2020 ANNUAL REPORT

Peoples Financial
SERVICES CORP.

THOMAS P. TULANEY APPOINTED PRESIDENT

On Friday, May 29, 2020, the Board of Directors appointed Thomas P. Tulaney as President and Chief Operating Officer of Peoples Security Bank and Trust Company and Peoples Financial Services Corp. Mr. Tulaney was also appointed to the bank's Board of Directors.

Mr. Tulaney joined Peoples Security Bank and Trust Company in April 2011 as Executive Vice President, Chief Lending Officer. Mr. Tulaney most recently served as Peoples Security Bank and Trust's Senior Executive Vice President and Chief Operating Officer (COO). As the bank's President and COO, he is responsible for the daily operations of the bank. With over 39 years of banking experience, Mr. Tulaney is well positioned to ensure our bank exceeds the expectations of our shareholders, employees, customers and our local communities. Mr. Tulaney's community involvement includes serving on the boards of Lackawanna College, Scranton Counseling Center and The Community Support Group, as well as currently serving as Trustee of the Peoples Security Charitable Foundation and the Roy W. Piper Charitable Trust.

Peoples Security
Bank & Trust Est. 1905


Craig W. Best
Chief Executive Officer
Thomas P. Tulaney
President | COO
William E. Aubrey II
Chairman of the Board

DEAR SHAREHOLDERS,

I feel it is safe to say that 2020 was a year like none of us have ever experienced. Our company, our communities, our nation and the world was put to the test dealing with the COVID-19 global pandemic. Little did we know last year at this time how this virus would impact our lives. Over the last 12 months, the majority of our country has been on lockdown as the virus has reportedly infected 29.3 million Americans and was the cause of over five hundred thirty thousand (530,000) deaths in the United States alone.

This time last year we were just learning of the seriousness of COVID-19. China reported the first cases of COVID-19 to the World Health Organization (WHO) on December 31, 2019. On January 11, 2020, China reported the first COVID-19 related death and on January 20th the United States reported its first case of COVID-19. By January 30th, the WHO declared a public health emergency.

In January 2020, management at Peoples Security Bank began discussing the potential impact of COVID-19 on our operations, employees, customers and communities. On January 30th, we made the decision to perform our pandemic tabletop exercise in February, instead of November when it is usually performed.

By February 12th our simulation converted to real life as we initiated our pandemic business continuity plan and immediately had 45 key employees working remotely. On February 29th, the first COVID-19 related death was reported in the United States, and on March 11th the United States declared a National Emergency. On March 26th, the United States weekly unemployment claims reached a record 3.3 million as many non-essential business, schools, universities and government offices shut down in efforts to slow the spread of the virus.

At year-end, Peoples Security Bank had 46% of our 386 employees having the capability to work remotely from home. As an essential business, we always kept our offices open; but in an effort to prioritize our employees' and customers' safety, we operated with limited staff. Business was conducted through our drive up windows with our lobbies accessible only by appointment. While most of our employees worked from home, we had many of our employees stay home even though their jobs could not be performed remotely. All employees continued to be paid their full salaries and benefits.

As our communities stayed locked down, Peoples Security Bank remained dedicated to serving our customers and local businesses. Peoples Security Bank participated in the Paycheck Protection Program (PPP) designed to assist businesses in keeping their employees working. Peoples Security Bank granted a total of 1,452 PPP loans aggregating over $217 million in assistance. Peoples Security Bank also granted loan deferments on 986 loans with outstanding balances of $330.1 million to customers in an effort to assist them during the economic hardships brought on by the pandemic.

Peoples Security Bank was also instrumental in supporting our communities during the pandemic. The shutdown put tremendous pressure on many non-profit and charitable organizations that support our community. During this time of increased need, Peoples Security Bank was proud to donate over $40,000 to area food banks and healthcare organizations.

All of our employees, especially those on the front line in our community offices, have done a tremendous job in continuing to serve the needs of our customers.

2020 FINANCIAL PERFORMANCE

Even with the difficult operating environment created by the pandemic, Peoples Security Bank was able to post record earnings for the third consecutive year. Earnings for the year totaled $29.4 million or $4.00 per diluted share. This represents a 14.1% increase in earnings and a 15.3% increase in earnings per share as compared to fiscal year end 2019. This increase was primarily driven by a $399 million or 17.5% increase in earning assets, which in turn created an increase in net interest income of $4.3 million. Asset growth was comprised of a $189 million increase in Paycheck Protection Loans, a $50 million increase in conventional loans and a $183 million increase in federal funds sold. Asset growth was funded with a $465 million increase (23.6%) in deposits.

Non-interest income increased by 10.1% and was fueled by strong mortgage banking performance and net gains on investment securities sales. Non-interest expense decreased $0.8 million compared to 2019 due to a decrease in salaries and benefit expense of $1.2 million.

Asset quality metrics also improved in 2020. Net charge-offs as a percentage of loans decrease to 0.13% in 2020 vs 0.26% in 2019 and non-performing assets to total assets decreased from 0.43% in 2019 to 0.36% in 2020. Despite these improvements, we increased our reserve for loan losses from 1.17% of total loans to 1.26% of total loans due to the negative impact the pandemic had on unemployment and our economy.

MARKET EXPANSION

The pandemic also slowed our progress on our market expansion initiatives. We did manage to open our new office in Doylestown, PA in March of 2020. The lenders we recruited at the end of 2019 and a retail banker are now housed in that office. Additional branch staffing will be added in the second quarter of 2021. We were also able to complete the renovations of our Nicholson Office as well as our Hop Bottom Office, bringing back the historical aspects of an office that was opened in 1910.

NEW PRESIDENT OF PEOPLES

In May of 2020, the board of directors of Peoples Financial Services Corp. appointed Thomas P. Tulaney as the 10th president of the bank and the holding company. Craig W. Best remains CEO of both companies. Tom has been with our company since our merger with Penseco in November 2013 and has served in the roles of Senior Executive Vice President and Chief Operating Officer from May 2017 until May 2020. In December 2018, he assumed oversight of the bank's Wealth Management Division. Prior to May 2017, and since our merger with Penseco in November 2013, he served as our Executive Vice President and Chief Lending Officer, the same position he held with Penseco from March 2012. He joined Penn Security Bank and Trust Company in April 2011 as Executive Vice President and Deputy Chief Lending Officer. Mr. Tulaney has over 35 years of banking experience and held various senior level executive positions with several financial institutions before joining Penseco Financial Services Corporation.

BOARD MEMBER RETIREMENT

At our annual meeting of shareholders this May, Mr. Steven Weinberger will be retiring from our board of directors as he has reached our mandatory age for retirement. Steven has been a director of Penseco Financial Services Corporation from 1999 to December 2013, when he was appointed to the Peoples Financial Services Corp. board by way of our acquisition of Penseco. We will miss Steven's valuable guidance and wish him well.

In closing, we would like to express our appreciation to all our employees who, in an unprecedented difficult environment, continued to provide our customers with the quality service Peoples Security Bank has become known for delivering. We also want to thank our shareholders for their continued support.

Sincerely yours,

Wm. E. Aubrey II

William E. Aubrey II
Chairman of the Board

Craig Best

Craig W. Best
Chief Executive Officer

Thomas P. Tulaney

Thomas P. Tulaney
President & COO

JOIN US ▪ VIRTUAL ANNUAL MEETING
Saturday, May 15, 2021 at 9:00am
www.virtualshareholdermeeting.com/PFIS2021

FINANCIAL HIGHLIGHTS

PEOPLES FINANCIAL SERVICES CORP.
CONSOLIDATED SELECTED FINANCIAL DATA
(Dollars in thousands, except per share data)

Year Ended December 31	2020	2019	2018	2017	2016
Condensed statements of financial performance:					
Interest income	$94,125	$93,381	$84,661	$74,242	$68,984
Interest expense	14,324	17,868	13,322	8,698	7,251
Net interest income	79,801	75,513	71,339	65,544	61,733
Provision for loan losses	7,400	6,100	4,200	4,800	5,000
Net interest income after the provision for loan losses	72,401	69,413	67,139	60,744	56,733
Noninterest income	16,642	15,120	13,659	17,186	15,888
Noninterest expense	54,868	55,642	52,487	51,293	48,030
Income before income taxes	34,175	28,891	28,311	26,637	24,591
Provision for income tax expense	4,821	3,155	3,391	8,180	5,008
Net income	$29,354	$25,736	$24,920	$18,457	$19,583
Condensed statements of financial position:					
Investments securities	$303,274	$338,557	$278,334	$281,822	$269,927
Net loans	2,150,638	1,915,563	1,801,887	1,674,105	1,517,004
Other assets	429,890	221,207	208,772	213,104	212,511
Total Assets	$2,883,802	$2,475,327	$2,288,993	$2,169,031	$1,999,442
Deposits	$2,437,113	$1,971,489	$1,875,022	$1,719,018	$1,588,757
Short-term borrowings	50,000	152,150	86,500	123,675	82,700
Long-term debt	14,769	32,733	37,906	49,734	58,134
Subordinated debt	33,000				
Other liabilities	32,043	19,945	10,951	11,628	13,233
Stockholders' equity	316,877	299,010	278,614	264,976	256,618
Total liabilities and stockholders' equity	$2,883,802	$2,475,327	$2,288,993	$2,169,031	$1,999,442
Per share data:					
Net income - basic	$4.02	$3.48	$3.37	$2.50	$2.65
Net income - diluted	4.00	3.47	3.37	2.50	2.65
Cash dividends declared	1.44	1.37	1.31	1.26	1.24
Stockholders' equity	$43.92	$40.47	$37.66	$35.82	$34.71
Cash dividends as a percentage of net income	35.83%	39.37%	38.90%	50.49%	46.83%
Average common shares outstanding - basic	7,304,956	7,395,429	7,397,797	7,395,837	7,396,716
Average common shares outstanding - diluted	7,337,843	7,412,369	7,402,900	7,395,837	7,396,716
Selected ratios (based on average balances):					
Net income as a percentage of total assets	1.09%	1.10%	1.12%	0.90%	1.02%
Net income as a percentage of stockholders' equity	9.48	8.87	9.21	7.02	7.64
Stockholders' equity as a percentage of total assets	11.48	12.37	12.14	12.77	13.36
Tier I capital as a percentage of adjusted total assets	9.28	10.14	10.03	9.94	10.16
Net interest income as a percentage of earning assets	3.25	3.58	3.59	3.69	3.77
Loans, net, as a percentage of deposits	95.70%	96.83%	99.55%	96.50%	95.81%
Selected ratios (based on period end balances):					
Tier I capital as a percentage of risk-weighted assets	12.16%	11.90%	11.95%	11.85%	12.49%
Total capital as a percentage of risk-weighted assets	15.10	13.04	13.10	12.95	13.51
Allowance for loan losses as a percentage of loans, net	1.26	1.17	1.17	1.12	1.04
Nonperforming loans as a percentage of loans, net	0.45%	0.52%	0.53%	0.67%	0.90%

NOTE: *Average balances were calculated using average daily balances. Average balances for loans include nonaccrual loans. Tax-equivalent adjustments were calculated using the prevailing statutory tax rate of 21.0 percent for 2020, 2019 and 2018, and 35.0 percent for the years 2017 and 2016.*

LEADERSHIP

BOARD OF DIRECTORS

William E. Aubrey II
Chairman of the Board
Peoples Financial Services Corp.
Peoples Security Bank & Trust

President of Alternative Investments
Gertrude Hawk Holdings

Craig W. Best
Chief Executive Officer
Peoples Financial Services Corp.
Peoples Security Bank & Trust

Sandra L. Bodnyk
Retired Banking Executive

Ronald G. Kukuchka
President
Ace Robbins, Inc.

Richard S. Lochen, Jr.
Certified Public Accountant
Partner | Lochen & Chase PC

James B. Nicholas
President
D.G. Nicholas Co.

Steven L. Weinberger
President
G. Weinberger Company

Joseph T. Wright, Jr., Esq
Attorney at Law | Partner
Wright & Reihner PC

MANAGEMENT TEAM

Craig W. Best
Chief Executive Officer

Thomas P. Tulaney
President
Chief Operating Officer

Neal D. Koplin
Senior Executive Vice President
Chief Banking Officer

John R. Anderson III
Executive Vice President
Chief Financial Officer

Timothy H. Kirtley
Executive Vice President
Chief Risk Officer
Corporate Secretary

Susan L. Hubble
Executive Vice President
Chief Information Officer

Joseph M. Ferretti
Northeast Market President

Jeffrey A. Drobins
Lehigh Valley Market President

Ian Matlack
Greater Delaware Valley Market President

Lynn M. Peters Thiel
Executive Vice President
Chief Retail Officer

Thomas C. Cassidy
Senior Vice President
Chief Investment Officer
Wealth Management Division

Linda A. Gardner
Senior Vice President
Human Resources Manager

NICHOLSON & HOP BOTTOM NEWLY RENOVATED OFFICE SPACE

On August 1, 2020, our newly renovated Nicholson office located at 42-48 State Street opened for business. These renovations have greatly improved our visibility and presence, allowing us to better serve our customers as well as provide an aesthetic addition to our local community.

The new branch is spacious with 3,000 square feet of upgraded features including a fully-automatic handicap entry for easy access and an enhanced, open lobby. Other upgrades include a state-of-the-art security system and private office space for our Branch Manager and Assistant Manager. Exterior improvements provide easy access to the front entrance and include a front canopy which leads to the ATM vestibule. Additionally, we have enhanced the exterior appearance and paved all points of entry, parking and drive-up areas to ensure safety precautions are in place. For added convenience, we installed a new digital LED message board featuring product information, time and temperature.

On February 19, 2021, we completed renovations at our Hop Bottom office that maintain its historical charm. In September of 1909, the Hop Bottom National Bank Board of Directors was appointed and opened their doors for business at this location, 126 Main Street, in 1910. The newly remodeled 1,750 square foot facility includes a new 350 square foot addition with tinted windows for added privacy and a state-of-the-art security system. The vestibule area was expanded to provide a fully-automatic handicap entry with access to the ATM and Night Depository, providing shelter from the elements. The main lobby ceiling has been refurbished to reveal its original Victorian style tin ceiling, restoring this attractive design element from the 1800s. The teller line has been reconstructed with solid oak and decorative glass to accommodate our customers with improved functionality. The facility has new and improved private office space for our Branch Manager and Assistant Manager. We also upgraded our pylon sign to feature a traditional clock and digital LED message board to share product messaging with the community.

Craig Best, Chief Executive Officer, commented, "We are fortunate to be a part of these communities and look forward to serving the needs of our customers from our new facilities".

LIVE UNITED

PEOPLES SECURITY BANK SUPPORTS THE UNITED WAY'S COMMUNITY IMPACT FUND

The United Way of Lackawanna and Wayne Counties' Community Impact fund helps to support dozens of programs within 18 organizations that work to improve the education, financial stability and health of everyone in our communities. Through the Community Impact fund, the United Way works to ensure people get the help they need now while addressing the root cause of the challenges facing our communities.

Our past contributions have been instrumental in supporting vital programs and services. We can be proud to know that, because of the generosity of our employees and management, the United Way continues to improve lives by funding programs and creating special initiatives that get to the heart of problems and create lasting changes right here in our local communities.

Peoples Security Bank and their employees have received numerous awards over the years; however, we were recognized by the United Way of Lackawanna and Wayne Counties with three separate awards for our 2019-2020 campaign, each with its own distinct honor and recognition. For our continued commitment to the United Way, we were awarded with the following:

- **PILLARS OF OUR COMMUNITY AWARD**, for the third consecutive year, which recognizes our company as being ranked among the top ten giving organizations and part of the foundation for the United Way campaign's success.

- **SPIRIT OF CARING CHAIRMAN'S AWARD**, these awards are presented annually to those who demonstrate exemplary commitment to the people of Lackawanna and Wayne Counties by service above and beyond the community.

- **RISING STAR AWARD**, for the fourth consecutive year, honoring PSBT employees with the recognition of the most new or increased dollars raised during the annual campaign.

Over the past fifteen years, combined employee and corporate contributions to the United Way have totaled nearly $690,000. These contributions have been instrumental in supporting vital programs and services the United Way provides throughout our local communities. The United Way works with their partner agencies to deliver programs and services that target community needs. Although the Community Impact fund program is managed by the United Way of Lackawanna and Wayne Counties, employee pledges may be designated to United Way agencies or other organizations and individuals of choice outside of Lackawanna and Wayne Counties. Last year, employee contributions also provided support to United Way organizations and individuals within: Bucks County, Carbon County, the Greater Hazelton area, the Greater Lehigh Valley, Luzerne County, Monroe County, Northampton County, Schuylkill County, Susquehanna County and Wyoming County in Pennsylvania and Broome County, New York.

2020 LEHIGH VALLEY BUSINESS READER RANKINGS AWARDS

Each year, Lehigh Valley Business (LVB) organizes Reader Rankings Awards. These awards recognize the best that the Lehigh Valley community has to offer. Local businesses are nominated in the following categories: Construction/Design, Education, Employers, Finance/Investments/Insurance, General Business, Health Care, Hospitality/Travel/Entertainment, IT/Tech Support Services, Professional Services and Real Estate. LVB readers vote online for whichever businesses they deem "**the best**" in each category. Lehigh Valley Business received over 31,000 votes from the business community for their 2020 Reader Rankings Awards. Out of all the nominees, Peoples Security Bank was recognized as both **BEST BANK FOR BUSINESS** and **BEST BANK FOR PERSONAL**.

"Peoples Security Bank and Trust is honored to be recognized as Best Bank for Business and Personal by Lehigh Valley Business readers. Having only been servicing the Lehigh Valley for the past six years, it's humbling to be recognized with these awards. The bank has been committed to creating positive change in the communities it serves for over 100 years, and it is proud to add the Lehigh Valley to that service area," stated Neal Koplin, Senior Executive Vice President, Chief Banking Officer.

We've been here for our customers throughout the last century helping them to purchase homes, start and grow their small businesses and protect and grow their assets. We strive to exceed our customers' expectations while helping them achieve their financial goals and helping make our communities better places to live and work.

Peoples Security Bank & Trust Co. has funded over **$217 MILLION** to Local Businesses as part of the CARES Act Paycheck Protection Loan Program in 2020

Peoples Security Bank & Trust Company ("PSBT") has taken proactive measures to approve customer applications for the Paycheck Protection Program ("PPP"), a program enacted by the Federal Government in response to the economic crisis triggered by COVID-19. To date, Peoples Security Bank has processed more than $217 million to over 1,452 small business entities within our local communities. These loans will help to retain thousands of jobs for hard working individuals and help to support their families during this difficult time period.

Since the program was launched on April 3, 2020, the bank's lending team fielded thousands of calls from small business customers who have requested PPP loans to support and sustain their business operations. Led by President and Chief Operating Officer Thomas P. Tulaney, an initial group of 45 employees were assigned to specific roles in the creation of a specialized team to handle the challenges associated with the rollout of the PPP loan program. Our team addressed customer questions and concerns regarding rules, regulations, and eligibility requirements; navigating the SBA portal and online system; and developing a streamlined process to manage the heavy influx of incoming applications for immediate processing.

The bank designed a solutions-oriented approach to barriers that overwhelmed both large banking institutions and community banks since the SBA and U.S. Treasury Department established the financial relief program. This process, coupled with an unwavering commitment from its entire Commercial Lending, Credit Administration and Branch Network teams, allowed the bank to timely and efficiently begin closing loans and disbursing proceeds to these small business customers.

"Small businesses are the backbone of our economy and account for approximately 50% of all private sector jobs. More importantly, small businesses provide character to our communities and strengthen partnerships between residents, community leaders and other public and private sector organizations. As a 115 year old community bank, our immediate focus has been to provide high quality service and innovative products to our small business partners. Peoples Security Bank is proud to support our local small business customers with the CARES Act PPP Loan Program during this very difficult time period," stated Mr. Tulaney.

Thank you!

to our Healthcare Workers for selflessly serving and protecting our communities.

PEOPLES SECURITY BANK PROVIDES SUPPORT TO FRONTLINE WORKERS AND COMMUNITIES AFFLICTED BY COVID-19 CRISIS

In April of 2020, Peoples Security Bank & Trust Company ("PSBT"), pledged over $40,000 to support healthcare workers and regional communities within PSBT's Pennsylvania-based footprint grappling with the impact of the COVID-19 pandemic. This specialized program enacted by PSBT focused on providing goodwill aid specifically to the healthcare workforce, as well as donations to address food stability to vulnerable, at-risk populations.

Peoples Security Bank donated over 1,200 meals from area restaurants, many of which are current customers of the bank, to ten hospitals across the Commonwealth of Pennsylvania. Approximately 120 frontline providers from each hospital - expanding its reach from Bucks County to Susquehanna County - received a lunch or dinner, complimented by a special message of encouragement and appreciation for their selflessness and commitment to their patients. COVID-19 disrupted the global stage and its players in innumerable ways, leaving many individuals, families, and businesses facing unanticipated and devastating obstacles in its wake. "At Peoples Security Bank, our primary concern has and will continue to be taking immediate, actionable steps to unwaveringly support our customers, our communities, and our heroic healthcare workers and first responders who have risen to the occasion for all they have done to keep us healthy and protected," stated Neal Koplin, Senior Executive Vice President and Chief Banking Officer.

