



**Shore
Bancshares** 
COMMUNITY of COMPANIES

ANNUAL REPORT
2017

SELECTED FINANCIAL DATA

(Dollars in thousands, except per share data.)

Years Ended December 31

RESULTS OF OPERATIONS:

	2017	2016	2015
Interest income	\$ 47,801	\$ 40,652	\$ 38,871
Interest expense	<u>2,273</u>	<u>2,403</u>	<u>3,346</u>
Net interest income	45,528	38,249	35,525
Provision for credit losses	<u>2,291</u>	<u>1,848</u>	<u>2,075</u>
Net interest income after provision for credit losses	43,237	36,401	33,450
Noninterest income	17,750	16,645	15,416
Noninterest expense	<u>41,202</u>	<u>37,147</u>	<u>37,350</u>
Income (loss) before income taxes	19,785	15,899	11,516
Income tax expense (benefit)	<u>8,523</u>	<u>6,261</u>	<u>4,408</u>
Net income (loss)	<u>\$ 11,262</u>	<u>\$ 9,638</u>	<u>\$ 7,108</u>

PER COMMON SHARE DATA:

Net income (loss) - basic	\$ 0.89	\$ 0.76	\$ 0.56
Net income (loss) - diluted	0.89	0.76	0.56
Dividends paid	0.22	0.14	0.04
Book value (at year end)	12.91	12.18	11.64
Tangible book value (at year end) ¹	10.31	11.16	10.59

FINANCIAL CONDITION (at year end):

Loans	\$ 1,093,514	\$ 871,525	\$ 795,114
Assets	1,393,860	1,160,271	1,135,143
Deposits	1,202,781	997,489	975,464
Stockholders' equity	163,736	154,299	146,967

PERFORMANCE RATIOS (for the year):

Return on average total assets	0.87%	0.84%	0.64%
Return on average stockholders' equity	7.05	6.32	4.93
Net interest margin	3.76	3.56	3.43
Efficiency ratio ²	65.11	67.67	73.32
Dividend payout ratio	24.72	18.42	7.14
Average stockholders' equity to average total assets	12.40	13.36	13.04

ASSET QUALITY RATIOS (for the year):

Nonperforming assets to total assets	0.53%	0.99%	1.44%
Nonperforming assets and accruing TDRs to total assets	1.49	2.11	2.81
Allowance for credit losses to loans	0.89	1.00	1.05
Allowance for credit losses to nonaccrual loans	196.76	97.26	68.77
Allowance for credit losses to nonaccrual loans and TDRs	53.46	39.71	30.14

¹Total Stockholders' equity, net of goodwill and other intangible assets, divided by the number of shares of common stock outstanding at year end.

²Noninterest expense as a percentage of total revenue (net interest income plus total noninterest income). Lower ratios indicate improved productivity.

Dear Shareholders:

2017 was a stellar year for Shore Bancshares in terms of growth and core earnings. Our market area expanded west with the successful acquisition of three branches in the Greater Baltimore Metropolitan area from Northwest Bank and south with two new office locations. In addition, the Bank experienced an increase in organic loan growth that outpaced the industry.



First a note about the branch acquisition, the expansion into the Greater Baltimore Metro area provides geographic diversification for our organization and supports future growth. The transaction resulted in Shore United Bank receiving \$212.5 million in assets from Northwest Bank, the bank subsidiary of Northwest Bancshares, Inc. Employees of both organizations worked tirelessly to ensure the former Northwest Bank customers had minimal impact through the transition.

It's important to note that in addition to expanding our market area west into Baltimore, the Company also expanded south into Ocean City, Maryland and Onley, Virginia. The new loan production office in Ocean City was a directional move to expand our footprint to the lower eastern shore of Maryland. The new full-service branch in Onley, Virginia further supports our strategic point south to offer our community banking model to businesses and consumers in these market areas.

