b> | <b>Number of<br/>Restricted Shares</b> |
|----------------------------------|--|
| 2019                             | 16,780                                 |
| 2020                             | 1,780                                  |
| 2021                             | 480                                    |
| 2022                             | 400                                    |
|                                  | 19,440                                 |

The Company recorded restricted stock awards expense of \$231,276 and \$227,646 for the years ended March 31, 2018 and 2017, respectively. As of March 31, 2018, there was \$225,445 of total unrecognized compensation expense related to nonvested shares granted under the 2013 stock incentive plan. The cost is expected to be recognized over a weighted-average period of 1.2 years.

**Note 19: Fair Value Measurements**

Generally accepted accounting principles define fair value, establish a framework for measuring fair value, and establish a hierarchy for determining fair value measurement. The hierarchy includes three levels and is based upon the valuation techniques used to measure assets and liabilities. The three levels are as follows:

*Level 1:* Valuation is based on quoted prices (unadjusted) for identical assets or liabilities in active markets;

*Level 2:* Valuation is determined from quoted prices for similar assets and liabilities in active markets, quoted prices for identical or similar instruments in markets that are not active or by model-based techniques in which all significant inputs are observable in the market; and

*Level 3:* Valuation is derived from model-based techniques in which at least one significant input is unobservable and based on the Company's own estimates about the assumptions that market participants would use to value the asset or

liability.

The following is a description of the valuation methods used for instruments measured at fair value as well as the general classification of such instruments pursuant to the applicable valuation method.

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## HAMILTON BANCORP, INC. AND SUBSIDIARY

## Notes to Consolidated Financial Statements (Continued)

*Fair value measurements on a recurring basis*

Securities available for sale – If quoted prices are available in an active market for identical assets, securities are classified within Level 1 of the hierarchy. If quoted market prices are not available, then fair values are estimated using pricing models, quoted prices of securities with similar characteristics or discounted cash flows. As of March 31, 2018 and 2017, the Bank has categorized its investment securities available for sale as follows:

|  | Level<br>1<br>inputs | Level 2<br>inputs | Level 3<br>inputs | Total        |
|--|----------------------|-------------------|-------------------|--------------|
| <b><u>March 31, 2018</u></b>                   |                      |                   |                   |              |
| U.S. government agencies                       | \$ -                 | \$2,718,649       | \$-               | \$2,718,649  |
| Municipal bonds                                | -                    | 11,705,991        | -                 | 11,705,991   |
| Corporate bonds                                | -                    | -                 | 1,954,076         | 1,954,076    |
| Mortgage-backed securities                     | -                    | 59,025,404        | 16                | 59,025,420   |
| Total investment securities available for sale | \$ -                 | \$73,450,044      | \$1,954,092       | \$75,404,136 |

|  | Level<br>1<br>inputs | Level 2<br>inputs | Level 3<br>inputs | Total         |
|--|----------------------|-------------------|-------------------|---------------|
| <b><u>March 31, 2017</u></b>                   |                      |                   |                   |               |
| U.S. government agencies                       | \$ -                 | \$3,512,303       | \$-               | \$3,512,303   |
| Municipal bonds                                | -                    | 14,239,526        | 1,928,313         | 16,167,839    |
| Corporate bonds                                | -                    | 1,916,522         | -                 | 1,916,522     |
| Mortgage-backed securities                     | -                    | 80,829,991        | 2,473             | 80,832,464    |
| Total investment securities available for sale | \$ -                 | \$100,498,342     | \$1,930,786       | \$102,429,128 |

During fiscal 2018, a corporate bond and one mortgage-backed security were moved from a Level 2 input to a Level 3 input. The quantitative unobservable input for these bonds was obtained based upon pricing from an independent third party. The securities were classified as a Level 3 input because there was no active market for these securities to obtain a fair value. Conversely, during fiscal 2018, several municipal bonds and mortgage backed securities were moved from Level 3 input to Level 2 input as additional market data and inputs became available.