In addition to the delivery of meals to frontline workers and a $10,000 donation to the Greater Easton Development Partnership, charitable monetary gifts totaling more than $15,000 were disbursed to twelve food banks in need in our area.

To honor their continued service and sacrifices amid the global health threat facing the nation, Peoples Security Bank also installed banners on the side of its Central City Scranton branch in Scranton, as well as the Emrick Boulevard Regional Office in Bethlehem, to thank the healthcare community for its ongoing efforts.

OUR LOCATIONS

BUCKS COUNTY | PA

Doylestown
325 S Main St, Doylestown, PA 18901
(215) 348-8207

BROOME COUNTY | NY

Binghamton West Side
273 Main St, Binghamton, NY 13905
(607) 729-3832

Conklin
1026 Conklin Rd, Conklin, NY 13748
(607) 722-2114

LACKAWANNA COUNTY | PA

Abington
1100 Northern Blvd, S Abington Twp, PA 18411
(570) 587-4898

Central City Scranton
150 N Washington Ave, Scranton, PA 18503
(570) 955-1700

East Scranton
968 Prescott Ave, Scranton, PA 18510
(570) 342-9101

Glenburn
494 N Gravel Pond Rd, Clarks Summit, PA 18411
(570) 585-5130

Green Ridge
1901 Sanderson Ave, Scranton, PA 18509
(570) 346-4695

Minooka
420 Davis St, Scranton, PA 18505
(570) 955-1883

Moscow
141 N Main St, Moscow, PA 18444
(570) 842-7626

Old Forge
216 S Main St, Old Forge, PA 18518
(570) 451-7200

Peckville
540 Main St, Peckville, PA 18452
(570) 383-2154

LEBANON COUNTY | PA

Central PA Business Center
830 Norman Dr, Lebanon, PA 17042
(717) 279-2200

LEHIGH COUNTY | PA

Airport Rd
2355 City Line Rd, Bethlehem, PA 18017
(610) 691-1202

Tilghman St
3920 W Tilghman St, Allentown, PA 18104
(610) 398-9680

LUZERNE COUNTY | PA

Kingston
435 Wyoming Ave, Kingston, PA 18704
(570) 288-0128

MONROE COUNTY | PA

Mount Pocono
1322 Pocono Blvd, Mount Pocono, PA 18344
(570) 839-8732

MONTGOMERY COUNTY | PA

King of Prussia
610 Freedom Business Center Dr
Suite 105, King of Prussia, PA 19406
(610) 205-1880

NORTHAMPTON COUNTY | PA

Emrick Blvd
2151 Emrick Blvd, Bethlehem, PA 18020
(610) 317-4690

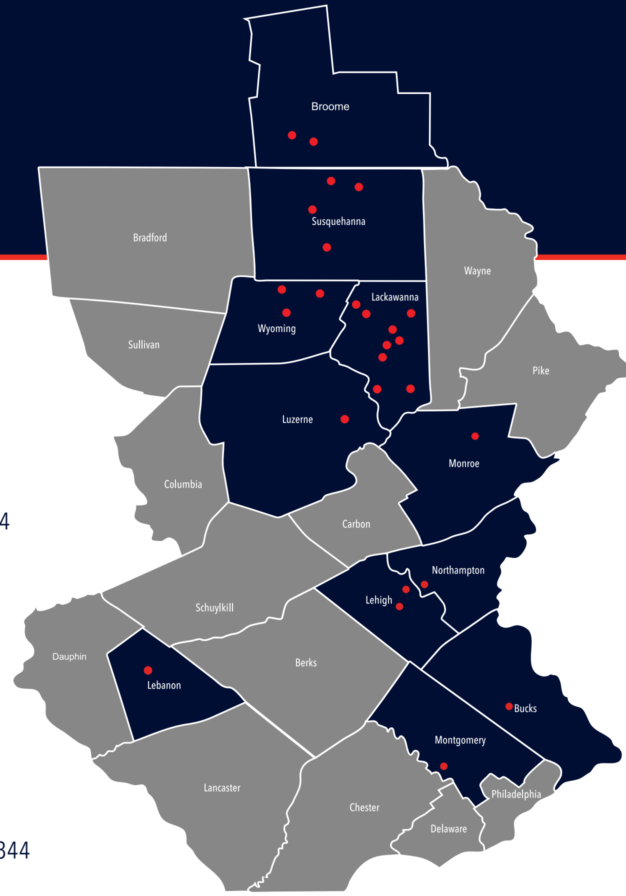
SUSQUEHANNA COUNTY | PA

Hallstead
25109 State Rt 11, Hallstead, PA 18822
(570) 879-2195

Hop Bottom
126 Main St, Hop Bottom, PA 18824
(570) 289-4124

Montrose
695 Grow Ave, Montrose, PA 18801
(570) 278-4100

Susquehanna
215 Erie Blvd, Susquehanna, PA 18847
(570) 853-4901



WYOMING COUNTY | PA

Meshoppen
8178 State Rt 6, Meshoppen, PA 18630
(570) 833-5171

Nicholson
42–48 State St, Nicholson, PA 18446
(570) 942-2265

Tunkhannock
83 E Tioga St, Tunkhannock, PA 18657
(570) 836-2135

OFF-SITE ATMs

Geisinger Commonwealth School of Medicine
525 Pine Street, Scranton, PA

Lackawanna College
501 Vine Street, Scranton, PA

Meadow Avenue
Meadow Avenue & Hemlock Street
Scranton, PA

Radisson Lackawanna Station Hotel
700 Lackawanna Avenue, Scranton, PA

Saint Mary's Villa Nursing Home
516 Saint Mary's Villa Road,
Elmhurst Township, PA

CORPORATE INFORMATION

CORPORATE HEADQUARTERS
150 North Washington Avenue | Scranton, PA 18503
(570) 346-7741 | (888) 868-3858 | psbt.com

INVESTOR RELATIONS OFFICER
Marie L. Luciani | (570) 346-7741 x2352 | (888) 868-3858 x2352

STOCK INFORMATION
The common stock of Peoples Financial Services Corp. is listed on the NASDAQ Stock Market under the ticker symbol PFIS.

STOCK TRANSFER AND REGISTRAR AGENT
AMERICAN STOCK TRANSFER & TRUST COMPANY, LLC
6201 15th Avenue | Brooklyn, NY 11219
(718) 921-8124 | (800) 937-5449

FORM 10-K ANNUAL REPORT
A copy of our form 10-K for the year ended December 31, 2020 is included herein. ***Copies of the company's Annual Report to the Securities and Exchange Commission on Form 10-K, quarterly reports on Form 10-Q and news releases may be obtained without charge upon request to:***
Marie L. Luciani | Investor Relations Officer
150 North Washington Avenue | Scranton, PA 18503

VIRTUAL ANNUAL MEETING
Saturday, May 15, 2021, 9:00am
www.virtualshareholdermeeting.com/PFIS2021

DIVIDEND CALENDAR
Dividends on Peoples Financial Services Corp. common stock are customarily payable on or about the 15th of March, June, September and December.

DIVIDEND REINVESTMENT PLAN
American Stock Transfer & Trust Company, LLC administers a Dividend Reinvestment Plan and Stock Purchase Plan. Additional information may be obtained on American Stock Transfer & Trust Company's website: astfinancial.com.

DIRECT DEPOSIT OF DIVIDENDS
As a shareholder of Peoples Financial Services Corp., you may have your dividend payments deposited directly into a personal checking, savings, or other account. Direct deposit of your dividend eliminates the chance of your dividend check being lost or stolen and is credited to your account on the same day that the dividend is paid. To begin direct deposit of your dividend, please contact Marie L. Luciani, Investor Relations Officer, at the Corporate Headquarters address.

INDEPENDENT AUDITORS
Baker Tilly US, LLP
7535 Windsor Drive, Suite 300 | Allentown, PA 18195-1014
(610) 336-8180

GENERAL COUNSEL
Jerry Weinberger, Esq. | Jerry Weinberger P.C.
345 Wyoming Avenue | Suite 200 | Scranton, PA 18503
(570) 963-8880

SEC COUNSEL
Troutman Pepper Hamilton Sanders, LLP
3000 Two Logan Square | Eighteenth & Arch Streets
Philadelphia, PA 19103 | (215) 981-4000

TRUST COUNSEL
James W. Reid, Esq. | Oliver, Price & Rhodes
1212 South Abington Road | Clarks Summit, PA 18411
(570) 585-1200

MARKET MAKERS
Boenning & Scattergood, Inc.
4 Tower Bridge | 200 Barr Harbor Drive | Suite 300
West Conshohocken, PA 19428 | (610) 862-5368

Griffin Financial Group, LLC
440 Monticello Avenue | Suite 1824 | Norfolk, VA 23510
(757) 955-8444

Keefe Bruyette & Woods (KBW)
The Equitable Building | 787 7th Avenue | New York, NY 10019
(212) 887-8996

Piper Sandler
1251 Avenue of the Americas | 6th Floor | New York, NY 10020
(800) 635-6851

PRODUCTS AND SERVICES
Detailed information on our products and services offered by Peoples Security Bank & Trust can be obtained by visiting psbt.com or by calling (888) 868-3858 or (570) 346-7741.

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

FORM 10-K

(Mark One)

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

For the fiscal year ended December 31, 2020

☐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: 001-36388

Peoples Financial Services Corp.
(Exact name of registrant as specified in its charter)

Pennsylvania	**23-2391852**
State or other jurisdiction of incorporation or organization	**(I.R.S. Employer Identification No.)**

150 North Washington Avenue,
Scranton, PA 18503
(Address of principal executive offices) (Zip Code)

(570) 346-7741
Registrant's telephone number, including area code

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

Title of each class	Trading Symbol	Name of each exchange on which registered
Common stock, $2.00 par value	**PFIS**	**The Nasdaq Stock Market**

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

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

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

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

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

Indicate by check mark 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	☒
Emerging growth company	☐		

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

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

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

The aggregate market value of the registrant's common stock held by non-affiliates of the registrant on June 30, 2020 was $280,041,771 (based on the closing sales price of the registrant's common stock on that date).

The number of shares of the registrant's common stock outstanding as of February 28, 2021 was 7,203,101.

DOCUMENTS INCORPORATED BY REFERENCE

Portions of the registrant's definitive proxy statement to be filed in connection with solicitation of proxies for its 2021 annual meeting of shareholders, within 120 days of the end of registrant's fiscal year, are incorporated by reference into Part III of this Annual Report on Form 10-K.

Peoples Financial Services Corp.
Form 10-K
For the Year Ended December 31, 2020
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Cautionary Note Regarding Forward-Looking Statements.

This Annual Report on Form 10-K contains forward-looking statements within the meaning of Section 27A of the Securities Act, as amended, and Section 21E of the Securities Exchange Act of 1934, as amended, which are subject to risks and uncertainties. These statements are based on assumptions and may describe future plans, strategies and expectations of Peoples Financial Services Corp. and its subsidiaries. These forward-looking statements are generally identified by use of the words "believe," "expect," "intend," "anticipate," "estimate," "project" or similar expressions. All statements in this report, other than statements of historical facts, are forward-looking statements.

The ability of Peoples Financial Services Corp. to predict results or the actual effect of future plans or strategies is inherently uncertain. Important factors that could cause our actual results to differ materially from those in the forward-looking statements include, but are not limited to: the unfolding of the coronavirus ("COVID-19") crisis and the governmental responses to the crisis; risks associated with business combinations; changes in interest rates; economic conditions, particularly in our market area; legislative and regulatory changes and the ability to comply with the significant laws and regulations governing the banking and financial services business; monetary and fiscal policies of the U.S. government, including policies of the U.S. Department of Treasury and the Federal Reserve System; credit risk associated with lending activities and changes in the quality and composition of our loan and investment portfolios; demand for loan and other products; deposit flows; competition; changes in the values of real estate and other collateral securing the loan portfolio, particularly in our market area; changes in relevant accounting principles and guidelines; inability of third party service providers to perform; and our ability to prevent, detect and respond to cyberattacks. Additional factors that may affect our results are discussed in Item 1A to this Annual Report on Form 10-K titled "Risk Factors".

These risks and uncertainties should be considered in evaluating forward-looking statements and undue reliance should not be placed on such statements. Except as required by applicable law or regulation, we do not undertake, and specifically disclaim any obligation, to release publicly the result of any revisions that may be made to any forward-looking statements to reflect events or circumstances after the date of the statements or to reflect the occurrence of anticipated or unanticipated events.

Part I

Item 1. Business.

General

Peoples Financial Services Corp., a bank holding company incorporated under the laws of Pennsylvania, provides a full range of financial services through its wholly-owned subsidiary, Peoples Security Bank and Trust Company.

Unless the context indicates otherwise, all references in this annual report to the "Peoples," "Company," "we," "us" and "our" refer to Peoples Financial Services Corp. and its subsidiaries. Peoples Security Bank and Trust Company is sometimes referred to as "Peoples Bank."

Peoples Bank is a state-chartered bank and trust company under the jurisdiction of the Pennsylvania Department of Banking and Securities and the Federal Deposit Insurance Corporation, or "FDIC." Peoples Bank's twenty-six community banking offices, all similar with respect to economic characteristics, share a majority of the following aggregation criteria: products and services; operating processes; customer bases; delivery systems; and regulatory oversight. Accordingly, they are aggregated into a single operating segment.

Market Areas

Our principal market area consists of Bucks, Lackawanna, Lebanon, Lehigh, Luzerne, Monroe, Montgomery, Northampton, Susquehanna, Wayne and Wyoming Counties in Pennsylvania and Broome County in New York. In addition, parts of Bradford and Schuylkill Counties in Pennsylvania are also considered part of the market area. Approximately half of our offices are located in and around Scranton, the largest city in Lackawanna County.

Specifically, we conduct the majority of our business in our legacy market of Binghamton and the southern tier of New York and northeastern Pennsylvania. Our recent growth strategy expanded our operations into the Greater Lehigh Valley, King of Prussia and the Greater Delaware Valley of southeastern Pennsylvania and suburban Philadelphia, and south central Pennsylvania.

Peoples commenced a growth strategy during the fourth quarter of 2014 with the opening of a community banking office in the Lehigh County market. During 2017, the Company added two additional branch offices, one in Allentown, Lehigh County and one in Bethlehem, Northampton County to continue our strategic expansion initiative into the Greater Lehigh Valley market. This market has a greater population than the other counties served, with Bethlehem being the second largest city within Lehigh County.

In 2015, the Company entered the King of Prussia market, which includes parts of Bucks and Montgomery counties of Pennsylvania and suburban Philadelphia, with the establishment of a loan production office and a team of experienced lenders. During the fourth quarter of 2016, a retail branch office was established, replacing the loan production office, and staffed by personal bankers and our experienced lenders. Montgomery and Bucks counties are two of the wealthiest counties in Pennsylvania. Significant types of employment industries include pharmaceuticals, health care, electronics, computer services, insurance, industrial machinery, retailing, schools and meat processing.

In 2019, the Company entered the south central Pennsylvania market with the establishment of a full-service branch in Lebanon County. A team of experienced lenders in this market was recruited to serve the Lancaster, Lebanon, and Harrisburg market. In 2020, the bank expanded further into the Greater Delaware Valley by opening a branch office in Doylestown, Bucks County and recruiting an experienced lending team.

In 2020, the Company permanently closed its Duryea, Gouldsboro, and South Scranton branches which had been temporarily closed during the pandemic. Each of the branches were consolidated into branches within close proximity and we re-allocated the operating expenses to the markets identified in our growth strategy.

The Marcellus Shale formation located in the heart of our northern market area has provided economic benefits to the communities served and as a result to us. Natural gas producers have invested billions of dollars in Pennsylvania in lease and land acquisition, new well drilling, infrastructure development and community partnerships.

COVID-19

As the COVID-19 events continue to unfold, our continued priority is the health and safety of our employees and customers. Our management team continues to implement its pandemic plan by modifying and enhancing strategies and protocols intended to protect our workforce and customers, maintain services for customers, assure the functional continuity of our operating systems, controls and processes, and mitigate financial risks posed by changing market conditions. We have followed the recommendations of our state governments by imposing business travel restrictions, implementing quarantine and work from home protocols and physically separating, to the extent possible, the critical operations site workforce that are unable to work remotely. As of March 1, 2021, we have re-opened the majority of our branch lobbies to the public with safety protocols in place. Our remaining branches are operating with drive-up services, with lobby access available by appointment only. We have also maintained active communications with our primary regulatory agencies and critical vendors in an effort to keep all mission-critical activities and functions performing in line with regulatory expectations and the Company's service standards.

The impact of the COVID-19 pandemic is fluid and continues to evolve, adversely affecting many of the Bank's clients. The COVID-19 pandemic and its associated impacts on trade (including supply chains), travel, employee productivity, unemployment, consumer spending, and other economic activities have resulted in less economic activity and significant volatility and disruption in financial markets, and has had an adverse effect on our business, financial condition and results of operations. The ultimate extent of the impact of the COVID-19 pandemic on our business, financial condition and results of operations is currently uncertain and will depend on various developments and other factors, including, among others, the duration and scope of the pandemic, as well as governmental, regulatory and private sector responses to the pandemic, and the associated impacts on the economy, financial markets and our customers, employees and vendors. Our business, financial condition and results of operations generally rely upon the ability of our borrowers to repay their loans, the value of collateral underlying our secured loans, and demand for loans and other products and services we offer, which are highly dependent on the business environment in our primary markets where we operate and in the United States generally.

We have participated as a lender in the Coronavirus Aid, Relief and Economic Security Act ("CARES Act"), Paycheck Protection Program ("PPP"), a $350 billion specialized low-interest loan program funded by the U.S. Treasury Department and administered by the U.S. Small Business Administration ("SBA"). The PPP provides borrower guarantees for lenders, as well as loan forgiveness incentives for borrowers that utilize the SBA loan proceeds to cover employee compensation related business operating costs. Our loan officers guided our commercial customers through the application process and now are guiding them through the forgiveness process and the second round of PPP. During 2020, we approved 1,450 PPP loans totaling $217.5 million. Substantially all of the loans were made to existing customers, funded under the two year PPP loan program, and the loan proceeds initially were deposited with our institution. At origination, loan fee income totaled $7.0 million and is being earned primarily over the 24-month duration of the loans as a part of the loan yield. PPP loan forgiveness commenced during the fourth quarter of 2020 with $27.8 million of forgiveness being received by our borrowers. We expect the majority of the remaining $189.7 million of PPP loans to be forgiven during 2021. At December 31, 2020, $4.0 million of fees remain to be earned in future periods and may be accelerated based on the timing of forgiveness of PPP loans by the SBA. In addition, the Company is participating in the 2021 second round of PPP lending and has received approval by the SBA on 605 applications totaling $80.7 million. The loans closed during January and February.

From a credit risk perspective, we took actions to identify and assess our COVID-19 related credit exposures based on asset class and borrower type. From the onset of the crisis, we worked to proactively monitor our loan portfolio by contacting many of our borrowers to evaluate the impact of the pandemic on them, their businesses and the underlying collateral for our loans. The Company implemented a customer payment deferral program to assist both consumer and business borrowers that may be experiencing financial hardship due to COVID-19 related challenges. For borrowers who received a loan payment deferral we worked with the borrowers to evaluate the potential for further deterioration of credit quality at the end of the deferral period. We evaluated our commercial loan and commercial real estate loan portfolios to identify those loans in industries that are most at risk or where other information indicates the borrower may be significantly impacted by the effects of COVID-19. The Company granted payment deferral requests for up to six months to a total of 481 commercial loans with outstanding loan balances of $306.9 million and to 505 consumer loans with outstanding balances of $23.3 million. At December 31, 2020, the majority of loans are no longer in deferral as borrowers have begun to make their regular payments. Outstanding loan balances remaining in deferral at December 31, 2020 totaled $6.1 million, a decrease of $324.0 million from the $330.1 million in deferral at June 30, 2020. As a percentage of total loan balances, excluding PPP loans, loans in deferral represented 0.6% of loans outstanding at December 31, 2020 compared to 16.7% of loans outstanding at June 30, 2020. At December 31, 2020, commercial loan balances remaining in deferral total $5.8 million while consumer loans total $0.3 million. Loan deferrals and modifications have been executed consistent with the guidelines of the CARES Act.

Human Capital Resource

Staffing. At December 31, 2020, our 352 full-time employees and 32 part-time employees are the keys to the success of Peoples. We are committed to attracting, retaining and promoting top quality talent regardless of race, color, religion, sex, sexual orientation, gender identity, national origin, age, disability or genetic information. We strive to identify and select the best candidates for all open positions based on qualifying factors for each job. We are dedicated to providing a workplace for our employees in which they are treated with dignity, decency and respect; that is inclusive, supportive, and free of any form of discrimination or harassment; rewarding and recognizing our employees based on their individual results and performance; and recognizing and respecting all of the characteristics and differences that make each of our employees unique.