We believe that the companies of tomorrow will be those that are able to look forward and embrace change. The Company is committed to investing in new technology, its employees, and processes so that our customers will have the same positive experiences when they visit a traditional branch or use one of our convenient services online. We look forward to introducing a new online loan application giving customers the option to apply for a loan online while keeping our lending decisions local with our experienced team of lending professionals.

Whether we introduce a new technology or execute an acquisition, planning is key to handle expansion and prepare for the future. In June, our insurance division, Avon-Dixon Agency relocated to a new modern building in Easton, Maryland. In conjunction with the move, our entire insurance division went through a re-brand adopting the corporate logo and brand standards launched in 2016 when our two banks merged to form Shore United Bank. By adding one common brand to all of our companies our clients and communities can further see the depth and breadth of the services we offer.

Turning to the Company's financial performance, we're pleased with the continued momentum in 2017. Absent the branch acquisition, total loans increased \$114 million or 13% and total deposits increased \$18 million or 1.8%. Stockholders' equity increased \$9.5 million or 6% over the previous year.

Overall the Company ended 2017 with positive results with increases to our net interest income, positive loan growth, and improvements to our net interest margin. Our financial success is attributable to the 352 employees throughout our community of companies who are committed to living the vision and values we represent. We are also fortunate to have a board of directors who are reliable and committed to our vision of the future. We share their commitment to delivering outstanding results to our clients, employees, communities, and shareholders. Thank you for your continued support and investment in Shore Bancshares.

Lloyd L. "Scott" Beatty, Jr.

Frank E. Mason, III

CLIENTS

Client's now have access to over 55,000 surcharge-free ATMs worldwide through the Allpoint Network. As our footprint expands so does the need for our clients to have access to their money anytime from anywhere. In May, Shore United Bank became a member of the Allpoint Network giving clients access to a surcharge-free network of ATMs with over 55,000 locations throughout the United States, Canada, Mexico, Puerto Rico, United Kingdom and Australia.

Allpoint Network ATMs are located in retail locations around the world, with 43,000 in the United States, which includes these retailers: Target, CVS Pharmacy, Walgreens, Costco, Safeway, Sunoco, Kangaroo Express, Speedway and Winn Dixie. The Allpoint Network allows our clients to enjoy surcharge-free ATMs where our traditional branches are not available. This service helps to increase the value of our client relationships and loyalty to our customers.

Client experience rated Best of by What's Up Eastern Shore Magazine in 2017. Shore United Bank, Wye Financial & Trust and Avon-Dixon were voted as the 2017 "Best of Eastern Shore" winners of the What's Up Eastern Shore Magazine's reader's poll. The awards were announced to the public on June 1, 2017. The winning categories were: Best Bank- Shore United Bank, Best Financial Advisor/Firm- Wye Financial & Trust, Best Life & Auto Insurance Advisor/Firm - Avon-Dixon Insurance Agency.

The recognition of this local honor speaks volumes about our employees and their commitment to our clients and the communities in which we serve.

Enhancements to consumer and business checking products to meet the needs of our clients. With a strategic goal to grow core deposits, we completed a thorough review of our bank products and services to understand how our clients use their accounts and how we measure up against our competitors. The review resulted in positive enhancements to our checking products and services putting us ahead of most competitors in the markets we serve. As a result, in January of 2018, we announced a new consumer E-Checking product with no minimum balance, no monthly service fee and access to over 55,000 surcharge-free ATMs worldwide through the Allpoint Network. Additional product enhancements include reductions to the transaction limits of our business checking accounts and more. With the introduction of a new consumer checking product, enhancements to existing products and services and the combination of an experienced team of leaders, our direction is on course for another successful year.

EMPLOYEES

Providing training and development opportunities to employees helps them succeed. This past year was not unlike any other year in that we continue to dedicate internal training resources for employees to enhance their working knowledge and job skills. We also invest in outside development programs like those offered by the Maryland Bankers Association.