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Derivative – Interest rate swap agreements - The fair values of derivatives are based on valuation models using observable market data as of the measurement date (Level 2). The quantitative models that are used utilize multiple market inputs. The inputs will vary based on the type of derivative, but could include interest rates, prices and indices to generate continuous yield or pricing curves, prepayment rates, and volatility factors to value the position. The majority of market inputs are actively quoted and can be validated through external sources, including brokers, market transactions and third-party pricing services. As of March 31, 2018 and 2017, the bank has categorized its interest rate swaps and related loan as follows:

|   | Level<br>1<br>inputs | Level 2<br>inputs | Level<br>3<br>inputs | Total       |
|---|----------------------|-------------------|----------------------|-------------|
| <b><u>March 31, 2018</u></b>                                    |                      |                   |                      |             |
| Loans - Commercial real estate loan                             | \$ -                 | \$3,022,744       | \$ -                 | \$3,022,744 |
| Derivative - Interest rate swap designated as fair value hedge  | -                    | 69,148            | -                    | 69,148      |
| Derivatives - Interest rate swaps designated as cash flow hedge | -                    | 217,464           | -                    | 247,736     |

|   | Level<br>1<br>inputs | Level 2<br>inputs | Level<br>3<br>inputs | Total       |
|---|----------------------|-------------------|----------------------|-------------|
| <b><u>March 31, 2017</u></b>                                    |                      |                   |                      |             |
| Loans - Commercial real estate loan                             | \$ -                 | \$3,201,691       | \$ -                 | \$3,201,691 |
| Derivative - Interest rate swap designated as fair value hedge  | -                    | (26,647 )         | -                    | (26,647 )   |
| Derivatives - Interest rate swaps designated as cash flow hedge | -                    | (83,634 )         | -                    | (83,634 )   |

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## HAMILTON BANCORP, INC. AND SUBSIDIARY

## Notes to Consolidated Financial Statements (Continued)

The following table presents the valuation and unobservable inputs for Level 3 assets measured at fair value on a recurring basis at March 31, 2018:

| Description           | Fair Value  | Valuation Methodology | Unobservable Inputs                           | Range of Inputs |
|-----------------------|-------------|-----------------------|---|-----------------|
| Investment securities | \$1,954,092 | 3rd party valuation   | Discount to reflect current market conditions | 0.00% - 10.00%  |

The following table presents a reconciliation of the investments which are measured at fair value on a recurring basis using significant unobservable inputs (Level 3) for the periods presented:

|                            | March 31,<br>2018 | March 31,<br>2017 |
|----------------------------|-------------------|-------------------|
| Balance, beginning of year | \$1,930,786       | \$1,898,640       |
| Transfers in:              |                   |                   |
| Corporate bonds            | 1,954,076         | -                 |
| Mortgage-backed securities | 16                | 2,473             |
| Municipal bonds            | -                 | 1,928,313         |
| Transfers out:             |                   |                   |
| Corporate bonds            | -                 | 1,898,640         |
| Mortgage-backed securities | 2,473             | -                 |
| Municipal bonds            | 1,928,313         | -                 |
| Balance, end of year       | \$1,954,092       | \$1,930,786       |

*Fair value measurements on a nonrecurring basis*

Impaired Loans - The Bank has measured impairment generally based on the fair value of the loan's collateral. Fair value is generally determined based upon independent appraisals of the properties, or discounted cash flows based upon the expected proceeds. These assets are included as Level 3 fair values. At March 31, 2018 and 2017, the fair values consist of loan balances of \$8,720,339 and \$5,657,048 that have been written down by \$266,256 and \$285,359, respectively, as a result of specific loan loss allowances.

Foreclosed real estate – The Bank's foreclosed real estate is measured at the lower of carrying value or fair value less estimated cost to sell. At March 31, 2018 and 2017, the fair value of foreclosed real estate was estimated to be \$457,778 and \$503,094, respectively. Fair value was determined based on offers and/or appraisals. Cost to sell the assets was based on standard market factors. The Company has categorized its foreclosed assets as Level 3.