Core values. We strive to meet our core values of integrity, excellence, teamwork and efficiency. Integrity is our foundation, the basis of everything we do, to be professional, honest, trustworthy, confidential and respectful at all times. We work together for a common good, engage our customers, coworkers, and partners. We work together to exceed our customers' expectations as we pro-actively help them achieve their goals, to create a dynamic environment that promotes life-long learning and personal growth of our employees, and to help to make our communities better places to live and work by being an important contributor of time, talent, and resources.

Diversity, Equity and Inclusion. Peoples is committed to fostering, cultivating and preserving a culture of diversity and inclusion. Our human capital is the most valuable asset we have. The collective sum of the individual differences, life experiences, knowledge, inventiveness, innovation, self-expression, unique capabilities and talent that our employees invest in their work represents a significant part of not only our culture, but our reputation and company's achievement as well.

We embrace and encourage our employees' differences in age, color, disability, ethnicity, family or marital status, gender identity or expression, language, national origin, physical and mental ability, political affiliation, race, religion, sexual orientation, socio-economic status, veteran status, and other characteristics that make our employees unique.

Health & Safety. Our health and safety policies, procedures and guidelines mandate all tasks be conducted in a safe and efficient manner complying with all local, state and federal safety and health regulations, and special safety concerns. Our policies and procedures encompass all facilities and operations and addresses on-site emergencies, injuries and illnesses, evacuation procedures, cell phone usage and general safety rules.

As the COVID-19 crisis unfolded throughout 2020, the safety and well-being of our employees and families, customers, and communities were our top priority. We implemented our pandemic plan and executed various strategies and protocols intended to protect our employees, maintain services for customers, assure functional continuity of the Company's operating systems, controls and processes, and mitigate financial risks posed by changing market conditions. We directed and enabled approximately 46% of our workforce to work remotely, imposed business travel restrictions, implemented quarantine protocols and physically separated, to the extent possible, the critical operations site workforce that are unable to work remotely. To limit the risk of virus spread, the Company implemented drive-thru only and by appointment operating protocols for its bank branch network. We followed the recommendations of our state and local governments as to conducting business.

Benefits. We are committed to offering a competitive total compensation package. We regularly compare compensation and benefits with peer companies and market data, making adjustments as needed to ensure compensation stays competitive. We also offer a wide array of benefits for our workforce and their families, including:

•Comprehensive medical, dental, and vision benefits, as well as group life insurance, accidental death and dismemberment insurance, voluntary life insurance, and short-term and long-term disability insurance for all eligible employees

•Employee Assistance Program

•401(k) Profit Sharing Plan

•Employee Stock Ownership Plan (ESOP)

•Disaster pay

•Paid time off (PTO), holidays and bank holidays

•Unpaid leave of absence

•Internal training and online development courses

•Tuition reimbursement for eligible associates

Products and Services

Our primary products are loans to small- and medium-sized businesses. Other lending products include one-to-four family residential mortgages and consumer loans. We fund our loans, primarily, by offering deposits to commercial enterprises and individuals. Our deposit products include certificates of deposits and various demand deposit accounts.

We generate interest income from our loan and securities portfolios. Other income is generated primarily from merchant transaction fees, trust and wealth management fees, fees generated from commercial loan interest rate swap transactions and service charges on deposit accounts. Our primary costs are interest paid on deposits and borrowings and general operating expenses. We provide a variety of commercial and retail banking services to business, non-profits, governmental, municipal agencies and professional customers, as well as retail customers, on a personalized basis. Our primary lending products are real estate, commercial and consumer loans. We also offer ATM access, credit cards, active investment accounts, trust department services and other various lending, depository and related financial services. Our primary deposit products are savings and demand deposit accounts and certificates of deposit.

We are not dependent upon a single customer, or a few customers, the loss of one or more of which would have a material adverse effect on our operations. In the ordinary course of our business, our operations and earnings are not materially affected by seasonal changes or by compliance with federal, state or local environmental laws or regulations.

Lending Activities

We provide a full range of retail and commercial lending products designed to meet the borrowing needs of consumers and small- and medium-sized businesses in our market areas. A significant amount of our loans are to customers located within our market area. We have no foreign loans or highly leveraged transaction loans, as defined by the Federal Reserve Board. Although we participate in loans originated by other banks, we have originated the majority of the loans in our portfolio.

Our retail lending products include the following types of loans, among others: residential real estate; automobiles; manufactured housing; personal and home equity. Our commercial lending products include the following types of loans, among others: commercial real estate; working capital; equipment and other commercial needs; construction; Small Business Administration; and agricultural and mineral rights. The terms offered on a loan vary depending primarily on the type of loan and credit-worthiness of the borrower.

Payment risk is a function of the economic climate in which our lending activities are conducted. Economic downturns in the economy generally or in a particular sector could cause cash flow problems for customers and make loan payments more difficult. We attempt to minimize this risk by not being exposed to loan concentrations of a single customer or a group of customers, the loss of any one or more of whom would have a materially adverse effect on our financial condition. One element of interest rate risk arises from our fixed rate loans in an environment of changing interest rates. We attempt to mitigate this risk by making adjustable rate commercial loans and by limiting repricing terms to five years or less for customers requiring fixed rate loans. Our lending activity also exposes us to risks that any collateral we take as security is not adequate. We attempt to manage collateral risk by avoiding loan concentrations to particular borrowers, by perfecting liens on collateral and by obtaining appraisals on property prior to extending loans. We attempt to mitigate our exposure to these and other types of risks by stratifying authorization requirements by loan size and complexity.

We offer a variety of loans including commercial, residential and consumer loans as described above. The consumer portfolio includes automobile loans, educational loans and lines of credit.

We intend to continue to evaluate commercial real estate, commercial business and governmental lending opportunities, including small business lending. We continue to proactively monitor and manage existing credit relationships.

We have not engaged in sub-prime residential mortgage lending, which is defined as mortgage loans advanced to borrowers who do not qualify for market interest rates because of problems with their credit history. We focus our lending efforts within our market area.

One-to-Four Family Residential Loans. We offer two types of residential mortgage loans: fixed-rate loans, with terms of up to 30 years, and adjustable-rate loans, with interest rates and payments that adjust annually after an initial fixed period of one, three, five or ten years. Interest rates and payments on our adjustable-rate loans generally are adjusted to a rate equal to a percentage above the appropriate U.S. Treasury Security Index. Our adjustable-rate single-family residential real estate loans generally have caps on increases or floors on decreases in the interest rate at any adjustment date, and a maximum adjustment limit over the life of the loan. Although we offer adjustable-rate loans with initial rates below the fully indexed rate, loans tied to the one-year constant maturity Treasury are underwritten using methods approved by the Federal Home Loan Mortgage Corporation, which require borrowers to be qualified at a rate equal to 200 basis points above the discounted loan rate under certain conditions.

Borrower demand for adjustable-rate loans compared to fixed-rate loans is a function of the level of interest rates, the expectations of changes in the level of interest rates, and the difference between the interest rates and loan fees offered for fixed-rate mortgage loans as compared to the interest rates and loan fees for adjustable-rate loans, among other factors. The loan fees, interest rates and other provisions of mortgage loans are determined by us on the basis of our own pricing criteria and competitive market conditions.

Most of our residential loans are underwritten to standards established by the secondary market. We also offer mortgages partially insured by the U.S. Department of Veteran Affairs (“VA”) and Federal Housing Administration (“FHA”) loans via a third party lending source.

While one-to-four family residential real estate loans are normally originated with up to 30-year terms, such loans typically remain outstanding for substantially shorter periods because borrowers often prepay their loans in full either upon sale of the property pledged as security or upon refinancing the original loan. Therefore, average loan maturity is a function of, among other factors, the level of purchase and sale activity in the real estate market, prevailing interest rates and the interest rates payable on outstanding loans. We do not offer loans with negative amortization or interest only loans.

We offer home equity loans and lines of credit, typically with a maximum combined loan-to-value ratio of 80%. Home equity loans generally have fixed-rates of interest and are originated with terms of up to 15 years. Home equity lines of credit generally have variable rates and are indexed to the prime rate. Home equity lines of credit generally have draw periods with 20 year repayment periods.

We generally do not make high loan-to-value loans (defined as loans with a loan-to-value ratio in excess of 80%) without private mortgage insurance. The maximum loan-to-value ratio we generally permit is 95% with private mortgage insurance. We require all properties securing residential mortgage loans to be appraised by a board-approved independent appraiser. We generally require title insurance on all first mortgage loans. Borrowers must obtain hazard insurance, and flood insurance is required for loans on properties located in a flood zone.

Commercial Real Estate Loans. We offer commercial real estate loans secured by real estate primarily with adjustable rates. We originate a variety of commercial real estate loans generally for terms up to 25 years and payments based on an amortization schedule of up to 25 years. These loans are typically based on either the Federal Home Loan Bank borrowing rate or our own pricing criteria and adjust every three, five, seven or ten years. Commercial real estate loans also are originated for the acquisition and development of land, including development for residential use. Conditions of acquisition and development loans originated generally limit the number of model homes and homes built on speculation, and draws are scheduled against executed agreements of sale. Commercial real estate loans for the acquisition and development of land are typically based upon the prime rate. Commercial real estate loans for developed real estate and for real estate acquisition and development are originated generally with loan-to-value ratios up to 75%, while loans for the acquisition of land are originated with a maximum loan to value ratio of 65%.

Loans secured by commercial real estate generally have larger balances and involve a greater degree of risk than one-to-four family residential mortgage loans. Of primary concern in commercial real estate lending is the borrower's and any guarantor's creditworthiness and the feasibility and cash flow potential of the financed project. Additional considerations include: location, market and geographic concentrations, loan to value, strength of guarantors and quality of tenants. Payments on loans secured by income properties often depend on successful operation and management of the properties. As a result, repayment of such loans may be subject to a greater extent than residential real estate loans, to adverse conditions in the real estate market or the economy. To monitor cash flows on income properties, we require borrowers and loan guarantors, if any, to provide annual consolidated financial statements on commercial real estate loans and rent rolls where applicable. In reaching a decision on whether to make a commercial real estate loan, we consider and review a cash flow analysis of the borrower and guarantor, when applicable, and consider the net operating income of the property, the borrower's expertise, credit history and profitability and the value of the underlying property. We have generally required that the properties securing these real estate loans have debt service coverage ratios (the ratio of earnings before debt service to debt service) of at least 1.2 times. An environmental report is obtained when the possibility exists that hazardous materials may exist or have existed on the site, or the site may be or have been impacted by adjoining properties that handled hazardous materials.

Commercial Loans. We offer commercial business loans to professionals, sole proprietorships and small businesses in our market area. We offer term loans for capital improvements, equipment acquisition and long-term working capital. These loans are typically priced at short term fixed rates or variable rates based on the prime rate. These loans are secured by business assets other than real estate, such as business equipment and inventory, and, generally, are backed by personal guarantees of the owner or owners of the business. We originate lines of credit to finance the working capital needs of businesses to be repaid by seasonal cash flows or to provide a period of time during which the business can borrow funds for planned equipment purchases.

We have participated in the CARES Act, Paycheck Protection Program, a $350 billion specialized low-interest loan program funded by the U.S. Treasury Department and administered by the U.S. Small Business Administration. The PPP provides borrower guarantees for lenders, as well as loan forgiveness incentives for borrowers that utilize the loan proceeds to cover employee compensation-related business operating costs.

When making commercial business loans, we consider the consolidated financial statements of the borrower and any guarantors, the borrower's payment history of both corporate and personal debt, the debt service capabilities of the borrower, the projected cash flows of the business and guarantor, the viability of the industry in which the customer operates and the value of the collateral.

Unlike residential mortgage loans, which generally are made on the basis of the borrower's ability to make repayment from his or her employment or other income, and which are secured by real property, the value of which 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 depend substantially on the success of the business itself. Further, any collateral securing such loans may depreciate over time, may be difficult to appraise and may fluctuate in value.

Consumer Loans. We offer a variety of consumer loans, including lines of credit, automobile loans and loans secured by savings accounts and certificates of deposit. We also offer unsecured loans.

Consumer loans may entail greater risk than do residential mortgage loans, particularly in the case of consumer loans that are unsecured or secured by assets that depreciate rapidly, such as motor vehicles. In the latter case, repossessed collateral for a defaulted consumer loan may not provide an adequate source of repayment for the outstanding loan and a small remaining deficiency often does not warrant further substantial collection efforts against the borrower. Consumer loan collections depend on the borrower's continuing financial stability, and therefore are likely to be adversely affected by various factors, including job loss, divorce, illness or personal bankruptcy. Furthermore, the application of various federal and state laws, including federal and state insolvency laws, may limit the amount that can be recovered on such loans.

Loans secured by new and used automobiles are offered, primarily indirectly through dealerships. These loans have fixed interest rates and generally have terms up to seven years. We offer automobile loans with loan-to-value ratios of up to 100% or more of the purchase price of the vehicle depending upon the credit history of the borrower and other factors.

Consumer loans secured by savings accounts and certificates of deposit held by us are offered based upon the deposit rates plus a margin with terms up to five years. We offer such loans up to 100% of the principal balance of the certificate of deposit or balance in the savings account. We also offer unsecured loans and lines of credit with terms up to five years. Our unsecured loans and lines of credit bear a substantially higher interest rate than our secured loans and lines of credit.

The procedures for underwriting consumer loans include an assessment of the applicant's payment history on other debts and ability to meet existing obligations and payments on the proposed loan. Although the applicant's creditworthiness is a primary consideration, the underwriting process also includes a comparison of the value of the collateral, if any, to the proposed loan amount.

We have adhered and continue to adhere to credit policies, which management believes are sound. Our loan policies require verification of information provided by loan applicants as well as an assessment of their ability to repay for all loans. At no time have we made loans similar to those commonly referred to as "no doc" or "stated income" loans.

While the vast majority of the loans in our loan portfolio are secured by collateral, we have made and will continue to make loans on an unsecured basis. Unsecured commercial loans are only granted to those borrowers exhibiting historically strong cash flow and capacity with seasoned management. Unsecured consumer loans are made for relatively short terms and to borrowers with strong credit histories.

Requests to modify, restructure or otherwise change the terms of loans are considered on an individual basis as circumstances and/or reasons for such changes may vary. All such changes in terms must be authorized by the appropriate approval body. Also, our credit policy prohibits the modification of loans or the extension of additional credit to borrowers who are not current on their payments. Exceptions are approved only where our position in the credit relationship is expected to be enhanced by such action.

Adjustable-Rate Loans. While we anticipate that adjustable-rate loans will better offset the adverse effects of an increase in interest rates as compared to fixed-rate loans, an increased monthly loan payment required of adjustable-rate loan borrowers in a rising interest rate environment could cause an increase in delinquencies and defaults. The marketability of collateral also may be adversely affected in a high interest rate environment. In addition, although adjustable-rate mortgage loans make our asset base more responsive to changes in interest rates, the extent of this interest sensitivity is limited by the annual and lifetime interest rate adjustment limits on residential mortgage loans. We attempt to negotiate floors on most adjustable rate commercial loans. The commercial adjustable rate loans generally provide a fixed rate re-negotiation at the end of the initial fixed rate period. If we and the borrower are unable to agree on a new fixed rate then the rate converts to a floating rate obligation. In addition, some commercial loans adjust to a predetermined index plus a spread at the end of the initial fixed rate period, for a like period of time. To a lesser degree, we have entered into transactions with collars generally for periods of five years or less.

Loan Originations. Loan originations come from a number of sources. The primary sources of loan originations are existing customers, walk-in traffic, advertising and referrals from customers. We also purchase participations in loans from local financial institutions to supplement our lending portfolio. Loan participations are subject to the same credit analysis and loan approvals as the loans we originate. We are permitted to review all of the documentation relating to any loan in which we participate. However, in a purchased participation loan, we do not service the loan and are subject to the policies and practices of the lead lender with regard to monitoring delinquencies, pursuing collections and instituting foreclosure proceedings.

Loan Approval Procedures and Authority. Our lending activities follow written, non-discriminatory, underwriting standards and loan origination procedures established by our board of directors and management. The board of directors has granted loan approval authority to certain officers or groups of officers up to prescribed limits, based on the officer's experience.

Loans to One Borrower. The maximum amount that we may lend to one borrower and the borrower's related entities generally is limited, by regulation, to 15% of the capital accounts of Peoples Bank. Capital accounts include the aggregate of capital, surplus, undivided profits, capital securities and reserve for loan losses. At December 31, 2020, our regulatory limit on loans to one borrower was $46.2 million.

Deposit Activities

Our primary source of funds is the cash flow provided by our financing activities, mainly deposit gathering. Other sources of funds are provided by investing activities, including principal and interest payments on loans and investment securities, and operating activities, primarily net income. We offer a variety of deposit accounts with a range of interest rates and terms, including, among others: money market accounts; NOW accounts; savings accounts; certificates of deposit; individual retirement accounts, and demand deposit accounts. These deposits are primarily obtained from areas surrounding our branch offices. We rely primarily on marketing, product innovation, technology, service and long-standing relationships with customers to attract and retain these deposits. Other deposit related services include: remote deposit capture; automatic clearing house transactions; cash management services; automated teller machines; point of sale transactions; safe deposit boxes; night depository services; direct deposit, and official check services.

Trust, Wealth Management and Brokerage Services

Through our trust department, we offer a broad range of fiduciary and investment services. Our trust and investment services include investment management, IRA trustee services, estate administration, living trusts, trustee under will, guardianships, life insurance trusts, custodial services / IRA custodial services, corporate trusts, and pension and profit sharing plans.

We provide a comprehensive array of wealth management products and services to individuals, small businesses and nonprofit entities. These products and services include the following, among others: investment portfolio management; estate planning; annuities; business succession planning; insurances; retirement plan services; education funding strategies, and tax planning.

We have a third party marketing agreement with a broker-dealer that allows us to offer a full range of securities, brokerage services and annuity sales to our customers. Our investor services division is located in our headquarters building and the services are offered throughout the branch system. Through this relationship, our clients have access to a wide array of financial and wealth management strategies, including services such as professional money management, retirement and education planning, and investment products including stocks, bonds, mutual funds, annuities and insurance products.

Merchant Services

We offer credit card processing and a variety of other products and services to our merchant customers, through a marketing and sales agreement with an industry leader in payment processing services. Services include small business checking accounts, merchant money market accounts, online banking, telephone banking, business credit cards, merchant line of credit and financial checkup.

Competition

We compete primarily with commercial banks, online financial institutions, thrift institutions and credit unions, many of which are substantially larger in terms of assets and available resources. Certain of these institutions have significantly higher lending limits than we do, and may provide various services for their customers that we presently do not. In addition, we experience competition for deposits from mutual funds and security brokers, while consumer discount, mortgage and insurance companies compete for various types of loans. Credit unions, finance companies and mortgage companies enjoy certain competitive advantages over us, as they are not subject to the same regulatory restrictions and taxations as commercial banks. Principal methods of competing for bank products, permitted nonbanking services and financial activities include price, nature of product, quality of service and convenience of location.

In our market area, we expect continued competition from these financial institutions in the foreseeable future. With the continued acceptance of internet banking by our customers and consumers generally, competition for deposits has increased from institutions operating outside of our market area as well as from insurance companies.

We believe that our most significant competitive advantage originates from our business philosophy which includes offering direct access to senior management and other officers and providing friendly, informed and courteous service, local and timely decision making, flexible and reasonable operating procedures and consistently applied credit policies. In addition, our success has been, and will continue to be, a result of our emphasis on community involvement and customer relationships. With consolidation continuing in the financial industry, and particularly in our market area, community banks like us are gaining opportunities and market share as larger institutions reduce their emphasis on or exit our market area.

Seasonality

Generally, our operations are not seasonal in nature.

Supervision and Regulation

We are extensively regulated under federal and state laws. Generally, these laws and regulations are intended to protect consumers, not shareholders. The following is a summary description of certain provisions of law that affect the regulation of bank holding companies and banks. This discussion is qualified in its entirety by reference to applicable laws and regulations. Changes in law and regulation may have a material effect on our business and prospects.

Peoples is a bank holding company within the meaning of the Bank Holding Company Act of 1956, as amended, and is subject to regulation, supervision, and examination by the Board of Governors of the Federal Reserve System, referred to as the “Federal Reserve Board” or the “FRB.” We are required to file annual and quarterly reports with the FRB and to provide the FRB with such additional information as the FRB may require. The FRB also conducts examinations of Peoples.

With certain limited exceptions, we are required to obtain prior approval from the FRB before acquiring direct or indirect ownership or control of more than 5% of any voting securities or substantially all of the assets of a bank or bank holding company, or before merging or consolidating with another bank holding company. Additionally, with certain exceptions, any person or entity proposing to acquire control through direct or indirect ownership of 25% or more of our voting securities is required to give 60 days' written notice of the acquisition to the FRB, which may prohibit the transaction, and to publish notice to the public.