Two programs offered by Maryland Bankers Association that we actively participate in are the Maryland Banking School and the Emerging Leaders Program. Both programs help leaders prepare for the changes ahead in the financial industry. Over the years, 28 employees graduated from the Maryland Banking School. Our most recent graduates are Chad Cronshaw and Ron Cannon, Branch Managers at Shore United Bank.

To help prepare our next generation of leaders for the financial industry changes ahead, we've selected three employees to participate in MBA's new Emerging Leaders Program: Philip "Phil" O'Neil, Financial Reporting Officer and Danielle Griffith, Enterprise Risk & Special Projects Officer both at Shore Bancshares and Matthew Marino, Branch Manager at Shore United Bank. The Emerging Leaders Program proactively supports a diverse group of leaders who will be able to make better decisions through engagement and understanding of the Maryland banking industry and those it serves.

Measuring employee satisfaction is important to us, the results are instrumental in guiding the future of our organization. In December of 2017, we launched our second employee satisfaction survey. The survey was conducted by a third-party vendor with all responses kept entirely confidential. The intention of the survey is to identify trends where we can drive improvement. The results from the survey conducted in 2014 were invaluable in helping us build a strong team that was connected to the organizations vision and mission. We look forward to the 2017 survey results as shared by our employees to help us make positive, measurable changes for the future success of our companies.

COMMUNITY

Giving back to the communities in which we serve is not something new at Shore Bancshares. Last year, we united with local community leaders to help students and parents with the fight against substance abuse through the Talbot Goes Purple and the THP Project Purple program. Opioid addiction is the fastest growing epidemic in our communities to date and overdoses are the number one cause of death in people under 50. These hard-hitting statistics are reasons why the organization came together to support both programs in the communities we serve.

Employees at Avon-Dixon Insurance Agency, Shore United Bank and Wye Financial & Trust, showed their support for the programs by participating in employee education sessions and taking part in 'purple Fridays' throughout the month of September. Each location brought awareness to the initiative by decorating their office in purple and offering information about the severity of this substance abuse to their customers.

Our employees remain connected to our communities by voluntarily donating their time and talents to over one hundred organizations in multiple states and counties. As a community-based organization, volunteering is another way that makes us different from large corporations. By staying connected, we build lasting relationships and stay engaged with other community leaders working towards a common goal. Our service to our communities benefited groups in many categories including community development, youth and education, environment, and agriculture as well as health and human services.

SHAREHOLDERS

Growth through acquisition reflects our intention to expand into new market areas. The acquisition of three former Northwest Bank branches on May 22, 2017 expanded Shore United Bank's footprint in Maryland. Our branch network now extends across the Bay Bridge to the Greater Baltimore Metropolitan communities of Elkridge, Owings Mills, and Arbutus. The transaction reflects our announced intention to expand our footprint through accretive acquisition opportunities. The acquisition provides us with the liquidity to support future growth as well as strengthen our franchise value and provide geographical diversification to our organization.

Our expansion did not stop in Baltimore. In April, Shore United Bank opened a new Loan Production Office in West Ocean City, Maryland. And, with a new full-service branch in Onley, Virginia that opened in November our market encompasses the entire Delmarva Peninsula.

Successful companies utilize strategic planning to prepare for expansion. Our insurance division, Avon-Dixon Agency, now has its entire team under one roof. In June, the Avon-Dixon Agency made their move to a new building in Easton, Maryland to accommodate their growth and efficiency needs. The new location provides a professional appearance, ample parking, and conference room space for employees and clients.

In connection with the move, the corporate logo and brand standards were adopted throughout the insurance division to further unite our companies with one common brand.

Having the right leaders is important for the future growth and success of our organization. Last year we announced three new market leaders at Shore United Bank. W. Thomas "Tom" Mears, is responsible for business development in the Lower Eastern Shore which includes Worcester, Wicomico, Somerset counties of Maryland and Accomack county of Virginia; William "Bill" Hudson leads the Greater Baltimore Metropolitan market that includes Baltimore and Howard counties; and Heather Bacher who is responsible for leading our Maryland north region of Queen Anne's and Kent counties.