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## HAMILTON BANCORP, INC. AND SUBSIDIARY

## Notes to Consolidated Financial Statements (Continued)

Premises and equipment held for sale – The Bank’s premises and equipment held for sale is measured at the fair value less estimated cost to sell. The assets in fiscal 2017 totaling \$547,884 were acquired in the acquisition of Fraternity and sold during the quarter ending December 31, 2017. Fair value was determined based upon appraisals and the cost to sell these assets was determined using standard market factors. The Company has categorized its premises and equipment held for sale as Level 3.

|                                      | Level<br>1<br>inputs | Level<br>2<br>inputs | Level 3<br>inputs | Total       |
|--------------------------------------|----------------------|----------------------|-------------------|-------------|
| <b><u>March 31, 2018</u></b>         |                      |                      |                   |             |
| Impaired loans                       | \$ -                 | \$ -                 | \$8,454,083       | \$8,454,083 |
| Foreclosed real estate               | -                    | -                    | 457,778           | 457,778     |
| Premises and equipment held for sale | -                    | -                    | -                 | -           |
| Loans held for sale                  | -                    | -                    | -                 | -           |

|                                      | Level<br>1<br>inputs | Level<br>2<br>inputs | Level 3<br>inputs | Total       |
|--------------------------------------|----------------------|----------------------|-------------------|-------------|
| <b><u>March 31, 2017</u></b>         |                      |                      |                   |             |
| Impaired loans                       | \$ -                 | \$ -                 | \$5,371,689       | \$5,371,689 |
| Foreclosed real estate               | -                    | -                    | 503,094           | 503,094     |
| Premises and equipment held for sale | -                    | -                    | 547,884           | 547,884     |
| Loans held for sale                  | -                    | -                    | -                 | -           |

The following table presents the valuation and unobservable inputs for Level 3 assets measured at fair value on a nonrecurring basis at March 31, 2018:

| Description                      | Fair Value  | Valuation<br>Methodology | Unobservable<br>Inputs                        | Range of<br>Inputs |
|----------------------------------|-------------|--------------------------|---|--------------------|
| Impaired loans, net of allowance | \$8,454,083 | Appraised value          | Discount to reflect current market conditions | 0.00% - 25.00%     |

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|                        |           |                       |   |                |
|------------------------|-----------|-----------------------|---|----------------|
|                        |           | Discounted cash flows | Discount rates                                | 2.63% - 7.25%  |
| Foreclosed real estate | \$457,778 | Appraised value       | Discount to reflect current market conditions | 0.00% - 25.00% |

The following table summarizes changes in foreclosed real estate for the years ended March 31, 2018 and 2017, which is measured on a nonrecurring basis using significant unobservable, level 3, inputs:

|  | Year Ended March 31, |           |
|--|----------------------|-----------|
|  | 2018                 | 2017      |
| Balance at beginning of period               | \$503,094            | \$443,015 |
| Transfer to foreclosed real estate           | 23,834               | 126,575   |
| Write-down of foreclosed real estate         | (31,955 )            | 0         |
| Proceeds from sale of foreclosed real estate | (35,896 )            | (60,258 ) |
| Loss on sale of foreclosed real estate       | (1,299 )             | (6,238 )  |
| Balance at end of period                     | \$457,778            | \$503,094 |

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## HAMILTON BANCORP, INC. AND SUBSIDIARY

## Notes to Consolidated Financial Statements (Continued)

The remaining financial assets and liabilities are not reported on the balance sheets at fair value on a recurring basis. The calculation of estimated fair values is based on market conditions at a specific point in time and may not reflect current or future fair values.