Peoples Bank is regulated by the Pennsylvania Department of Banking and Securities (the "Department of Banking") and the FDIC. The Department of Banking may prohibit an institution over which it has supervisory authority from engaging in activities or investments that the agency believes constitute unsafe or unsound banking practices. Federal banking regulators have extensive enforcement authority over the institutions they regulate to prohibit or correct activities that violate law, regulation or a regulatory agreement or which are deemed to constitute unsafe or unsound practices.

Enforcement actions may include:

- the appointment of a conservator or receiver;
- the issuance of a cease and desist order;
- the termination of deposit insurance, the imposition of civil money penalties on the institution, its directors, officers, employees and institution affiliated parties;
- the issuance of directives to increase capital;
- the issuance of formal and informal agreements and orders;
- the removal of or restrictions on directors, officers, employees and institution-affiliated parties; and
- the enforcement of any such mechanisms through restraining orders or any other court actions.

We are subject to certain restrictions on extensions of credit to executive officers, directors, principal shareholders or any related interests of such persons which generally require that such credit extensions be made on substantially the same terms as are available to third persons dealing with us, and not involving more than the normal risk of repayment. Other laws tie the maximum amount that may be loaned to any one customer and its related interests to our capital levels. Other laws restrict or prohibit transactions between Peoples Bank and its affiliates.

Limitations on Dividends and Other Payments

Our ability to pay dividends is largely dependent upon the receipt of dividends from Peoples Bank. Both federal and state laws impose restrictions on our ability and the ability of Peoples Bank to pay dividends. Under such restrictions, Peoples Bank may only declare and pay dividends out of accumulated net earnings, including accumulated net earnings acquired as a result of a merger within seven years. Further, Peoples Bank may not declare or pay any dividends unless Peoples Bank's surplus would not be reduced by the payment of the dividend below 100% of our capital stock. Pennsylvania law requires that each year Peoples Bank set aside as surplus, a sum equal to not less than 10 percent of its net earnings if surplus does not equal at least 100 percent of our capital stock. In addition to these specific restrictions, bank regulatory agencies, in general, also have the ability to prohibit proposed dividends by a financial institution that would otherwise be permitted under applicable regulations if the regulatory body determines that such distribution would constitute an unsafe or unsound practice.

Permitted Non-Banking Activities

A bank holding company that the FRB has determined to be well capitalized and well managed and that has well capitalized and well managed subsidiary banks may engage in certain nonbanking activities closely related to banking or managing or controlling banks, on a de novo basis, by providing notice to the FRB after commencing the activities. Such a bank holding company proposing to engage in other permissible nonbanking activities either de novo, or through the acquisition of an existing company, must provide prior notice to the FRB. For transactions that do not qualify for the post or expedited prior notice procedures, a bank holding company must file a notice for prior FRB approval.

Subsidiary banks of a bank holding company are subject to certain quantitative and qualitative restrictions on extensions of credit to the bank holding company or its subsidiaries, and on the use of their securities as collateral for loans to any borrower. These regulations and restrictions may limit our ability to obtain funds from Peoples Bank for our cash needs, including funds for the payment of dividends, interest and operating expenses. Further, subject to certain exceptions, a bank holding company and its subsidiaries are prohibited from engaging in certain tie-in arrangements in connection with any extension of credit, lease or sale of property or furnishing of services.

A bank holding company is required to act as a source of financial strength to its subsidiary banks and to make capital injections into a troubled subsidiary bank, and the FRB may charge the bank holding company with engaging in unsafe and unsound practices for failure to commit resources to a subsidiary bank when required. A required capital injection may be called for at a time when the holding company does not have the resources to provide it. In addition, depository institutions insured by the FDIC can be held liable for any losses incurred by, or reasonably anticipated to be incurred by, the FDIC in connection with the default of or assistance provided to, a commonly controlled FDIC-insured depository institution. Accordingly, in the event that any insured subsidiary of a bank holding company causes a loss to the FDIC, other insured subsidiaries of a bank holding company could be required to compensate the FDIC by reimbursing it for the estimated amount of such loss. Such cross guarantee liabilities generally are superior in priority to the obligation of the depository institutions to its shareholders due solely to their status as shareholders and obligations to other affiliates.

Pennsylvania Law

As a Pennsylvania incorporated bank holding company, Peoples is subject to various restrictions on its activities as set forth in Pennsylvania law. This is in addition to those restrictions set forth in federal law. Under Pennsylvania law, a bank holding company that desires to acquire a bank or bank holding company that has its principal place of business in Pennsylvania must obtain permission from the Department of Banking.

Financial Institution Reform, Recovery, and Enforcement Act ("FIRREA")

FIRREA was enacted into law in order to address the financial condition of the Federal Savings and Loan Insurance Corporation, to restructure the regulation of the thrift industry, and to enhance the supervisory and enforcement powers of the federal bank and thrift regulatory agencies. As the primary federal regulator of Peoples Bank, the FDIC, in conjunction with the Department of Banking, is responsible for its supervision. When dealing with capital requirements, those regulatory bodies have the flexibility to impose supervisory agreements on institutions that fail to comply with regulatory requirements. The imposition of a capital plan, termination of deposit insurance, and removal or temporary suspension of an officer, director or other institution-affiliated person may cause enforcement actions.

There are three levels of civil penalties under FIRREA, with the amount of the penalty varying based on the action penalized.

During most of 2020, civil money penalties could range from very low amounts up to the lesser of $2.5 million or 1% of an institution's total assets per violation. These penalties are subject to inflation adjustment procedures prescribed under applicable law. Penalties for continuing violations can be substantially higher.

Federal Deposit Insurance Corporation Improvement Act of 1991 ("FDICIA")

FDICIA provides for, among other things:

- publicly available annual financial condition and management reports for financial institutions, including audits by independent accountants;
- the establishment of uniform accounting standards by federal banking agencies;
- the establishment of a "prompt corrective action" system of regulatory supervision and intervention, based on capitalization levels, with more scrutiny and restrictions placed on depository institutions with lower levels of capital;
- additional grounds for the appointment of a conservator or receiver; and
- restrictions or prohibitions on accepting brokered deposits, except for institutions which significantly exceed minimum capital requirements.

A central feature of FDICIA is the requirement that the federal banking agencies take “prompt corrective action” with respect to depository institutions that do not meet minimum capital requirements. Pursuant to FDICIA, the federal bank regulatory authorities have adopted regulations setting forth a five-tiered system for measuring the capital adequacy of the depository institutions that they supervise. Under these regulations, a depository institution is classified in one of the following capital categories:

- “well capitalized”;
- “adequately capitalized”;
- “under capitalized”;
- “significantly undercapitalized”; and
- “critically undercapitalized”.

Peoples Bank was “well capitalized” based on its actual capital position at December 31, 2020. However, an institution may be deemed by the regulators to be in a capitalization category that is lower than is indicated by its actual capital position if, among other things, it receives an unsatisfactory examination rating with respect to asset quality, management, earnings or liquidity.

FDICIA generally prohibits a depository institution from making any capital distributions including payment of a cash dividend or paying any management fees to its holding company, if the depository institution would thereafter be undercapitalized. Undercapitalized depository institutions are subject to growth limitations and are required to submit capital restoration plans. If a depository fails to submit an acceptable plan, it is treated as if it is “significantly undercapitalized”. Significantly undercapitalized depository institutions may be subject to a number of other requirements and restrictions, including orders to sell sufficient voting stock to become adequately capitalized, requirements to reduce total assets and stop accepting deposits from correspondent banks. Critically undercapitalized institutions are subject to the appointment of a receiver or conservator; generally within 90 days of the date such institution is determined to be critically undercapitalized.

FDICIA provides the federal banking agencies with significantly expanded powers to take enforcement action against institutions that fail to comply with capital or other standards. Such actions may include the termination of deposit insurance by the FDIC or the appointment of a receiver or conservator for the institution. FDICIA also limits the circumstances under which the FDIC is permitted to provide financial assistance to an insured institution before appointment of a conservator or receiver.

Under FDICIA, each federal banking agency is required to prescribe, by regulation, non-capital safety and soundness standards for institutions under its authority. In addition to adopting information security standards, the federal banking agencies, including the FDIC, have adopted standards covering:

- internal controls;
- information systems and internal audit systems;
- loan documentation;
- credit underwriting;
- interest rate exposure;
- asset growth; and
- compensation fees and benefits.

Any institution that fails to meet these standards may be required to develop an acceptable plan, specifying the steps that the institutions will take to meet the standards. Failure to submit or implement such a plan may subject the institution to regulatory sanctions. Peoples believes that it meets substantially all the standards that have been adopted. Before establishing new branch offices, Peoples Bank must meet certain minimum capital stock and surplus requirements and must obtain state approval from the Department of Banking.

Risk-Based Capital Requirements

The federal banking regulators have adopted certain risk-based capital guidelines to assist in assessing capital adequacy of a banking organization's operations for both transactions reported on the balance sheet as assets and transactions, such as letters of credit, and recourse agreements, which are recorded as off-balance sheet items. Under these guidelines, nominal dollar amounts of assets and credit-equivalent amounts of off-balance sheet items are multiplied by one of several risk adjustment percentages, which range from 0% for assets with low credit risk, such as certain U.S. Treasury securities, to 150% for assets with relatively high credit risk, such as business loans.

A banking organization's risk-based capital ratios are obtained by dividing its qualifying capital by its total risk adjusted assets. The regulators measure risk-adjusted assets, which include off-balance-sheet items, against both total qualifying capital, Common Equity Tier 1 capital, and Tier 1 capital.

- "Common Equity Tier 1 Capital" includes common equity and minority interest in equity accounts of consolidated subsidiaries, less goodwill and other intangibles, subject to certain exceptions, and retained earnings.
- "Tier 1", or core capital, includes common equity, non-cumulative preferred stock and minority interest in equity accounts of consolidated subsidiaries, less goodwill and other intangibles, subject to certain exceptions.
- "Tier 2", or supplementary capital, includes, among other things, limited life preferred stock, hybrid capital instruments, mandatory convertible securities, qualifying subordinated debt, and the allowance for loan and lease losses, subject to certain limitations and less restricted deductions. The inclusion of elements of Tier 2 capital is subject to certain other requirements and limitations of the federal banking agencies.

Current rules, which implemented the Basel III regulatory capital reforms and changes required by the Dodd-Frank Act, call for the following capital requirements:

- A minimum ratio of common equity tier 1 capital to risk-weighted assets of 4.5%.
- A minimum ratio of tier 1 capital to risk-weighted assets of 6%.
- A minimum ratio of total capital to risk-weighted assets of 8%.
- A minimum leverage ratio of 4%.

In addition, the current rules provide for a common equity tier 1 capital conservation buffer of 2.5% of risk-weighted assets. If a banking organization fails to hold capital above the minimum capital ratios and the capital conservation buffer, it will be subject to certain restrictions on capital distributions and discretionary bonus payments.

Accumulated other comprehensive income (AOCI) is included in a banking organization's common equity tier 1 capital. The rules, however, allowed community banks to make a one-time election not to include components of AOCI in regulatory capital and instead exclude most AOCI components from regulatory capital. Peoples Bank made that one-time election to "opt-out" of the inclusion of components of AOCI in regulatory capital.

The rules grandfather non-qualifying capital instruments (such as trust preferred securities and cumulative perpetual preferred stock) issued before May 19, 2010 for inclusion in the tier 1 capital of banking organizations with total consolidated assets less than $15 billion as of December 31, 2009 and banking organizations that were mutual holding companies as of May 19, 2010.

Banking organizations may use the existing gross-up approach to assign securitization exposures to a risk weight category or choose to assign such exposures a 1,250 percent risk weight.

Mortgage servicing assets (MSAs) and certain deferred tax assets (DTAs) are subject to stricter limitations than those applicable to other assets under the capital rules.

Failure to meet applicable capital guidelines could subject a banking organization to a variety of enforcement actions including:

- limitations on its ability to pay dividends;

- the issuance by the applicable regulatory authority of a capital directive to increase capital, and in the case of depository institutions, the termination of deposit insurance by the FDIC, as well as to the measures described under FDICIA as applicable to undercapitalized institutions.

In addition, future changes in regulations or practices could further reduce the amount of capital recognized for purposes of capital adequacy. Such a change could affect the ability of Peoples Bank to grow and could restrict the amount of profits, if any, available for the payment of dividends to Peoples.

At December 31, 2020, Peoples met its capital requirements with a ratio of common equity tier 1 capital to risk-weighted assets of 13.73%; its ratio of tier 1 capital to risk-weighted assets of 13.73%; its ratio of total capital to risk-weighted assets of 14.98%; and its leverage ratio of 10.08%.

A qualifying community banking organization (defined to have, among other things, total consolidated assets of less than $10 billion) that has made an election to use the community bank leverage ratio framework will be considered to have met the minimum capital requirements, the capital ratio requirements, and any other capital or leverage requirements to which the qualifying community banking organization would be subject, if it has a leverage ratio of greater than 9 percent.

Interest Rate Risk

Regulatory agencies include, in their evaluations of a bank's capital adequacy, an assessment of the bank's interest rate risk exposure. The standards for measuring the adequacy and effectiveness of a banking organization's interest rate risk management includes a measurement of board of directors and senior management oversight, and a determination of whether a banking organization's procedures for comprehensive risk management are appropriate to the circumstances of the specific banking organization. We utilize interest rate risk models to measure and monitor interest rate risk. In addition, we employ an independent consultant to provide a quarterly assessment of our interest rate risk. Finally, regulatory agencies, as part of the scope of their periodic examinations, evaluate our interest rate risk.

Community Reinvestment Act ("CRA")

The Community Reinvestment Act of 1977 is designed to create a system for bank regulatory agencies to evaluate a depository institution's record in meeting the credit needs of its community. The CRA regulations establish performance-based standards for use in examining for compliance. Peoples Bank had its last CRA compliance examination in 2020 and received a "satisfactory" rating.

USA Patriot Act of 2001

The Patriot Act contains anti-money laundering and financial transparency laws and imposes various regulations, including standards for verifying client identification at account opening, and rules to promote cooperation among financial institutions, regulators and law enforcement entities in identifying parties that may be involved in terrorism or money laundering.

Dodd-Frank Wall Street Reform and Consumer Protection Act (Dodd-Frank)

In 2010, the Dodd-Frank Wall Street Reform and Consumer Protection Act was signed into law. Dodd-Frank is intended to effect a fundamental restructuring of federal banking regulation. Among other things, Dodd-Frank created the Financial Stability Oversight Council to identify systemic risks in the financial system and gives federal regulators authority to take control of and liquidate financial firms. Dodd-Frank additionally created an independent federal regulator to administer federal consumer protection laws. Dodd-Frank has and is expected to continue to have a significant impact on our business operations as its provisions take effect. Among the provisions that affect us are the following:

Holding Company Capital Requirements. Dodd-Frank requires the FRB to apply consolidated capital requirements to bank holding companies that are no less stringent than those currently applied to depository institutions. Dodd-Frank additionally requires that bank regulators issue countercyclical capital requirements so that the required amount of capital increases in times of economic expansion, consistent with safety and soundness.

Deposit Insurance. Dodd-Frank permanently increases the maximum deposit insurance amount for banks, savings institutions and credit unions to $250,000 per depositor. Dodd-Frank also broadens the base for FDIC insurance assessments. Further, Dodd-Frank eliminated the federal statutory prohibition against the payment of interest on business checking accounts. Assessments for institutions such as Peoples Bank (assets of less than $10 billion), are based on initial assessment rates that are adjusted by combining supervisory ratings with financial ratios to determine a total assessment rate. For most institutions, assessment rates are based on weighted-average supervisory ratings of banking operation components and six financial ratios. The financial ratios are: the leverage ratio; loans past due 30-89 days/gross assets; nonperforming assets/gross assets; net loan charge-offs/gross assets; net income before taxes/risk-weighted assets; and the adjusted brokered deposit ratio. In addition, an institution's assessment rate may be lowered if the institution holds long-term unsecured debt and raised if it holds long-term unsecured debt that is issued by another depository institution.

Corporate Governance. Dodd-Frank requires publicly-traded companies to give stockholders a non-binding vote on executive compensation at least every three years, a non-binding vote regarding the frequency of the vote on executive compensation at least every six years, and a non-binding vote on "golden parachute" payments in connection with approvals of mergers and acquisitions unless previously voted on by stockholders. Additionally, Dodd-Frank directs the federal banking regulators to promulgate rules prohibiting excessive compensation paid to executives of depository institutions and their holding companies with assets of $1.0 billion or more, regardless of whether the company is publicly traded. Dodd-Frank also gives the SEC authority to prohibit broker discretionary voting on elections of directors and executive compensation matters.

Limits on Interstate Acquisitions and Mergers. Dodd-Frank precludes a bank holding company from engaging in an interstate acquisition–the acquisition of a bank outside its home state–unless the bank holding company is both well capitalized and well managed. Furthermore, a bank may not engage in an interstate merger with another bank headquartered in another state unless the surviving institution will be well capitalized and well managed.

Limits on Interchange Fees. Dodd-Frank amended the Electronic Fund Transfer Act to, among other things, give the Federal Reserve the authority to establish rules regarding interchange fees charged for electronic debit transactions by payment card issuers having assets of $10 billion or more and to enforce a statutory requirement that such fees be reasonable and proportional to the actual cost of a transaction to the issuer. Issuers with less than $10 billion in assets, like us, are exempt from debit card interchange fee standards.

Consumer Financial Protection Bureau. Dodd-Frank created the Consumer Financial Protection Bureau (CFPB), which is granted broad rulemaking, supervisory and enforcement powers under various federal consumer financial protection laws. The CFPB has examination and primary enforcement authority with respect to depository institutions with $10 billion or more in assets. Smaller institutions are subject to rules promulgated by the CFPB, but continue to be examined and supervised by federal banking regulators for consumer compliance purposes. The CFPB has authority to prevent unfair, deceptive or abusive practices in connection with the offering of consumer financial products. Dodd-Frank authorizes the CFPB to establish certain minimum standards for the origination of residential mortgages including a determination of the borrower's ability to repay. In addition, Dodd-Frank allows borrowers to raise certain defenses to foreclosure if they receive any loan other than a "qualified mortgage" as defined by the CFPB. Dodd-Frank permits states to adopt consumer protection laws and standards that are more stringent than those adopted at the federal level and, in certain circumstances, permits state attorneys general to enforce compliance with both the state and federal laws and regulations.

Ability to Repay and Qualified Mortgage Rule. Mortgage lenders are required to make a reasonable and good faith determination based on verified and documented information that a consumer applying for a mortgage loan has a reasonable ability to repay the loan according to its terms. Mortgage lenders are required to determine consumers' ability to repay in one of two ways. The first alternative requires the mortgage lender to consider, at a minimum, the following eight underwriting factors when making the credit decision:

- current or reasonably expected income or assets;
- current employment status;
- the monthly payment on the covered transaction;
- the monthly payment on any simultaneous loan;
- the monthly payment for mortgage-related obligations;

- current debt obligations, alimony, and child support;
- the monthly debt-to-income ratio or residual income; and
- credit history.

Alternatively, the mortgage lender can originate "qualified mortgages," which are entitled to a presumption that the creditor making the loan satisfied the ability-to-repay requirements. In general, a "qualified mortgage" is a mortgage loan without negative amortization, interest-only payments, balloon payments, or terms exceeding 30 years. In addition, to be a qualified mortgage, the points and fees paid by a consumer cannot exceed 3% of the total loan amount. Loans which meet these criteria will be considered qualified mortgages, and as a result generally protect lenders from fines or litigation in the event of foreclosure. Qualified mortgages that are "higher-priced" (e.g. subprime loans) garner a rebuttable presumption of compliance with the ability-to-repay rules, while qualified mortgages that are not "higher-priced" (e.g. prime loans) are given a safe harbor of compliance.

Future Legislation

Proposed legislation is introduced in almost every legislative session that would dramatically affect the regulation of the banking industry. We cannot predict if any such legislation will be adopted nor if adopted how it would affect our business. Past history has demonstrated that new legislation or change to existing laws or regulations usually results in greater compliance burden and therefore generally increases the cost of doing business.

Availability of Securities Filings

We maintain an Internet website at www.psbt.com. We make available free of charge through the "Investor Relations" link on our Internet website, our annual report on Form 10-K, quarterly reports on Form 10-Q, current reports on Form 8-K, and amendments to those reports filed or furnished pursuant to Section 13(a) or 15(d) of the Exchange Act as soon as reasonably practicable after we electronically file such material with, or furnish it to, the SEC.

Item 1A. Risk Factors.

In addition to the other information set forth in this report, one should carefully consider the factors discussed below, which could materially affect our business, financial condition or future results. The risks described below are not the only risks that we face. Additional risks and uncertainties not currently known to us or that we currently deem to be insignificant also may materially adversely affect our business, financial condition and/or operating results.

Risks Relating to Peoples and Its Business

The outbreak of the coronavirus ("COVID-19"), or an outbreak of another highly infectious or contagious disease, could adversely affect our business activities, financial condition and results of operations.