At Wye Financial & Trust we added three new advisors to our team; Colin Pryor, Christopher Parks, and Neil Zurowski who have combined experiences in wealth management, trust administration, retirement planning, investment and annuity strategies and portfolio management. By adding experienced professionals to our team, we expand our client services to the lower eastern shore of Maryland and Virginia, the Greater Baltimore Metropolitan area, and Delaware to help preserve and grow wealth for our clients.

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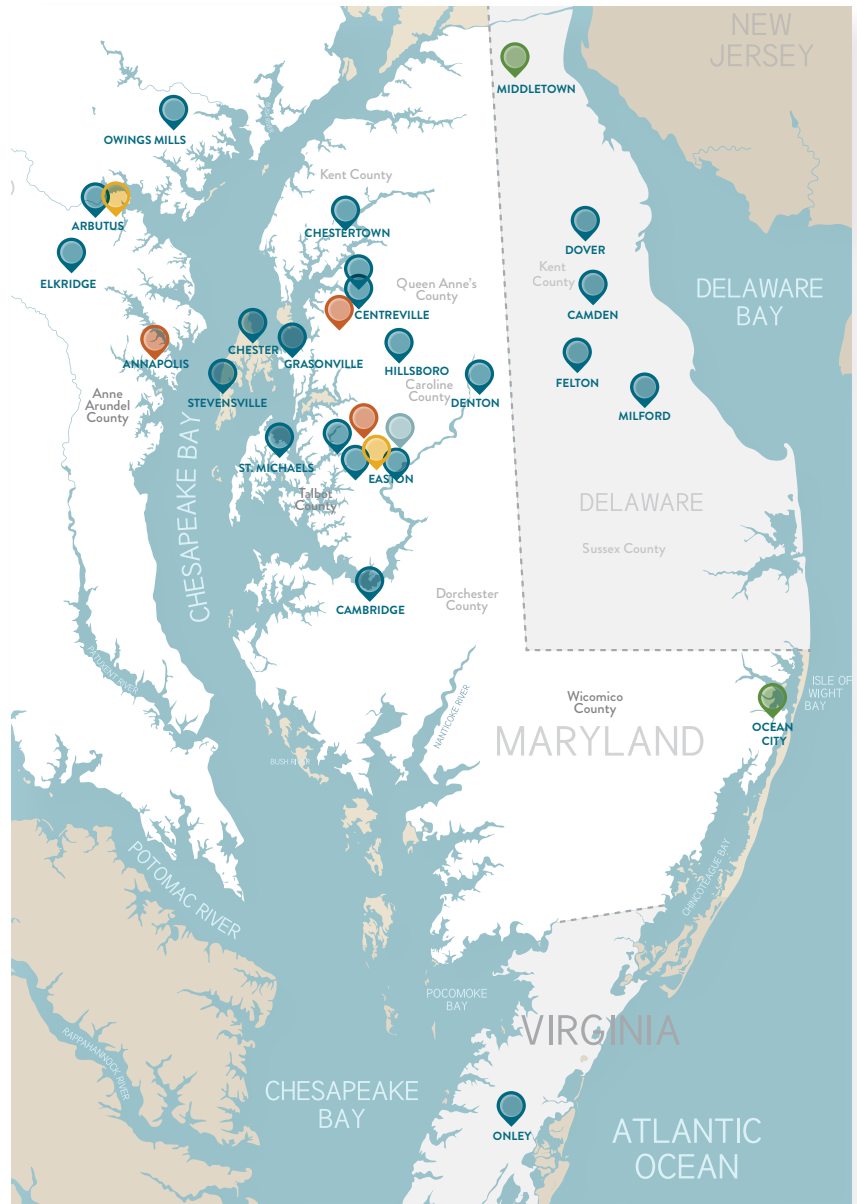
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