|   | <b>March 31, 2018</b> |                     | March 31, 2017  |              |
|---|-----------------------|---------------------|-----------------|--------------|
|   | Carrying amount       | Fair value          | Carrying amount | Fair value   |
| <u>Financial assets</u>                               |                       |                     |                 |              |
| Level 1 inputs  |                       |                     |                 |              |
| Cash and cash equivalents                             | <b>\$23,368,415</b>   | <b>\$23,368,415</b> | \$29,353,921    | \$29,353,921 |
| Level 2 inputs  |                       |                     |                 |              |
| Federal Home Loan Bank stock                          | <b>3,122,400</b>      | <b>3,122,400</b>    | 2,020,200       | 2,020,200    |
| Bank-owned life insurance                             | <b>17,455,850</b>     | <b>17,455,850</b>   | 18,253,348      | 18,253,348   |
| Level 3 inputs  |                       |                     |                 |              |
| Certificates of deposit held as investment            | <b>499,189</b>        | <b>492,751</b>      | 499,280         | 505,641      |
| Loans receivable, net of unearned income              | <b>387,328,993</b>    | <b>385,818,260</b>  | 335,758,154     | 337,444,534  |
| <u>Financial liabilities</u>                          |                       |                     |                 |              |
| Level 3 inputs  |                       |                     |                 |              |
| Deposits  | <b>405,142,975</b>    | <b>405,026,957</b>  | 412,855,774     | 413,148,503  |
| Advance payments by borrowers for taxes and insurance | <b>1,962,665</b>      | <b>1,962,665</b>    | 1,868,110       | 1,868,110    |
| Borrowings  | <b>60,672,140</b>     | <b>60,494,922</b>   | 36,124,899      | 36,697,631   |

The fair values of cash and cash equivalents and advances by borrowers for taxes and insurance are estimated to equal the carrying amount.

The fair values of Federal Home Loan Bank stock and bank-owned life insurance are estimated to equal carrying amounts, which are based on repurchase prices of the FHLB stock and the insurance company.

The fair value of fixed-rate loans is estimated to be the present value of scheduled payments discounted using interest rates currently in effect. The fair value of variable-rate loans, including loans with a demand feature, is estimated to equal the carrying amount. The valuation of loans is adjusted for estimated loan losses.

The fair value of certificates of deposit held as investments is estimated based on interest rates currently offered for certificates of deposit with similar remaining maturities.

The fair value of interest-bearing checking, savings, and money market deposit accounts is equal to the carrying amount. The fair value of fixed-maturity time deposits is estimated based on interest rates currently offered for deposits of similar remaining maturities.

The fair value of borrowings is estimated based on interest rates currently offered for borrowings of similar remaining maturities.

The fair value of outstanding loan commitments and unused lines of credit are considered to be the same as the contractual amounts, and are not included in the table above. These commitments generate fees that approximate those currently charged to originate similar commitments.

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## HAMILTON BANCORP, INC. AND SUBSIDIARY

## Notes to Consolidated Financial Statements (Continued)

**Note 20: Condensed Financial Statements of Parent Company**

Presented below are the condensed statements of financial condition as of March 31, 2018 and 2017, and the related condensed statements of operations and condensed statements of cash flows for Hamilton Bancorp, Inc. for the years ended March 31, 2018 and 2017.

**Condensed  
Statements  
of  
Financial  
Condition**

|  | <b>March 31,<br/>2018</b> | March 31,<br>2017 |
|--|---------------------------|-------------------|
| <b>Assets</b>                              |                           |                   |
| Cash and due from bank                     | <b>\$3,421,827</b>        | \$3,250,700       |
| Investment securities available-for-sale   | <b>1,995,625</b>          | 2,016,730         |
| Loans and leases, net of unearned income   | <b>433,222</b>            | 479,473           |
| ESOP loan receivable                       | <b>2,214,298</b>          | 2,332,992         |
| Investment in bank subsidiary              | <b>45,903,508</b>         | 51,487,261        |
| Other assets                               | <b>107,652</b>            | 224,074           |
| Total Assets                               | <b>\$54,076,132</b>       | \$59,791,230      |
| <b>Liabilities</b>                         |                           |                   |
|  | <b>\$-</b>                | \$-               |
| <b>Shareholders' Equity</b>                |                           |                   |
| Common stock                               | <b>34,076</b>             | 34,111            |
| Additional paid in capital                 | <b>32,113,534</b>         | 31,656,235        |
| Retained earnings                          | <b>25,920,490</b>         | 31,730,673        |
| Unearned ESOP shares                       | <b>(2,073,680 )</b>       | (2,221,800 )      |
| Accumulated other comprehensive loss       | <b>(1,918,288 )</b>       | (1,407,989 )      |
| Total Shareholders' Equity                 | <b>54,076,132</b>         | 59,791,230        |
| Total Liabilities and Shareholders' Equity | <b>\$54,076,132</b>       | \$59,791,230      |