Our business is dependent upon the willingness and ability of our customers to conduct banking and other financial transactions. The spread of a highly infectious or contagious disease, such as COVID-19, could cause severe disruptions in the U.S. economy, which could in turn disrupt the business, activities, and operations of our customers, as well as our business and operations. Moreover, since the beginning of January 2020, the coronavirus outbreak has caused significant disruption in the financial markets both globally and in the United States. The spread of COVID-19, or an outbreak of another highly infectious or contagious disease, may result in a significant decrease in business and/or cause our customers to be unable to meet existing payment or other obligations to us, particularly in the event of a spread of COVID-19 or an outbreak of an infectious disease in our market area. Although we maintain contingency plans for pandemic outbreaks, a spread of COVID-19, or an outbreak of another contagious disease, could also negatively impact the availability of key personnel necessary to conduct our business activities. Such a spread or outbreak could also negatively impact the business and operations of third-party service providers who perform critical services for us. If COVID-19, or another highly infectious or contagious disease, spreads or the response to contain COVID-19 is unsuccessful, we could experience a material adverse effect to our business, financial condition, and results of operations.

The extent of the impact of the COVID-19 pandemic on our capital, liquidity, and other financial positions and on our business, results of operations, and prospects will depend on a number of evolving factors, including:

The duration, extent, and severity of the pandemic. COVID-19 has not been contained and could affect significantly more households and businesses. The uncertain duration and severity of the pandemic continues.

The response of governmental authorities. Many of the actions taken by the national and state governmental authorities have been directed at curtailing personal and business activity to contain COVID-19 while simultaneously deploying fiscal-and monetary-policy measures to assist in mitigating the adverse effects on individuals and businesses. These actions are not consistent across jurisdictions but, in general, have been rapidly expanding in scope and intensity.

The effect on our customers, counterparties, employees, and third-party service providers. COVID-19 and its associated consequences and uncertainties may affect individuals, households, and businesses differently and unevenly. Our credit, operational, and other risks are generally expected to increase.

The effect on economies and markets. Whether the actions of governmental authorities will be successful in mitigating the adverse effects of COVID-19 is unclear. National, regional, and local economies and markets could suffer lasting disruptions.

The success of relief efforts to bridge the gap to reopening the economy. The U.S. government has implemented programs to directly compensate individuals and grant or loan money to businesses in an effort to provide funding while the economy is shut down. Many banks, including Peoples, have implemented hardship relief programs that include payment deferral options. The success of these programs could mute the effect on the Company's credit losses, which may be difficult to determine.

The duration of these business interruptions and related impacts on our business and operations, which will depend on future developments, are highly uncertain and cannot be reasonably estimated at this time. The pandemic could cause us to experience higher credit losses in our lending portfolio, impairment of our goodwill and other financial assets, reduced demand for our products and services, and other negative impacts on our financial position, results of operations, and prospects.

We are subject to credit risk in connection with our lending activities, and our financial condition and results of operations may be negatively impacted by economic conditions and other factors that adversely affect our borrowers.

Lending money is a significant part of the banking business and interest income on our loan portfolio is the principal component of our revenue. Our financial condition and results of operations are affected by the ability of our borrowers to repay their loans, and in a timely manner. Borrowers, however, do not always repay their loans. The risk of non-payment is assessed through our underwriting and loan review procedures based on several factors including credit risks of a particular borrower, changes in economic conditions, the duration of the loan and in the case of a collateralized loan, uncertainties as to the future value of the collateral and other factors. Despite our efforts, we do and will experience loan and lease losses, and our financial condition and results of operations will be adversely affected. Our loans which were between 30 and 89 days delinquent on December 31, 2020 totaled $3.5 million. Our non-performing assets were approximately $10.5 million on December 31, 2020. Our allowance for loan and lease losses was approximately $27.3 million on December 31, 2020.

Our emphasis on the Eastern Pennsylvania and the Southern Tier of New York market area exposes us to a risk of loss associated with the region.

At December 31, 2020, $277.4 million or 12.7%, of our loan portfolio consisted of residential mortgage loans and $1.1 billion or 52.3%, of our loan portfolio consisted of commercial real estate loans. A majority of these loans are made to borrowers or secured by properties located in Eastern Pennsylvania and the southern tier of New York. Deterioration in economic conditions in this market area, particularly in the industries on which this geographic area depend, or a general decline in economic conditions may adversely affect the quality of our loan portfolio (including the level of non-performing assets, charge offs and provision for loan losses) and demand for our products and services, and, accordingly, our results of operations. Future declines in real estate values in the region could also cause some of our mortgage and commercial real estate loans to be inadequately collateralized, which would expose us to a greater risk of loss if we seek to recover on defaulted loans by selling the real estate collateral.

We make commercial and industrial, construction, and commercial real estate loans, which present greater risks than other types of loans.

As of December 31, 2020, approximately 83.4% of our loan portfolio consisted of commercial and industrial, construction, and commercial real estate loans. These types of loans are generally viewed as having more risk of default than residential real estate loans or consumer loans. These types of loans are also typically larger than residential real estate loans and consumer loans. Because our loan portfolio contains a significant number of commercial and industrial, construction, and commercial real estate loans some of which have large balances, the deterioration of one or a few of these loans could cause a significant increase in non-performing loans. An increase in non-performing loans could result in a net loss of earnings from these loans, an increase in the provision for loan losses, and an increase in loan charge-offs, all of which could have a material adverse effect on our financial condition and results of operations.

The commercial real estate market is cyclical and poses risks of loss to us because of the concentration of commercial real estate loans in our loan portfolio, and the lack of diversity in risk associated with such a concentration. Banking regulators have been giving and continue to give commercial real estate lending greater scrutiny, and banks with larger commercial real estate loan portfolios are expected by their regulators to implement improved underwriting, internal controls, risk management policies and portfolio stress-testing practices to manage risks associated with commercial real estate lending. Additional losses or regulatory requirements related to our commercial real estate loan concentration could materially adversely affect our business, financial condition and results of operations.

Our allowance for loan losses may not be adequate to absorb actual loan losses, and we may be required to make further provisions for loan losses and charge off additional loans in the future, which could materially and adversely affect our business.

We attempt to maintain an allowance for loan losses, established through a provision for loan losses accounted for as an expense, which is adequate to absorb losses inherent in our loan portfolio. If our allowance for loan losses is inadequate, it may have a material adverse effect on our financial condition and results of operations.

The determination of the allowance for loan losses involves a high degree of subjectivity and judgment and requires us to make significant estimates of current credit risks and future trends, all of which may undergo material changes. Changes in economic conditions affecting borrowers, new information regarding existing loans, identification of additional problem loans and other factors, both within and outside of our control, may require us to increase our allowance for loan losses. Increases in non-performing loans have a significant impact on our allowance for loan losses. Our allowance for loan losses may not be adequate to absorb actual loan losses. If conditions in our regional real estate markets decline, we could experience increased delinquencies and credit losses, particularly with respect to real estate construction and land acquisition and development loans and one-to-four family residential mortgage loans. Moreover, if the economy slows, the negative impact to our market areas could result in higher delinquencies and credit losses. As a result, we will continue to make provisions for loan losses and to charge off additional loans in the future, which could materially adversely affect our financial conditions and results of operations.

In addition to our internal processes for determining loss allowances, bank regulatory agencies periodically review our allowance for loan losses and may require us to increase the provision for loan losses, to recognize further loan charge-offs, or to take other actions, based on judgments that differ from those of our management. If loan charge-offs in future periods exceed the allowance for loan losses, we will need to increase our allowance for loan losses. Furthermore, growth in our loan portfolio would generally lead to an increase in the provision for loan losses. Provisions for loan losses will result in a decrease in net income and capital, and may have a material adverse effect on our financial condition, and results of operations and cash flows.

Changes in interest rates could adversely impact our financial condition and results of operations.

Our ability to generate net income substantially depends upon our net interest income, which is the difference between the interest income earned on interest-earning assets, such as loans and investment securities, and the interest expense paid on interest-bearing liabilities, such as deposits and borrowings. Certain assets and liabilities react differently to changes in market interest rates. Further, interest rates on some types of assets and liabilities may fluctuate prior to changes in broader market interest rates, while rates on other types of assets may lag behind. Additionally, some assets such as adjustable-rate mortgages have features, and rate caps, which restrict changes in their interest rates.

Factors such as monetary policy, inflation, recession, unemployment, money supply, global disorder, terrorist activity, instability in domestic and foreign financial markets, global pandemic, and other factors beyond our control, may affect interest rates. Changes in market interest rates will also affect the level of voluntary prepayments on loans and the receipt of payments on mortgage-backed securities, resulting in the receipt of proceeds that may have to be reinvested at a lower rate than the loan or mortgage-backed security being prepaid. Although we pursue an asset-liability management strategy designed to manage our risk from changes in market interest rates, changes in interest rates can still have a material adverse effect on our profitability.

The Company may be required to transition from the use of the LIBOR interest rate index in the future.

The Company has certain loans and derivative instruments whose interest rate is indexed to the London InterBank Offered Rate (LIBOR). The United Kingdom's Financial Conduct Authority, which is responsible for regulating LIBOR, has announced that the publication of one week and two month U.S. dollar (USD) LIBOR settings is not guaranteed beyond December 31, 2021 and the remaining USD LIBOR settings beyond June 30, 2023. At this time, no consensus exists as to what reference rate or rates or benchmarks may become acceptable alternatives to LIBOR, although the Alternative Reference Rates Committee (a group of private-market participants convened by the Federal Reserve Board and the Federal Reserve Bank of New York) has identified the Secured Overnight Financing Rate, or SOFR, as the recommend alternative to LIBOR. Uncertainty as to the adoption, market acceptance or availability of SOFR or other alternative reference rates may adversely affect the value of LIBOR-based loans in the Company's portfolio and may impact the availability and cost of hedging instruments and borrowings. The language in the Company's LIBOR-based contracts and financial instruments has developed over time and may have various events that trigger when a successor index to LIBOR would be selected. If a trigger is satisfied, contracts and financial instruments may give the Company or the calculation agent, as applicable, discretion over the selection of the substitute index for the calculation of interest rates. The implementation of a substitute index for the calculation of interest rates under the Company's loan agreements may result in the Company incurring significant expenses in effecting the transition and may result in disputes or litigation with customers over the appropriateness or comparability to LIBOR of the substitute index, any of which could have an adverse effect on the Company's results of operations.

Changes in interest rates could affect our investment values and impact comprehensive income and stockholders' equity.

At December 31, 2020, we had approximately $295.9 million of securities available-for-sale. These securities are carried at fair value on our consolidated balance sheets. Unrealized gains or losses on these securities, that is, the difference between the fair value and the amortized cost of these securities, are reflected in stockholders' equity, net of deferred taxes. As of December 31, 2020, our available-for-sale securities had an unrealized gain, net of taxes, of $7.7 million. The fair value of our available-for-sale securities is subject to interest rate change, which would not affect recorded earnings, but would increase or decrease comprehensive income and stockholders' equity.

Our results of operations may be materially and adversely affected by other-than-temporary impairment charges relating to our investment portfolio.

Numerous factors, including the lack of liquidity for re-sales of certain investment securities, the absence of reliable pricing information for investment securities, adverse changes in the business climate, adverse regulatory actions or unanticipated changes in the competitive environment, could have a negative effect on our investment portfolio in future periods. Investments are evaluated periodically to determine whether a decline in their value is other than temporary.

Management utilizes criteria such as the magnitude and duration of the decline, in addition to the reasons underlying the decline, to determine whether the loss in value is other than temporary. The term “other than temporary” indicates that the prospects for a near term recovery of value are not necessarily favorable, or that there is a lack of evidence to support fair values equal to, or greater than, the carrying value of the investment.

Once a decline in value is determined to be other than temporary, the value of the security is reduced and a corresponding charge to earnings is recognized. If an impairment charge is significant enough, it could affect our ability to pay dividends, which could materially adversely affect us and our ability to pay dividends to shareholders. Significant impairment charges could also negatively impact our regulatory capital ratios and result in us not being classified as “well-capitalized” for regulatory purposes.

The requirement to record certain assets and liabilities at fair value may adversely affect our financial results.

We report certain assets, including available-for-sale investment securities, at fair value. Generally, for assets that are reported at fair value we use quoted market prices or valuation models that utilize market data inputs to estimate fair value. Because we record these assets at their estimated fair value, we may incur losses even if the asset in question presents minimal credit risk. The level of interest rates can impact the estimated fair value of investment securities. Disruptions in the capital markets may require us to recognize other-than-temporary impairments in future periods with respect to investment securities in our portfolio. The amount and timing of any impairment recognized will depend on the severity and duration of the decline in fair value of our investment securities and our estimation of the anticipated recovery period.

Changes in the value of goodwill and intangible assets could reduce our earnings.

We account for goodwill and other intangible assets in accordance with accounting principles generally accepted in the United States of America (“GAAP”), which, in general, requires that goodwill not be amortized, but rather that it be tested for impairment at least annually at the reporting unit level using the two step approach. Testing for impairment of goodwill and intangible assets is performed annually and involves the identification of reporting units and the estimation of fair values. The estimation of fair values involves a high degree of judgment and subjectivity in the assumptions used. At December 31, 2020, we completed a qualitative goodwill impairment test to determine if it is more likely than not (that is, a likelihood of more than 50%) that the fair value of the Company is less than its carrying value, including goodwill, as described by the GAAP methodology. Based on this analysis, we concluded it is more likely than not that the fair value of the Company, as of December 31, 2020, is higher than its carrying value, and, therefore, goodwill is not considered impaired and no further testing is required. Changes in the local and national economy, the federal and state legislative and regulatory environments for financial institutions, the stock market, interest rates and other external factors (such as global pandemics or natural disasters) may occur from time to time, often with great unpredictability, and may materially impact the fair value of publicly traded financial institutions and could result in an impairment charge at a future date.

Changes in U.S. or regional economic conditions could have an adverse effect on the Company’s business, financial condition and results of operations.

The Company’s business activities and earnings are affected by general business conditions in the United States and in the Company’s local market area. These conditions include short-term and long-term interest rates, inflation, unemployment levels, consumer confidence and spending, fluctuations in both debt and equity capital markets, and the strength of the economy in the United States generally and, in particular, the Company’s market area. A favorable business environment is generally characterized by, among other factors, economic growth, efficient capital markets, low inflation, low unemployment, high business and investor confidence, and strong business earnings. Unfavorable or uncertain economic and market conditions can be caused by declines in economic growth, business activity or investor or business confidence; limitations on the availability or increases in the cost of credit and capital; increases in inflation or interest rates; high unemployment; global pandemics, natural disasters; or a combination of these or other factors. Economic pressure on consumers and uncertainty regarding continuing economic improvement may result in changes in consumer and business spending, borrowing and savings habits. Elevated levels of unemployment, declines in the values of real estate, extended federal government shutdowns, or other events that affect household and/or corporate incomes could impair the ability of the Company's borrowers to repay their loans in accordance with their terms and reduce demand for banking products and services.

Strong competition within our market area may limit our growth and profitability.

Competition in the banking and financial services industry is intense. We compete actively with other Pennsylvania and southern New York financial institutions, many larger than us, as well as with financial and non-financial institutions headquartered elsewhere. Commercial banks, savings banks, savings and loan associations, credit unions, and money market funds actively compete for deposits and loans. Such institutions, as well as consumer finance, insurance companies and brokerage firms, may be considered competitors with respect to one or more services they render. Many of the institutions with which we compete have substantially greater resources and lending limits and may offer certain services that we do not or cannot provide. Our profitability depends upon our ability to successfully compete in our market area.

Increased needs for disbursement of funds on loans and deposits can affect our liquidity.

We manage our liquidity with an objective of maintaining a balance between sources and uses of funds in such a way that the cash requirements of customers for loans and deposit withdrawals are met in the most economical manner. If we do not properly manage our liquidity, our business, financial condition, results of operations and cash flows may be materially and adversely affected.

Our future pension plan costs and contributions could be unfavorably impacted by the factors that are used in the actuarial calculations.

We maintain a non-contributory defined benefit pension plan, which was frozen in 2008. The costs for this legacy pension plan are dependent upon a number of factors, such as the rates of return on plan assets, discount rates, the level of interest rates used to measure the required minimum funding levels of the plans, future government regulation and required or voluntary contributions made to the plans. Without sustained growth in the pension investments over time to increase the value of our plan assets and depending upon the other factors impacting net income as listed above, we could be required to fund the plan with higher amounts of cash than are anticipated by our actuaries. Such increased funding obligations could have a material impact on our liquidity by reducing our cash flows.

Our holding company is dependent for liquidity on payments from Peoples Bank, which payments are subject to restrictions.

We depend on dividends, distributions and other payments from Peoples Bank to fund dividend payments to our shareholders, if any, and to fund all payments on obligations of our holding company. Peoples Bank is subject to laws that restrict dividend payments or authorize regulatory bodies to block or reduce the flow of funds from Peoples Bank to us. Restrictions or regulatory actions of that kind could impede our access to funds that we may need to make payments on our obligations or dividend payments, if any. In addition, our right to participate in a distribution of assets upon a subsidiary's liquidation or reorganization is subject to the prior claims of the subsidiary's creditors. Holders of our common stock are entitled to receive dividends if and when declared from time to time by our board of directors in its sole discretion out of funds legally available for that purpose.

We need to continually attract and retain qualified personnel for our operations.

Our ability to provide high-quality customer service and to operate efficiently and profitably is dependent on our ability to attract and retain qualified individuals for key positions within the organization. We rely heavily on our executive officers and employees. The loss of certain executive officers or employees could have an adverse effect on us because, as a community bank, the executive officers and employees typically have more responsibility than would be typical at a larger financial institution with more employees. In addition, due to our size as a community bank, we have fewer management-level and other personnel who are in position to succeed to and assume the responsibilities of certain existing executive officers and employees. If we expand geographically or expand to provide non-banking services, current management may not have the necessary experience for successful operation in these new areas. There is no guarantee that management would be able to meet these new challenges or that we would be able to retain new officers or personnel with the appropriate background and expertise.

Our financial performance may suffer if our information technology is unable to keep pace with growth or industry developments.

Effective and competitive delivery of our products and services is increasingly dependent upon information technology resources and processes, both those provided internally as well as those provided through third party vendors. In addition to better serving customers, the effective use of technology increases efficiency and enables us to reduce costs. Our future success will depend, in part, upon our ability to address the needs of our customers by using technology to provide products and services to enhance customer convenience, as well as to create additional efficiencies in our operations. Many of our competitors have greater resources to invest in technological improvements. Additionally, as technology in the financial services industry changes and evolves, keeping pace becomes increasingly complex and expensive for us. There can be no assurance that we will be able to effectively implement new technology-driven products and services, which could reduce our ability to compete effectively.

A failure in or a breach of our information systems or infrastructure, including as a result of cyber-attacks, could disrupt our business, damage our reputation, and could have a material adverse effect on our business, financial condition and results of operations.

In the ordinary course of our business activities, including the ongoing maintenance of deposits, loan and other account relationships for our customers, receiving instructions and effecting transactions for those customers and other users of our products and services, we regularly collect, process, transmit and store significant amounts of confidential information regarding our customers, employees and others. In addition to confidential information regarding our customers, employees and others, we, and in some cases a third party, compile, process, transmit and store proprietary, non-public information concerning our business, operations, plans and strategies.

Information security risks have significantly increased in recent years in part because of the proliferation of new technologies, the use of the Internet and telecommunications technologies to conduct financial transactions, and the increased sophistication and activities of organized crime, hackers, terrorists and other external parties. We rely on digital technologies, computer and email systems, software, and networks to conduct secure processing, transmission and storage of confidential information. In addition, to access our products and services, our customers may use personal smart phones, tablet PCs and other mobile devices that are beyond our control systems. Our technologies, systems, networks and our customers' 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 use, loss or destruction of our or our customers' or third parties' confidential information, or otherwise disrupt our or our customers' or other third parties' business operations.

In addition to cyber-attacks or other security breaches involving the theft of sensitive and confidential information, hackers have engaged in attacks against large financial institutions, particularly denial of service attacks, that are designed to disrupt key business services, such as customer-facing web sites. We are not able to anticipate or implement effective preventive measures against all security breaches of these types, especially because the techniques used change frequently and because attacks can originate from a wide variety of sources.

Although we use a variety of physical, procedural and technological safeguards to protect confidential information from mishandling, misuse or loss, these safeguards cannot provide assurance that mishandling, misuse or loss of the information will not occur, and that if mishandling, misuse or loss of the information did occur, those events will be promptly detected and addressed. A failure in or breach of our operational or information security systems, or those of a third-party service provider, as a result of cyber-attacks or information security breaches or otherwise could have a material adverse effect on our business, damage our reputation, increase our costs and/or cause significant losses. As information security risks and cyber threats continue to evolve, we may be required to expend substantial resources to further enhance our information security measures and/or to investigate and remediate any information security vulnerabilities.

If information security is breached, despite the controls we and our third-party vendors have instituted, information can be lost or misappropriated, resulting in financial loss or costs to us or damages to others. These costs or losses could materially exceed the amount of insurance coverage, if any, which would adversely affect our earnings. In addition, our reputation could be damaged which could result in loss of customers, greater difficulty in attracting new customers, or an adverse effect on the value of our common stock.

Our disclosure controls and procedures and our internal control over financial reporting may not achieve their intended objectives.

We maintain disclosure controls and procedures designed to ensure that we timely report information as specified in the rules and forms of the Securities and Exchange Commission ("SEC"). We also maintain a system of internal control over financial reporting. These controls may not achieve their intended objectives. Control processes that involve human diligence and compliance, such as our disclosure controls and procedures and internal control over financial reporting, are subject to lapses in judgment and breakdowns resulting from human failures. Controls can also be circumvented by collusion or improper management override. Because of such limitations, there are risks that material misstatements due to error or fraud may not be prevented or detected and that information may not be reported on a timely basis. If our controls are not effective, it could have a material adverse effect on our financial condition, results of operations, and market for our common stock, and could subject us to regulatory scrutiny.

We are exposed to environmental liabilities with respect to real estate.

We currently operate 26 branch offices, and own additional real estate. In addition, a significant portion of our loan portfolio is secured by real property. In the course of our business, we may foreclose, accept deeds in lieu of foreclosure, or otherwise acquire real estate, and in doing so could become subject to environmental liabilities with respect to these properties. We may become responsible to a governmental agency or third parties for property damage, personal injury, investigation and clean-up costs incurred by those parties in connection with environmental contamination, or may be required to investigate or clean-up hazardous or toxic substances, or chemical releases at a property. The costs associated with environmental investigation or remediation activities could be substantial. In addition, as the owner or former owner of a contaminated site, we may be subject to common law claims by third parties based on damages and costs resulting from environmental contamination emanating from the property. Although we have policies and procedures to perform an environmental review before acquiring title to any real property, these may not be sufficient to detect all potential environmental hazards. If we were to become subject to significant environmental liabilities, it could materially and adversely affect us.

The soundness of other financial services institutions may adversely affect our credit risk.

We rely on other financial services institutions through trading, clearing, counterparty, and other relationships. We maintain limits and monitor concentration levels of our counterparties as specified in our internal policies. Our reliance on other financial services institutions exposes us to credit risk in the event of default by these institutions or counterparties. These losses could adversely affect our results of operations and financial condition.

Our operations could be interrupted if certain external vendors on which we rely experience difficulty, terminate their services or fail to comply with applicable laws and regulations.

We depend to a significant extent on relationships with third party service providers. Specifically, we utilize third party core banking services and receive credit card and debit card services, branch capture services, Internet banking services and services complementary to our banking products from various third party service providers. If these third party service providers experience difficulties or terminate their services and we are unable to replace them with other service providers, our operations could be interrupted. It may be difficult for us to replace some of our third party vendors, particularly vendors providing our core banking, credit card and debit card services, in a timely manner if they were unwilling or unable to provide us with these services in the future for any reason. If an interruption were to continue for a significant period of time, it could have a material adverse effect on our business, financial condition or results of operations. Even if we are able to replace them, it may be at higher cost to us, which could have a material adverse effect on our business, financial condition or results of operations. In addition, if a third party provider fails to provide the services we require, fails to meet contractual requirements, such as compliance with applicable laws and regulations, or suffers a cyber-attack or other security breach, our business could suffer economic and reputational harm that could have a material adverse effect on our business, financial condition or results of operations.

Our use of third party vendors and our other ongoing third party business relationships are subject to regulatory requirements and attention.

We regularly use third party vendors as part of our business. We also have substantial ongoing business relationships with other third parties. These types of third party relationships are subject to demanding regulatory requirements and attention by our bank regulators. Banking regulations requires us to perform due diligence, ongoing monitoring and maintain control over our third party vendors and other ongoing third party business relationships. We expect that our regulators will hold us responsible for deficiencies in our oversight and control of our third party relationships and in the performance of the parties with which we have these relationships. As a result, if our regulators conclude that we have not exercised adequate oversight and control over our third party vendors or other ongoing third party business relationships or that such third parties have not performed appropriately, we could be subject to enforcement actions, including civil money penalties or other administrative or judicial penalties or fines as well as requirements for customer remediation, any of which could have a material adverse effect on our business, financial condition or results of operations.

Risks Related to Our Common Stock

Our ability to pay dividends or repurchase shares is subject to limitations.

Our ability to pay dividends on or repurchase shares of our stock depends upon our receipt of dividends from Peoples Bank. Additionally, our ability to pay dividends is limited by Pennsylvania corporate law and by federal banking regulations. Under Pennsylvania law, we may not pay a dividend if, after payment, we could not pay our debts as they become due in the usual course of business or our total assets would be less than our total liabilities. The Federal Reserve Board has issued a policy statement on the payment of cash dividends by bank holding companies, which expresses the Federal Reserve Board's view that a bank holding company should pay cash dividends only to the extent that the company's net income for the past year is sufficient to cover both the cash dividends and a rate of earnings retention that is consistent with the company's capital needs, asset quality and overall financial condition.

As a state-chartered bank, Peoples Bank is subject to regulatory restrictions on the payment and amounts of dividends under the Pennsylvania Banking Code. Further, Peoples Bank's ability to pay dividends is also subject to its profitability, financial condition, capital expenditures and other cash flow requirements. There is no assurance that Peoples Bank will be able to pay dividends. Our failure to pay dividends could have a material adverse effect on the market price of our common stock.

Proxy contests and shareholder litigation may adversely affect our results of operations.

Proxy contests or shareholder litigation could cause us to use resources, both in expense and in the time and attention of our management, which could otherwise be used in operating our business. Accordingly, our results of operations may be adversely effected.

Risks Related to Potential Future Transactions

Future acquisitions by us could dilute existing shareholders' ownership of Peoples and may cause us to become more susceptible to adverse economic events.

We may issue shares of our common stock in connection with future acquisitions and other investments, which would dilute existing shareholders' ownership interests in Peoples. While there is no assurance that these transactions will occur, or that they will occur on terms favorable to us, future business acquisitions could be material to us, and the degree of success achieved in acquiring and integrating these businesses could have a material effect on the value of our common stock. In addition, these acquisitions could require us to expend substantial cash or other liquid assets or to incur debt, which could cause us to become more susceptible to economic downturns and competitive pressures.

Our governing documents, Pennsylvania law, and current policies of our board of directors contain provisions which may reduce the likelihood of a change in control transaction that may otherwise be available and attractive to shareholders.

Our articles of incorporation and bylaws contain certain anti-takeover provisions that may make it more difficult or expensive or may discourage a tender offer, change in control or takeover attempt that is opposed by our board of directors. In particular, the articles of incorporation and bylaws: classify our board of directors into three groups, so that shareholders elect only approximately one-third of the board each year; require our shareholders to give us advance notice to nominate candidates for election to the board of directors or to make shareholder proposals at a shareholders' meeting; and require the affirmative vote of the holders of at least 75% of our common stock to approve amendments to our bylaws or to approve certain business combinations that have not received the support of two-thirds of our board of directors. These provisions of our articles of incorporation and bylaws could discourage potential acquisition proposals and could delay or prevent a change in control, even though a majority of our shareholders may consider such proposals desirable. Such provisions could also make it more difficult for third parties to remove and replace the members of our board of directors. Moreover, these provisions could diminish the opportunities for shareholders to participate in certain tender offers, including tender offers at prices above the then-current market value of our common stock, and may also inhibit increases in the trading price of our common stock that could result from takeover attempts or speculation.

In addition, anti-takeover provisions in Pennsylvania law could make it more difficult for a third party to acquire control of us. These provisions could adversely affect the market price of our common stock and could reduce the amount that shareholders might receive if we are sold. For example, Pennsylvania law may restrict a third party's ability to obtain control of Peoples and may prevent shareholders from receiving a premium for their shares of our common stock. Pennsylvania law also provides that our shareholders are not entitled by statute to propose amendments to our articles of incorporation.

Our ability to make opportunistic acquisitions is subject to significant risks, including the risk that regulators will not provide the requisite approvals.

We may make opportunistic whole or partial acquisitions of other banks, branches, financial institutions, or related businesses from time to time that we expect may further our business strategy. Any possible acquisition will be subject to regulatory approval, and there can be no assurance that we will be able to obtain such approval in a timely manner or at all. Even if we obtain regulatory approval, these acquisitions could involve numerous risks, including lower than expected performance or higher than expected costs, difficulties related to integration, diversion of management's attention from other business activities, changes in relationships with customers, and the potential loss of key employees. In addition, we may not be successful in identifying acquisition candidates, integrating acquired institutions, or preventing deposit erosion or loan quality deterioration at acquired institutions. Competition for acquisitions can be highly competitive, and we may not be able to acquire other institutions on attractive terms. There can be no assurance that we will be successful in completing or will even pursue future acquisitions, or if such transactions are completed, that we will be successful in integrating acquired businesses into operations. Our ability to grow may be limited if we choose not to pursue or are unable to successfully make acquisitions in the future.

Risks Related to Government Regulation

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

We are subject to extensive regulation, supervision and examination by certain state and federal agencies including the FDIC, the Board of Governors of the Federal Reserve System and the Pennsylvania Department of Banking. Such regulation and supervision govern the activities in which we may engage and are intended primarily to ensure the safety and soundness of financial institutions. Regulatory authorities have extensive discretion in their supervisory and enforcement activities, including the imposition of restrictions on operations, the classification of assets and determination of the level of the 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 us and our operations. There also are several federal and state statutes which regulate the obligation and liabilities of financial institutions pertaining to environmental issues. In addition to the potential for attachment of liability resulting from our own actions, we may be held liable under certain circumstances for the actions of our borrowers, or third parties, when such actions result in environmental problems on properties that collateralize loans held by us. Further, the liability has the potential to far exceed the original amount of a loan.

We may be subject to more stringent capital and liquidity requirements in the future, which may adversely affect our net income and future growth.

Future increases, if any, in minimum capital requirements could adversely affect our net income. Furthermore, our failure to comply with the minimum capital requirements could result in our regulators taking formal or informal actions against us which could restrict our future growth or operations.

The regulations issued by the Consumer Financial Protection Bureau have increased and may continue to increase our costs of operations.

The Consumer Financial Protection Bureau has broad powers to supervise and enforce consumer protection laws and broad rule-making authority for a wide range of consumer protection laws that apply to all banks and savings institutions, including the authority to prohibit “unfair, deceptive or abusive” acts and practices. The Consumer Financial Protection Bureau considers whether additional rules are needed and has direct examination and enforcement authority over all banks and savings institutions with more than $10 billion in assets. Banks with $10 billion or less in assets, like us, are examined for compliance with these consumer laws by their primary bank regulators. The Dodd-Frank Act permits states to adopt consumer protection laws and standards that are more stringent than those adopted at the federal level and, in certain circumstances, permits state attorneys general to enforce compliance with both the state and federal laws and regulations.

Increases in FDIC insurance premiums may adversely affect our earnings.

Our deposits are insured by the FDIC up to legal limits and, accordingly, we are subject to FDIC deposit insurance assessments. Should our supervisory rating be lowered or our unsecured debt increase, we may be required to pay an increased assessment. More generally, should the designated reserve ratio of the FDIC Deposit Insurance Fund be raised or the fund suffer losses, we may be required to pay an increased assessment. An increase in the assessment we pay may adversely impact our earnings.

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 that 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, increased insurance cost and damage to our reputation, which could have a material adverse effect on our business, financial condition or results of operations.

Item 1B. Unresolved Staff Comments.

None.

Item 2. Properties.

Our corporate headquarters is located at 150 N. Washington Avenue, Scranton, Pennsylvania, which houses our finance and planning, trust, commercial lending, human resources and investor services divisions, as well as our executive offices. Our operations division is located at 82 Franklin Avenue, Hallstead, Pennsylvania.

We operate 26 full-service community banking offices located within the Lackawanna, Lebanon, Lehigh, Luzerne, Monroe, Montgomery, Northampton, Susquehanna and Wyoming Counties of Pennsylvania and Broome County of New York. Seven offices are leased and the balance are owned by Peoples Bank.

We lease several remote ATM locations throughout our market area. All branches and ATM locations are equipped with closed circuit television monitoring.

We consider our properties to be suitable and adequate for our current and immediate future purposes.

Item 3. Legal Proceedings.

There are no material pending legal proceedings, other than ordinary routine litigation incidental to our business, as to which we are a party or of which any of our property is subject.

Item 4. Mine Safety Disclosures.

Not applicable.

Part II

Item 5. Market for Registrant's Common Equity, Related Stockholder Matters and Issuer Purchases of Equity Securities.

As of February 28, 2021 there were approximately 3,794 holders of our common stock, $2.00 par value, including individual participants in security position listings. Our common stock trades on The Nasdaq Stock Market under the symbol "PFIS."

Peoples has paid cash dividends since its incorporation in 1986. It is the present intention of the Board of Directors to continue to pay quarterly cash dividends, however, the payment of future dividends must necessarily depend upon earnings, financial position, appropriate restrictions under applicable laws and other factors relevant at the time our board of directors considers any declaration of dividends. The Board declared on January 29, 2021 a first quarter dividend of $0.37 per share payable March 15, 2021. For information on dividend restrictions on the Company and Peoples Bank, refer to Part I, Item 1 "Supervision and Regulation – Limitations on Dividends and Other Payments" to this report and refer to the consolidated financial statements and notes to these statements filed at Item 8 to this report and incorporated in their entirety by reference under this Item 5.

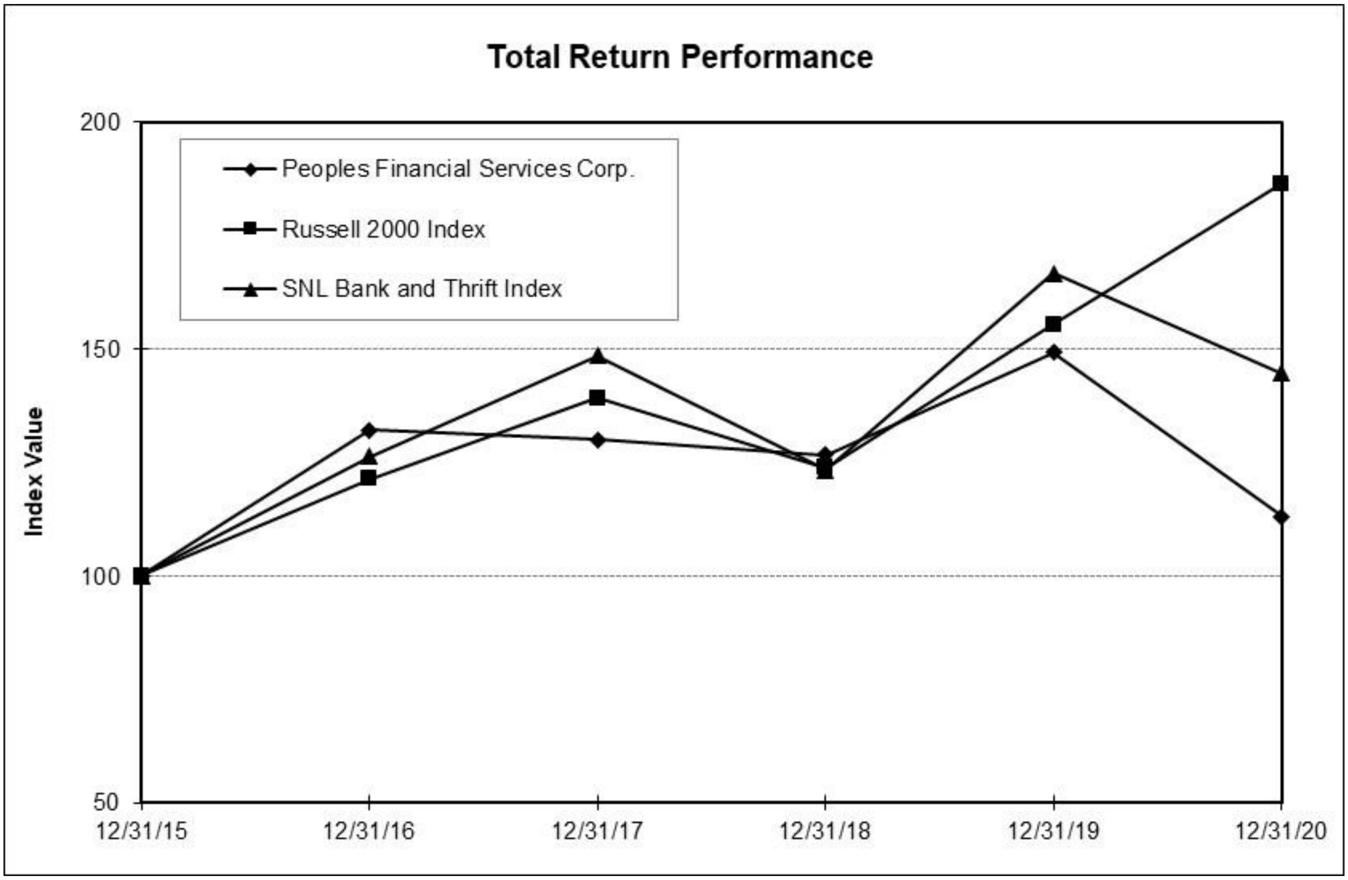
The following table presents information with respect to purchases made by or on behalf of the Company or any "affiliated purchaser," as defined in the Exchange Act Rule 10b-18(a)(3), of the Company's common stock during each of the three months ended December 31, 2020:

Month Ending	Total Number of Shares Purchased	Average Price Paid Per Share	Total Number of Shares Purchased as Part of Publicly Announced Programs	Maximum Number of Shares that may yet be Purchased Under the Programs
October 31, 2020	19,483	$ 35.98	188,388	51,040
November 30, 2020	3,904	$ 37.40	192,292	47,136
December 31, 2020	3,736	$ 37.18	196,028	43,400

On February 28, 2020, our board of directors authorized a common stock repurchase plan whereby we were authorized to repurchase up to 225,000 shares of our outstanding common stock through open market purchases. That plan expired on December 31, 2020. On January 29, 2021, our board of directors authorized a new common stock repurchase plan whereby we are authorized to repurchase up to 4.9 percent of our outstanding common stock, or 353,422 shares.

The following graph and table show the cumulative total return on the common stock of the Company over the last five years, compared with the cumulative total return of a broad stock market index (the Russell 2000 Index or "Russell 2000"), and the SNL Bank and Thrift Index. The cumulative total return on the stock or the index equals the total increase in value since December 31, 2015, assuming reinvestment of all dividends paid into the stock or the index. The graph and table were prepared assuming that $100 was invested on December 31, 2015, in the common stock and the securities included in the indexes.

Comparison of Five-Year Cumulative Total Returns
Performance Graph of
PEOPLES FINANCIAL SERVICES CORP



	Period Ending					
Index	**12/31/2015**	**12/31/2016**	**12/31/2017**	**12/31/2018**	**12/31/2019**	**12/31/2020**
Peoples Financial Services Corp.	100.00	132.04	130.02	126.65	149.18	113.04
Russell 2000 Index	100.00	121.31	139.08	123.76	155.35	186.36
SNL Bank and Thrift Index	100.00	126.25	148.45	123.32	166.67	144.61

Source: S& P Global Market Intelligence
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Item 6. Selected Financial Data.

Consolidated Selected Financial Data
(Dollars in thousands, except per share data)

Year Ended December 31	2020	2019	2018	2017	2016
Condensed statements of financial performance:					
Interest income	$ 94,125	$ 93,381	$ 84,661	$ 74,242	$ 68,984
Interest expense	14,324	17,868	13,322	8,698	7,251
Net interest income	79,801	75,513	71,339	65,544	61,733
Provision for loan losses	7,400	6,100	4,200	4,800	5,000
Net interest income after provision for loan losses	72,401	69,413	67,139	60,744	56,733
Noninterest income	16,642	15,120	13,659	17,186	15,888
Noninterest expense	54,868	55,642	52,487	51,293	48,030
Income before income taxes	34,175	28,891	28,311	26,637	24,591
Provision for income tax expense	4,821	3,155	3,391	8,180	5,008
Net income	$ 29,354	$ 25,736	$ 24,920	$ 18,457	$ 19,583
Condensed statements of financial position:					
Investment securities	$ 303,274	$ 338,557	$ 278,334	$ 281,822	$ 269,927
Net loans	2,150,638	1,915,563	1,801,887	1,674,105	1,517,004
Other assets	429,890	221,207	208,772	213,104	212,511
Total assets	$ 2,883,802	$ 2,475,327	$ 2,288,993	$ 2,169,031	$ 1,999,442
Deposits	$ 2,437,113	$ 1,971,489	$ 1,875,022	$ 1,719,018	$ 1,588,757
Short-term borrowings	50,000	152,150	86,500	123,675	82,700
Long-term debt	14,769	32,733	37,906	49,734	58,134
Subordinated debt	33,000				
Other liabilities	32,043	19,945	10,951	11,628	13,233
Stockholders' equity	316,877	299,010	278,614	264,976	256,618
Total liabilities and stockholders' equity	$ 2,883,802	$ 2,475,327	$ 2,288,993	$ 2,169,031	$ 1,999,442
Per share data:					
Net income - basic	$ 4.02	$ 3.48	$ 3.37	$ 2.50	$ 2.65
Net income - diluted	4.00	3.47	3.37	2.50	2.65
Cash dividends declared	1.44	1.37	1.31	1.26	1.24
Stockholders' equity	$ 43.92	$ 40.47	$ 37.66	$ 35.82	$ 34.71
Cash dividends declared as a percentage of net income	35.83 %	39.37 %	38.90 %	50.49 %	46.83 %
Average common shares outstanding - basic	7,304,956	7,395,429	7,397,797	7,395,837	7,396,716
Average common shares outstanding - diluted	7,337,843	7,412,369	7,402,900	7,395,837	7,396,716
Selected ratios (based on average balances):					
Net income as a percentage of total assets	1.09 %	1.10 %	1.12 %	0.90 %	1.02 %
Net income as a percentage of stockholders' equity	9.48	8.87	9.21	7.02	7.64
Stockholders' equity as a percentage of total assets	11.48	12.37	12.14	12.77	13.36
Tier I capital as a percentage of adjusted total assets	9.28	10.14	10.03	9.94	10.16
Net interest income as a percentage of earning assets	3.25	3.58	3.59	3.69	3.77
Loans, net, as a percentage of deposits	95.70 %	96.83 %	99.55 %	96.50 %	95.81 %
Selected ratios and data (based on period end balances):					
Tier I capital as a percentage of risk-weighted assets	12.16 %	11.90 %	11.95 %	11.85 %	12.49 %
Total capital as a percentage of risk-weighted assets	15.10	13.04	13.10	12.95	13.51
Allowance for loan losses as a percentage of loans, net	1.26	1.17	1.17	1.12	1.04
Nonperforming loans as a percentage of loans, net	0.45 %	0.52 %	0.53 %	0.67 %	0.90 %

Note: Average balances were calculated using average daily balances. Average balances for loans include nonaccrual loans. Tax-equivalent adjustments were calculated using the prevailing statutory tax rate of 21.0% for 2020, 2019, and 2018 and 35.0% for the years 2017 and 2016.