**Condensed  
Statements  
of  
Operations  
Years  
Ended  
March 31,  
2018 and  
2017**

|  | <b>March 31,<br/>2018</b> | March 31,<br>2017 |
|--|---------------------------|-------------------|
| <b>Interest revenue</b>  |                           |                   |
| Interest on loans, including fees  | <b>\$21,213</b>           | \$30,464          |
| Interest on bank deposits  | <b>3,059</b>              | 5,307             |
| Interest on investments  | <b>21,967</b>             | 18,932            |
| Interest on ESOP loan  | <b>90,526</b>             | 87,710            |
| Total interest revenue   | <b>136,765</b>            | 142,413           |
| <b>Noninterest expenses</b>  |                           |                   |
| Legal  | <b>45,466</b>             | 25,232            |
| Other professional services  | -                         | 587               |
| Merger related expenses  | -                         | 219,417           |
| Other operating  | <b>159,870</b>            | 171,516           |
| Total noninterest expenses   | <b>205,336</b>            | 416,752           |
| Loss before income tax benefit and equity in net loss of bank subsidiary | <b>(68,571 )</b>          | (274,339)         |
| Income tax expense (benefit)   | <b>58,014</b>             | (16,013 )         |
| Loss before equity in net loss of bank subsidiary                        | <b>(126,585 )</b>         | (258,326)         |
| <b>Equity in net loss of bank subsidiary</b>                             | <b>(5,922,357)</b>        | (670,456)         |
| <b>Net loss</b>  | <b>\$(6,048,942)</b>      | \$(928,782)       |

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## HAMILTON BANCORP, INC. AND SUBSIDIARY

## Notes to Consolidated Financial Statements (Continued)

**Condensed Statements of Cash Flows  
Years Ended March 31, 2018 and 2017**

|  | <b>March 31,<br/>2018</b> | March 31,<br>2017 |
|--|---------------------------|-------------------|
| <b>Cash flows from operating activities:</b>   |                           |                   |
| Net loss   | <b>\$(6,048,942)</b>      | \$(928,782 )      |
| Adjustments to reconcile net loss to net cash provided (used) by operating activities:         |                           |                   |
| Equity in undistributed net loss of subsidiary   | <b>5,922,357</b>          | 670,456           |
| Amortization of premium on investment securities   | <b>13,034</b>             | 4,707             |
| Increase (decrease) in other assets  | <b>119,768</b>            | (9,593 )          |
| Decrease in other liabilities  | -                         | (23,976 )         |
| Net cash provided (used) by operating activities   | <b>6,217</b>              | (287,188 )        |
| <b>Cash flows from investing activities:</b>   |                           |                   |
| Acquisition, net of cash acquired  | -                         | (22,430,749)      |
| Principal collected on ESOP loan   | <b>118,694</b>            | 116,819           |
| Principal repayments on loans  | <b>46,251</b>             | 153,313           |
| Proceeds from maturing and called securities available for sale, including principal pay downs | -                         | 1,000,000         |
| Purchase of investment securities available-for-sale   | -                         | (2,026,900 )      |
| Net cash provided (used) by investing activities   | <b>164,945</b>            | (23,187,517)      |
| <b>Cash flows from financing activities:</b>   |                           |                   |
| Dividend from Bank subsidiary  | -                         | 24,000,000        |
| Dividend to Bank subsidiary  | -                         | (3,000,000 )      |
| Issuance of restricted stock   | -                         | 20                |
| Redemption of restricted stock   | <b>(35 )</b>              | (45 )             |
| Net cash (used) provided by financing activities   | <b>(35 )</b>              | 20,999,975        |
| <b>Net increase (decrease) in cash and cash equivalents</b>                                    | <b>171,127</b>            | (2,474,730 )      |
| Cash and cash equivalents at beginning of period   | <b>3,250,700</b>          | 5,725,430         |
| <b>Cash and cash equivalents at end of period</b>  | <b>\$3,421,827</b>        | \$3,250,700       |