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

Management's Discussion and Analysis 2020 versus 2019
(Dollars in thousands, except per share data)

Management's Discussion and Analysis appearing on the following pages should be read in conjunction with the Consolidated Financial Statements and Management's Discussion and Analysis 2019 versus 2018 contained in this Annual Report on Form 10-K.

Forward-Looking Discussion:

In addition to the historical information contained in this document, the discussion presented may contain and, from time to time, may make, certain statements that constitute forward-looking statements. Words such as "expects," "anticipates," "believes," "estimates" and other similar expressions or future or conditional verbs such as "should," "would" and "could" are intended to identify such forward-looking statements. These statements are not historical facts, but instead represent the current expectations, plans or forecasts of Peoples Financial Services Corp. and its subsidiaries regarding its future operating results, financial position, asset quality, credit reserves, credit losses, capital levels, dividends, liquidity, service charges, cost savings, effective tax rate, impact of changes in fair value of financial assets and liabilities, impact of new accounting and regulatory guidance, legal proceedings and other matters relating to us and the securities that we may offer from time to time. These statements are not guarantees of future results or performance and involve certain risks, uncertainties and assumptions that are difficult to predict, change over time and are often beyond our control. Actual outcomes and results may differ materially from those expressed in, or implied by, forward-looking statements.

You should not place undue reliance on any forward-looking statement and should consider the uncertainties and risks discussed in the "Risk Factors" in Part I, Item 1A of this Annual Report, among others, and in any of our subsequent SEC filings. Forward-looking statements speak only as of the date they are made, and we undertake no obligation to update any forward-looking statement to reflect the impact of circumstances or events that arise after the date the forward-looking statement was made. Notes to the Consolidated Financial Statements referred to in the Management's Discussion and Analysis of Financial Condition and Results of Operations ("MD&A") are incorporated by reference into the MD&A. Certain prior period amounts have been reclassified to conform with the current year's presentation.

Critical Accounting Policies:

Our consolidated financial statements are prepared in accordance with GAAP. The preparation of consolidated financial statements in conformity with GAAP requires us to establish critical accounting policies and make accounting estimates and assumptions that affect the reported amounts of assets and liabilities at the date of the consolidated financial statements, as well as the reported amounts of revenues and expenses during those reporting periods.

For a discussion of the recent Accounting Standards Updates ("ASU") issued by the Financial Accounting Standards Board ("FASB") refer to Note 1 entitled "Summary of significant accounting policies — Recent accounting standards," in the Notes to Consolidated Financial Statements included in Part II, Item 8 of this Annual Report.

An accounting estimate requires assumptions about uncertain matters that could have a material effect on the consolidated financial statements if a different amount within a range of estimates were used or if estimates changed from period to period. Readers of this report should understand that estimates are made considering facts and circumstances at a point in time, and changes in those facts and circumstances could produce results that differ from when those estimates were made. Significant estimates that are particularly susceptible to material change within the near term relate to the determination of allowance for loan losses, determination of other-than-temporary impairment of investment securities, fair value of financial instruments, the valuation of real estate acquired in connection with foreclosures or satisfaction of loans, the valuation of deferred tax assets, and the impairment of goodwill. Actual amounts could differ from those estimates.

We maintain the allowance for loan losses at a level we believe adequate to absorb probable credit losses related to individually evaluated loans, as well as probable incurred losses inherent in the remainder of the loan portfolio as of the balance sheet date. The balance in the allowance for loan losses account is based on past events and current economic conditions among other things.

The allowance for loan losses account consists of an allocated element and an unallocated element. The allocated element consists of a specific portion for the impairment of loans individually evaluated and a formula portion for loss contingencies on those loans collectively evaluated. The unallocated element, if any, is used to cover inherent losses that exist as of the evaluation date, but which have not been identified as part of the allocated allowance using our impairment evaluation methodology due to limitations in the process.

We monitor the adequacy of the allocated portion of the allowance quarterly and adjust the allowance as necessary through normal operations. This ongoing evaluation reduces potential differences between estimates and actual observed losses. The determination of the level of the allowance for loan losses is inherently subjective as it requires estimates that are susceptible to significant revision as more information becomes available. Accordingly, management cannot ensure that charge-offs in future periods will not exceed the allowance for loan losses or that additional increases in the allowance for loan losses will not be required, resulting in an adverse impact on operating results.

In determining the requirement to record an other-than-temporary impairment on securities owned by us, four main characteristics are considered including: (i) the length of time and the extent to which the fair value has been less than amortized cost; (ii) the financial condition and near-term prospects of the issuer; (iii) whether the market decline was affected by macroeconomic conditions and (iv) whether the Company has the intent to sell the debt security or more likely than not will be required to sell the debt security before its anticipated recovery. The assessment of whether an other-than-temporary impairment exists involves a high degree of subjectivity and judgment and is based on information available to us at a point in time.

Fair values of financial instruments, in cases where quoted market prices are not available, are based on estimates using present value or other valuation techniques which are subject to change.

Real estate acquired in connection with foreclosures or in satisfaction of loans is adjusted to fair value based upon current estimates derived through independent appraisals less cost to sell. However, proceeds realized from sales may ultimately be higher or lower than those estimates.

Deferred tax assets and liabilities are recognized for the estimated future tax effects of temporary differences by applying enacted statutory tax rates to differences between the financial statement carrying amounts and the tax bases of existing assets and liabilities. The amount of deferred tax assets is reduced, if necessary, to the amount that, based on available evidence, will more likely than not be realized. As changes in tax laws or rates are enacted, deferred tax assets and liabilities are adjusted through the provision for income taxes.

Goodwill is evaluated at least annually for impairment or more frequently if conditions indicate potential impairment exist. Any impairment losses arising from such testing are reported in the income statement in the current period as a separate line item within operations.

For a further discussion of our critical accounting policies, refer to Note 1 entitled, “Summary of significant accounting policies,” in the Notes to Consolidated Financial Statements to this Annual Report. Note 1 lists the significant accounting policies used by us in the development and presentation of the consolidated financial statements. This discussion and analysis, the Notes to Consolidated Financial Statements and other financial statement disclosures identify and address key variables and other qualitative and quantitative factors that are necessary for the understanding and evaluation of our financial position, results of operations and cash flows.

Operating Environment:

On March 11, 2020, the World Health Organization declared a coronavirus, identified as COVID-19, a global pandemic. In the United States, the rapid spread of the COVID-19 virus invoked various federal, state and local authorities to make emergency declarations and issue executive orders to limit the spread of the disease. Measures included restrictions on travel, limitations on public gatherings, implementation of social distancing protocols, school closings, orders to shelter in place and mandates to close all non-essential businesses to the public. Concerns about the spread of the disease and its anticipated negative impact on economic activity severely disrupted domestic financial markets prompting the Federal Reserve System's FOMC to aggressively cut the target federal funds rate to a range of 0% to 0.25%, including a 50 basis point reduction in the target federal funds rate on March 3, 2020 and an additional 100 basis point reduction on March 15, 2020. In addition, the Federal Reserve rolled out various market support programs to ease the stress on financial markets which continue to be in place.

The rate cuts in March marked the fourth and fifth cut in the overnight rate in the most recent monetary easing cycle, which began in July 2019 after the most recent high for the target range for federal funds of 2.25% to 2.50% which was in December 2018. Overall inflation lags below the FOMC's long-term desired 2% level for items other than food and energy. The consumer price index ("CPI") registered 1.6% for the 12 months ended December 31, 2020, down from 1.7% for the 12 months ended September 30, 2020 but higher than the 1.2% reading for the 12 months ended June 30, 2020. The all items index increased 1.4% for the 12 months ending December 31, 2020, level from the 1.4% registered for the 12 months ending September 30, 2020 and up from the reading for the 12 months ending June 30, 2020 which was 0.6%. As the U.S. economy rebounded from the initial slowdown in the second quarter of 2020 that was brought on by the nation wide shutdown, Gross domestic product ("GDP"), the value of all goods and services produced in the nation, grew in the fourth quarter at a 2.1% annualized rate, in line with consensus forecasts, which followed a third quarter 2020 reading of a 33.4% annualized rate, better than the consensus forecast of 32.0% for the quarter. Personal consumption increased by 1.7% during the fourth quarter.

The employment situation deteriorated in New York and Pennsylvania and in all of the thirteen counties representing our market areas in Pennsylvania and New York from one year ago when comparing December 31, 2020 to December 31, 2019. Projections for our local market unemployment are not readily available, however the most current economic statistics as of January 31, 2021 show continuing jobless claims of over 4.5 million. This indicates a significant improvement from the peak of 17 million jobless claims from 2020, but it remains elevated as does the unemployment rate at 8.1% on a national level per the latest report from the Bureau of Labor Statistics at December 31, 2020. By comparison, the unemployment rate was 8.8% at quarter end September 30, 2020 and 13.0% at quarter end June 30, 2020. Prior to the economic fallout of the COVID-19 pandemic, the highest recorded unemployment rate in recent history was 9.9% in 2009 during the Great Recession. As the pandemic continues to remain a focus of the economic recovery, elevated unemployment rates could have an adverse effect on our credit quality and may result in increased credit losses within the loan portfolio in future periods. On a national level, as with our regional and local economies, employment conditions deteriorated in 2020. The civilian labor force decreased 4.0 million, while the number of people employed decreased 8.9 million in 2020. As a result, the annual unemployment rate for the U.S. increased in 2020 when compared to 2019.

National, Pennsylvania, New York and our market area's non-seasonally-adjusted annual unemployment rates in 2020 and 2019, are summarized as follows:

	2020	2019
United States	8.1 %	3.7 %
New York (statewide)	10.0	4.0
Pennsylvania (statewide)	9.1	4.1
Broome County	8.3	4.6
Bucks County	8.4	3.6
Lackawanna County	9.9	4.6
Lebanon County	7.9	3.7
Lehigh County	9.5	4.3
Luzerne County	11.2	5.4
Monroe County	11.6	5.1
Montgomery County	7.8	3.3
Northampton County	9.0	4.2
Schuylkill County	9.3	5.1
Susquehanna County	7.5	4.1
Wayne County	9.5	4.4
Wyoming County	8.7 %	4.6 %

With respect to the banking industry, net income for all FDIC-insured banks in 2020 totaled $147.9 billion, a decrease of $84.9 billion or 36.5 percent from 2019. The decline was primarily attributable to the increased provisioning due to the decline in economic conditions in the first six months of 2020. Approximately 53.7 percent of all institutions reported higher net income in 2020, while only 3.9 percent reported net losses, up slightly from last year's reported 3.6 percent unprofitable institutions. Loan loss provisions of $132.2 billion in 2020 were $77.1 billion or 140.0 percent more than banks set aside in 2019. Net interest income decreased for the first time in seven years, by $20.0 billion or 3.7 percent. Noninterest income was $15.9 billion or 6.0 percent above the level of 2019. Realized gains on sales of investments were $8.1 billion compared to $4.0 billion in 2019. Total noninterest expense increased $32.9 billion or 6.9 percent comparing 2020 and 2019. The return on average assets for 2020 was 0.72 percent compared to 1.29 percent in 2019.

Review of Financial Position:

Peoples Financial Services Corp., a bank holding company incorporated under the laws of Pennsylvania, provides a full range of financial services through its wholly-owned subsidiary, Peoples Security Bank and Trust Company ("Peoples Bank"), collectively, the "Company" or "Peoples". The Company services its retail and commercial customers through twenty-six full-service community banking offices located within the Lackawanna, Lebanon, Lehigh, Luzerne, Monroe, Montgomery, Northampton, Susquehanna and Wyoming Counties of Pennsylvania and Broome County of New York.

Peoples Bank is a state-chartered bank and trust company under the jurisdiction of the Pennsylvania Department of Banking and Securities and the Federal Deposit Insurance Corporation. Peoples Bank's primary product is loans to small- and medium-sized businesses. Other lending products include one-to-four family residential mortgages and consumer loans. Peoples Bank primarily funds its loans by offering checking accounts and money market accounts to commercial enterprises and individuals. Other deposit product offerings include certificates of deposits and various non-maturity deposit accounts.

The Company faces competition primarily from commercial banks, thrift institutions and credit unions within its Pennsylvania and New York market, many of which are substantially larger in terms of assets and capital. In addition, mutual funds and security brokers compete for various types of deposits, and consumer, mortgage, leasing and insurance companies compete for various types of loans and leases. Principal methods of competing for banking and permitted nonbanking services include price, nature of product, quality of service and convenience of location.

The Company and Peoples Bank are subject to regulations of certain federal and state regulatory agencies, including the Federal Reserve, the FDIC, and Pennsylvania Department of Banking and Securities, and undergo periodic examinations by such agencies.

Total assets, loans and deposits were $2.9 billion, $2.2 billion and $2.4 billion, respectively, at December 31, 2020. Total assets, loans and deposits grew 16.5 percent, 12.4 percent and 23.6 percent, respectively, compared to 2019 year-end balances.

The loan portfolio consisted of $1.8 billion of business loans, including commercial and commercial real estate loans, and $360.7 million in retail loans, including residential mortgage and consumer loans at December 31, 2020. Total investment securities were $303.3 million at December 31, 2020, including $295.9 million of investment securities classified as available-for sale and $7.2 million classified as held-to-maturity. Total deposits consisted of $622.5 million in noninterest-bearing deposits and $1.8 billion in interest-bearing deposits at December 31, 2020.

Stockholders' equity equaled $316.9 million, or $43.92 per share, at December 31, 2020, and $299.0 million, or $40.47 per share, at December 31, 2019. Our equity to asset ratio was 11.0 percent and 12.1 percent at those respective period ends. Dividends declared for the 2020 amounted to $1.44 per share representing 35.8 percent of net income.

Nonperforming assets equaled $10.5 million or 0.48 percent of loans, net and foreclosed assets at December 31, 2020, as the balance remained the same, however, the percentage was lower when compared to $10.5 million or 0.54 percent at December 31, 2019. The allowance for loan losses equaled $27.3 million or 1.26 percent of loans, net, at December 31, 2020, compared to $22.7 million or 1.17 percent at year-end 2019. Loans charged-off, net of recoveries equaled $2.7 million or 0.13 percent of average loans in 2020, compared to $4.8 million or 0.26 percent of average loans in 2019.

Investment Portfolio:

Primarily, our investment portfolio provides a source of liquidity needed to meet expected loan demand and generates a reasonable return in order to increase our profitability. Additionally, we utilize the investment portfolio to meet pledging requirements and reduce income taxes. At December 31, 2020, our portfolio consisted primarily of short-term U.S. Treasury and government agency securities, which provide a source of liquidity and intermediate-term, tax-exempt state and municipal obligations, which mitigate our tax burden.

Our investment portfolio is subject to various risk elements that may negatively impact our liquidity and profitability. The greatest risk element affecting our portfolio is market risk or interest rate risk ("IRR"). Understanding IRR, along with other inherent risks and their potential effects, is essential in effectively managing the investment portfolio.

Market risk or IRR relates to the inverse relationship between bond prices and market yields. It is defined as the risk that increases in general market interest rates will result in market value depreciation. A marked reduction in the value of the investment portfolio could subject us to liquidity strains and reduced earnings if we are unable or unwilling to sell these investments at a loss. Moreover, the inability to liquidate these assets could require us to seek alternative funding, which may further reduce profitability and expose us to greater risk in the future. In addition, since the majority of our investment portfolio is designated as available-for-sale and carried at estimated fair value, with net unrealized gains and losses reported as a separate component of stockholders' equity, market value depreciation could negatively impact our capital position.

During March 2020, the FOMC took aggressive actions to cut the targeted federal funds rate 150 basis points to a range of 0.00% to 0.25% in an effort to help protect the U.S. economy from COVID-19. At their January 2021 meeting, the FOMC decided to keep the target range for the federal funds rate at 0 to 1/4 percent and expects it will be appropriate to maintain this target range until labor market conditions have reached levels consistent with the Committee's assessments of maximum employment and inflation has risen to 2 percent and is on track to moderately exceed 2 percent for some time. Furthermore, the Committee stated it is committed to using its full range of tools to support the U.S. economy during the COVID-19 pandemic. Our investment portfolio consists primarily of fixed-rate bonds. As a result, changes in the velocity and magnitude of future FOMC actions can significantly influence the fair value of our portfolio.

Specifically, the parts of the yield curve most closely related to our investments include the 2-year and 10-year U.S. Treasury security. The yield on the 2-year U.S. Treasury note affects the values of our U.S. Treasury and government agency securities, whereas the 10-year U.S. Treasury note influences the value of tax-exempt and taxable state and municipal obligations. The yield on the 2-year U.S. Treasury ranged from a low of 10 basis points to a high of 160 basis points during 2020 before ending the year at 12 basis points. The yield on the 10-year U.S. Treasury ranged from a low of 39 basis points to a high of 189 basis points while ending 2020 at 91 basis points. Since bond prices move inversely to yields, we experienced an increase in the aggregate fair value of our investment portfolio when comparing December 31, 2020 to December 31, 2019 due to lower market rates at year end 2020. The net unrealized holding gains included in our available-for-sale investment portfolio were $9.7 million at December 31, 2020 compared to a gain of $1.8 million at December 31, 2019. We reported net unrealized holding gain, included as a separate component of stockholders' equity of $7.7 million, net of income taxes of $2.0 million, at December 31, 2020, and an unrealized holding gain of $1.4 million, net of income taxes of $0.4 million, at December 31, 2019. An increase in interest rates could negatively impact the market value of our investments and our capital position. In order to monitor the potential effects a rise in interest rates could have on the value of our investments, we perform stress test modeling on the portfolio. Stress tests conducted on our portfolio at December 31, 2020, indicated that should general market rates increase by 100, 200 or 300 basis points, we would anticipate declines of 4.8 percent, 9.9 percent and 14.9 percent in the market value of our portfolio.

The carrying values of the major classifications of investment securities and their respective percentages of total investment securities for the past three years are summarized as follows:

Distribution of investment securities (Dollars in thousands)

	2020		2019		2018	
December 31,	**Amount**	**%**	**Amount**	**%**	**Amount**	**%**
U.S. Treasury securities	$ 18,905	6.23 %	$ 24,128	7.13 %	$ 25,592	9.20 %
U.S. government-sponsored enterprises	65,188	21.49	87,110	25.73	92,818	33.35
State and municipals:						
Taxable	55,366	18.26	34,898	10.31	13,853	4.98
Tax-exempt	63,843	21.05	67,015	19.79	92,809	33.34
Corporate debt securities	1,000	0.33				
Residential mortgage-backed securities:						
U.S. government agencies	3,728	1.23	8,501	2.51	12,671	4.55
U.S. government-sponsored enterprises	81,606	26.91	103,621	30.60	34,261	12.31
Commercial mortgage-backed securities:						
U.S. government-sponsored enterprises	13,500	4.45	12,861	3.80	6,039	2.17
Common equity securities	138	0.05	423	0.13	291	0.10
Total	$ 303,274	100.00 %	$ 338,557	100.00 %	$ 278,334	100.00 %

Investment securities decreased $35.3 million, to $303.3 million at December 31, 2020, from $338.6 million at December 31, 2019. At December 31, 2020, the investment portfolio consisted of $295.9 million of investment securities classified as available-for-sale and $7.2 million classified as held-to-maturity. Investment cash flow was used to fund the loan pipeline prior to the economic slowdown brought on by COVID-19 during the first quarter of 2020. For the majority of the remainder of 2020, investment cash flow was directed to overnight federal funds sold, as management focused on increasing liquidity in the uncertain economic environment. As the level of overnight funds increased, our Asset Liability Committee recommended a strategy to deploy a portion of those funds back into the investment portfolio through purchases of primarily taxable and tax-free municipal bonds and mortgage-backed securities to mitigate risk in a flat and down rate environment. Security purchases totaled $107.2 million in 2020, with purchases consisting of longer term taxable and tax-exempt municipal securities and mortgage-backed securities. Investment purchases in 2019 amounted to $124.5 million.

Repayments of investment securities totaled $85.0 million in 2020 and $58.2 million in 2019. During the first quarter of 2020, the Company sold $26.5 million of low-yielding short-term municipal bonds resulting in a gain of $267 thousand. The proceeds were used to fund higher yielding loans. Additionally, two mortgage-backed securities were sold during the second half of 2020 with proceeds totaling $38.3 million and gains recognized of $651 thousand due to favorable market rates. Sales of $9.7 million of low-yielding municipal securities during 2019 resulted in a gain of $23 thousand. We continually analyze the investment portfolio with respect to its exposure to various risk elements.

The composition of our investment portfolio changed during 2020 as a result of the aforementioned transactions. Short-term bullet U.S. Treasury and U.S. government-sponsored enterprise securities comprised 27.7 percent of our total portfolio at yearend 2020 compared to 32.9 percent at the end of 2019. Tax-exempt municipal obligations increased as a percentage of the total portfolio to 21.1 percent at year-end 2020 from 19.8 percent at the end of 2019, however the total balance declined as the sales of $26.5 million, maturities and bond calls offset the new purchases. Taxable municipals increased as a percentage of the total portfolio to 18.3 percent at year-end 2020 from 10.3 percent at the end of 2019 as the sector provided value opportunities. The weighted average life of the investment portfolio lengthened to 4.3 years at December 31, 2020 from 3.7 years at year end 2019, while the effective duration of the investment portfolio increased to 4.4 years at December 31, 2020 from 3.6 years at December 31, 2019.

There were no other-than-temporary impairments ("OTTI") recognized for the years ended December 31, 2020, 2019 and 2018. For additional information related to OTTI refer to Note 3 entitled "Investment securities" in the Notes to Consolidated Financial Statements to this Annual Report.

Investment securities averaged $292.7 million and equaled 11.7 percent of average earning assets in 2020, compared to $279.4 million and 13.0 percent of average earning assets in 2019. The tax-equivalent yield on the investment portfolio decreased eleven basis points to 2.36 percent in 2020 from 2.47 percent in 2019. The decrease in the tax-equivalent yield is due primarily to cash flow from maturing and called bonds being reinvested into lower market rates.

At December 31, 2020 and 2019, there were no securities of any individual issuer, except for U.S. government agency mortgage-backed securities, that exceeded 10.0 percent of stockholders' equity.

The maturity distribution based on the carrying value and weighted-average, tax-equivalent yield of the investment portfolio at December 31, 2020, is summarized as follows. The weighted-average yield, based on amortized cost, has been computed for tax-exempt state and municipals on a tax-equivalent basis using the prevailing federal statutory tax rate of 21.0 percent. The distributions are based on contractual maturity. Expected maturities may differ from contractual maturities because borrowers have the right to call or prepay obligations with or without call or prepayment penalties.

Maturity distribution of investment securities (Dollars in thousands)

December 31, 2020	Within one year Amount	Yield	After one but within five years Amount	Yield	After five but within ten years Amount	Yield	After ten years Amount	Yield	Total Amount	Yield
U.S. Treasury securities	$ 7,097	1.81 %	$ 11,808	2.09 %					$ 18,905	1.98 %
U.S. government-sponsored enterprises	30,254	1.62	31,432	1.69	$ 37	4.37 %	$ 3,465	2.24 %	65,188	1.71
State and municipals:										
Taxable			4,173	5.10	16,959	2.35	34,234	2.15	55,366	2.42
Tax-exempt			2,031	4.39	5,163	2.65	56,649	2.88	63,843	2.91
Corporate debt securities					1,000	4.25			1,000	4.25
Residential mortgage-backed securities:										
U.S. government agencies			536	1.93			3,192	3.51	3,728	3.27
U.S. government-sponsored enterprises	65	0.77	1,547	2.57	9,030	2.86	70,964	1.85	81,606	1.97
Commercial mortgage-backed securities:										
U.S. government-sponsored enterprises			6,557	2.27	6,943	2.67			13,500	2.47
Total	$ 37,416	1.66 %	$ 58,084	2.22 %	$ 39,132	2.62 %	$ 168,504	2.29 %	$ 303,136	2.24 %

Loan Portfolio:

Economic factors and how they affect loan demand are of extreme importance to us and the overall banking industry, as lending is a primary business activity. Loans are the most significant component of earning assets and they generate the greatest amount of revenue for us. Similar to the investment portfolio, there are risks inherent in the loan portfolio that must be understood and considered in managing the lending function. These risks include IRR, credit concentrations and fluctuations in demand. Changes in economic conditions and interest rates affect these risks which influence loan demand, the composition of the loan portfolio and profitability of the lending function.

The composition of the loan portfolio at year-end for the past five years is summarized as follows:

Distribution of loan portfolio (Dollars in thousands)

December 31,	2020 Amount	%	2019 Amount	%	2018 Amount	%	2017 Amount	%	2016 Amount	%
Commercial	$ 679,286	31.19 %	$ 522,957	26.98 %	$ 494,134	27.10 %	$ 476,199	28.12 %	$ 408,814	26.67 %
Real estate:										
Commercial	1,137,990	52.25	1,011,423	52.18	907,803	49.79	786,210	46.44	700,144	45.67
Residential	277,414	12.74	301,378	15.55	299,876	16.45	287,935	17.01	289,781	18.90
Consumer	83,292	3.82	102,482	5.29	121,453	6.66	142,721	8.43	134,226	8.76
Total loans	2,177,982	100.00 %	1,938,240	100.00 %	1,823,266	100.00 %	1,693,065	100.00 %	1,532,965	100.00 %
Less: allowance for loan loss	27,344		22,677		21,379		18,960		15,961	
Net loans	$ 2,150,638		$ 1,915,563		$ 1,801,887		$ 1,674,105		$ 1,517,004	

From a lending perspective, organic loan growth, with the exception of PPP loans, slowed during 2020 as we focused on managing our existing portfolio during the pandemic. We participated in the CARES Act, Paycheck Protection Program, a $350 billion specialized low-interest loan program funded by the U.S. Treasury Department and administered by the U.S. Small Business Administration. The PPP provides borrower guarantees for lenders, as well as loan forgiveness incentives for borrowers that utilize the loan proceeds to cover employee compensation related business operating costs. During 2020, we had approved 1,450 PPP loans totaling $217.5 million. Substantially all of the loans were made to existing customers, funded under the two year PPP loan program. PPP loan forgiveness commenced during the fourth quarter of 2020 with $27.8 million being received. We expect the majority of the remaining $189.7 million to be forgiven during 2021. In addition, the Company is participating in the 2021 second round of PPP lending and has received approval by the SBA on 605 applications totaling $80.7 million. These loans closed during January and February.

Overall, total loans increased $239.7 million or 12.4 percent in 2020 to $2.2 billion at December 31, 2020. Excluding PPP loans, loan growth totaled $50.0 million or 2.6%. Business loans, including commercial loans and commercial real estate loans, were $1.8 billion or 83.4 percent of total loans at December 31, 2020, and $1.5 billion or 79.2 percent at year-end 2019. Residential mortgages and consumer loans totaled $360.7 million or 16.6 percent of total loans at year-end 2020 and $403.9 million or 20.8 percent at year-end 2019. Loan growth, excluding PPP loans, was significantly affected by the economic slowdown resulting from COVID-19. Total loan growth, excluding PPP loans, of $50.0 million was primarily attributable to increases in our commercial real estate portfolio which grew $126.6 million in 2020 due to continued success of our strategy to expand in larger markets with strong growth potential, and strong organic growth in our legacy markets. Our expansion strategy commenced during 2014 in the Lehigh Valley with a community banking office and team of dedicated lenders and has expanded with two additional branch offices and additional teams of experienced lenders and credit professionals. Growth is also due to our presence in the Greater Delaware Valley, first by opening a branch office in King of Prussia in 2016, and most recently during the first quarter of 2020 with the opening of a branch in Doylestown and recruitment of two experienced lenders. Further growth was attained by our entrance into Central Pennsylvania with a branch office in Lebanon, staffed with a team of lending professionals during the middle of 2018. Based on the customer service oriented philosophy of our organization along with the commitment of these employees, we continue to be well received in these new markets as we are in our existing markets.

Residential mortgage loans decreased $24.0 million during 2020 as low market rates due to the FOMC's actions to cut rates in response to the adverse economic impact of the pandemic, were an incentive for borrowers to refinance their current mortgages. We sold the majority of our residential mortgage originations into the secondary market instead of holding the mortgages in portfolio to mitigate interest rate risk. Consumer loans declined $19.2 million during 2020 primarily from the run-off in our indirect automobile portfolio due to pricing changes.

Loans averaged $2.1 billion in 2020, compared to $1.9 billion in 2019. Taxable loans averaged $2.0 billion, while tax-exempt loans averaged $124.9 million in 2020. The loan portfolio continues to play the prominent role in our earning asset mix. As a percentage of earning assets, average loans equaled 85.1 percent in 2020, a decrease from 86.6 percent in 2019.

The tax-equivalent yield on our loan portfolio decreased 55 basis points to 4.16 percent in 2020 from 4.71 percent in 2019 due to lower yields on new loan originations, the repricing lower of floating and adjustable rate loans due to the decrease in market rates beginning during the second half of 2019 and continuing into 2020, and the low 1% interest rate on PPP loans. In the first quarter of 2020 we decreased our prime lending rate 150 basis points after reducing it 75 basis points during the second half of 2019 all in response to the FOMC cutting its targeted federal funds rate. Our prime rate ended the year at 3.25%. The lower prime rate has resulted in lower loan yields which can be evidenced by evaluating 2020 quarterly loan yields, which ranged from 4.55 percent in the first quarter to 3.97 percent in the fourth quarter. The yield on the loan portfolio may continue to be under pressure as repayments on loans are replaced with new originations at current market rates, floating and adjustable rate loans continue to reprice lower, PPP loans continue to be included in the portfolio and competition continues to prompt more aggressive pricing for high quality fixed rate intermediate term loans, thus providing downward momentum in loan yields.

The maturity distribution and sensitivity information of the loan portfolio by major classification at December 31, 2020, is summarized as follows:

Maturity distribution and interest sensitivity of loan portfolio (Dollars in thousands)

December 31, 2020	Within one year	After one but within five years	After five years	Total
Maturity schedule:				
Commercial	$ 330,653	$ 194,997	$ 153,636	$ 679,286
Real estate:				
Commercial	229,025	588,135	320,830	1,137,990
Residential	78,593	153,686	45,135	277,414
Consumer	40,025	42,249	1,018	83,292
Total	$ 678,296	$ 979,067	$ 520,619	$ 2,177,982
Predetermined interest rates	$ 379,085	$ 494,988	$ 156,492	$ 1,030,565
Floating or adjustable interest rates	299,211	484,079	364,127	1,147,417
Total	$ 678,296	$ 979,067	$ 520,619	$ 2,177,982

As previously mentioned, there are numerous risks inherent in the loan portfolio. We manage the portfolio by employing sound credit policies and utilizing various modeling techniques in order to limit the effects of such risks. In addition, we utilize private mortgage insurance ("PMI") and guaranteed Small Business Administration and Federal Home Loan Bank of Pittsburgh ("FHLB-Pgh") loan programs to mitigate credit risk in the loan portfolio.

In an attempt to limit interest rate risk ("IRR") and liquidity strains, we continually examine the maturity distribution and interest rate sensitivity of the loan portfolio. Market interest rates began to fall during the final six months of 2019 as the FOMC cut the targeted federal funds rate three times and continued to fall as the FOMC cut the targeted federal funds rate 150 basis points in March 2020 in response to COVID-19. Given our IRR to flat or falling rates, we placed emphasis on originating longer-term fixed-rate and adjustable-rate loans with interest rate floors. Fixed-rate loans represented 47.3 percent of the loan portfolio at December 31, 2020, compared to floating or adjustable-rate loans at 52.7 percent. Approximately 31.1 percent of the loan portfolio is expected to reprice within the next 12 months.

Additionally, our secondary market mortgage banking program provides us with an additional source of liquidity and a means to limit our exposure to IRR. Through this program, we are able to competitively price conforming one-to-four family residential mortgage loans without taking on IRR which would result from retaining these long-term, low fixed-rate loans on our books. The loans originated are subsequently sold in the secondary market, with the sales price locked in at the time of commitment, thereby greatly reducing our exposure to IRR.

Loan concentrations are considered to exist when the total amount of loans to any one borrower, or a multiple number of borrowers engaged in similar business activities or having similar characteristics, exceeds 25.0 percent of capital outstanding in any one category. We provide deposit and loan products and other financial services to individual and corporate customers in our current market area. There are no significant concentrations of credit risk from any individual counterparty or groups of counterparties, except for geographic concentrations in our market area.

Off- Balance Sheet Arrangements:

In addition to the risks inherent in our loan portfolio, in the normal course of business, we are also a party to financial instruments with off-balance sheet risk to meet the financing needs of our customers. These instruments include legally binding commitments to extend credit, unused portions of lines of credit and commercial letters of credit, and may involve, to varying degrees, elements of credit risk and IRR in excess of the amount recognized in the consolidated financial statements.

Credit risk is the principal risk associated with these instruments. Our involvement and exposure to credit loss in the event that the instruments are fully drawn upon and the customer defaults is represented by the contractual amounts of these instruments. In order to control credit risk associated with entering into commitments and issuing letters of credit, we employ the same credit quality and collateral policies in making commitments that we use in other lending activities. We evaluate each customer’s creditworthiness on a case-by-case basis, and if deemed necessary, obtain collateral. The amount and nature of the collateral obtained is based on our credit evaluation.

The contractual amounts of off-balance sheet commitments at year-end for the past three years are summarized as follows:

Distribution of off-balance sheet commitments (Dollars in thousands)

December 31	2020	2019	2018
Commitments to extend credit	$ 336,667	$ 290,517	$ 294,122
Unused portions of lines of credit	55,391	52,168	51,790
Commercial letters of credit	34,428	45,018	33,275
Total	$ 426,486	$ 387,703	$ 379,187

We record a valuation allowance for off-balance sheet credit losses, if deemed necessary, separately as a liability. The valuation allowance amounted to $122 thousand and $45 thousand at December 31, 2020 and 2019. We do not anticipate that losses, if any, that may occur as a result of funding off-balance sheet commitments, would have a material adverse effect on our operating results or financial position.

Contractual Obligations and Commitments:

In the ordinary course of operations, we enter into various financial obligations, including contractual obligations that may require future cash payments. As a financial services provider, we routinely enter into commitments to extend credit, including loan commitments, standby and commercial letters of credit. Such commitments are subject to the same credit policies and approval process accorded to loans made by the Bank. See Note 5 of the consolidated financial statements for additional information.

The following table summarizes our contractual obligations and other commitments to make future payments as of December 31, 2020. Payments for deposits and borrowings do not include interest. Payments related to leases are based on actual payments specified in the underlying contracts. Commitments to extend credit and standby letters of credit are presented at contractual amounts; however, since many of these commitments are expected to expire unused or only partially used based upon our historical experience, the total amounts of these commitments do not necessarily reflect future cash requirements.

	December 31, 2020				
(Dollars in thousands)	Total	One Year or Less	Over One Year Through Three Years	Over Three Years Through Five Years	Over Five Years
Contractual Obligations:					
Time Deposits	$ 319,693	$ 223,247	$ 62,998	$ 22,415	$ 11,033
Short-term borrowings	50,000	50,000			
FHLB advances	14,769	12,058	2,711	-	
Subordinated debt	33,000				33,000
Operating leases	8,281	611	1,178	992	5,500
Total	$ 425,743	$ 285,916	$ 66,887	$ 23,407	$ 49,533
Other commitments:					
Commitments to extend credit	$ 393,871	$ 335,019	$ 1,378	$	$ 57,474
Standby letters of credit	36,859	36,859			
Total	$ 430,730	$ 371,878	$ 1,378	$	$ 57,474

Asset Quality:

We are committed to developing and maintaining sound, quality assets through our credit risk management policies and procedures. Credit risk is the risk to earnings or capital which arises from a borrower's failure to meet the terms of their loan obligations. We manage credit risk by diversifying the loan portfolio and applying policies and procedures designed to foster sound lending practices. These policies include certain standards that assist lenders in making judgments regarding the character, capacity, cash flow, capital structure and collateral of the borrower.

With regard to managing our exposure to credit risk in light of general devaluations in real estate values, we have established maximum loan-to-value ratios for commercial mortgage loans not to exceed 80.0 percent of the appraised value. With regard to residential mortgages, customers with loan-to-value ratios in excess of 80.0 percent are generally required to obtain Private Mortgage Insurance (PMI). PMI is used to protect us from loss in the event loan-to-value ratios exceed 80.0 percent and the customer defaults on the loan. Appraisals are performed by an independent appraiser engaged by us, not the customer, who is either state certified or state licensed depending upon collateral type and loan amount.

With respect to lending procedures, lenders and our credit underwriters must determine the borrower's ability to repay their loans based on prevailing and expected market conditions prior to requesting approval for the loan. The Bank's board of directors establishes and reviews, at least annually, the lending authority for certain senior officers, loan underwriters and branch personnel. Credit approvals beyond the scope of these individual authority levels are forwarded to a loan committee. This committee, comprised of certain members of senior management, review credits to monitor the quality of the loan portfolio through careful analysis of credit applications, adherence to credit policies and the examination of outstanding loans and delinquencies. These procedures assist in the early detection and timely follow-up of problem loans.

Credit risk is also managed by monthly internal reviews of individual credit relationships in our loan portfolio by credit administration and the asset quality committee. These reviews aid us in identifying deteriorating financial conditions of borrowers and allows us the opportunity to assist customers in remedying these situations.

Nonperforming assets consist of nonperforming loans and foreclosed assets. Nonperforming loans include nonaccrual loans, troubled debt restructured loans and accruing loans past due 90 days or more. For a discussion of our policy regarding nonperforming assets and the recognition of interest income on impaired loans, refer to the notes entitled, "Summary of significant accounting policies — Nonperforming assets," and "Loans, net and allowance for loan losses" in the Notes to Consolidated Financial Statements to this Annual Report which are incorporated in this item by reference.

Information concerning nonperforming assets for the past five years is summarized as follows. The table includes credits classified for regulatory purposes and all material credits that cause us to have serious doubts as to the borrower's ability to comply with present loan repayment terms.

Distribution of nonperforming assets (Dollars in thousands)

December 31	2020	2019	2018	2017	2016
Nonaccrual loans:					
Commercial	$ 3,359	$ 3,336	$ 776	$ 860	$ 934
Real estate:					
Commercial	2,642	2,765	2,328	3,454	7,016
Residential	869	1,144	2,574	2,994	2,961
Consumer	111	261	212	177	155
Total nonaccrual loans	6,981	7,506	5,890	7,485	11,066
Troubled debt restructured loans:					
Commercial	920	1,302	1,438	1,577	1,150
Real estate:					
Commercial	1,310	283	719	836	141
Residential	588	608	622	661	618
Total troubled debt restructured loans	2,818	2,193	2,779	3,074	1,909
Accruing loans past due 90 days or more:					
Real estate:					
Commercial			73		
Residential	71	378	850	548	558
Consumer				186	286
Total accruing loans past due 90 days or more	71	378	923	734	844
Total nonperforming loans	9,870	10,077	9,592	11,293	13,819
Foreclosed assets	632	450	376	284	393
Total nonperforming assets	$ 10,502	$ 10,527	$ 9,968	$ 11,577	$ 14,212
Nonperforming loans as a percentage of loans, net	0.45 %	0.52 %	0.53 %	0.67 %	0.90 %
Nonperforming assets as a percentage of loans, net and foreclosed assets	0.48 %	0.54 %	0.55 %	0.68 %	0.93 %

Our nonperforming assets remained relatively stable decreasing $25 thousand or 0.2 percent at December 31, 2020 when compared to the end of 2019, however, we experienced improvement in our asset quality ratios as evidenced by a decrease in nonperforming assets as a percentage of loans, net and foreclosed assets to 0.48 percent from 0.54 percent, and nonperforming loans as a percentage of loans, net to 0.45 percent from 0.52 percent. The slight decrease in balances resulted from a $0.5 million decrease in nonaccrual loans due to the transfer of a $0.4 million residential mortgage to other real estate owned, offset by an increase in troubled debt restructurings of $0.6 million. The increase of $0.6 million in troubled debt restructured loans resulted from a $1.0 million increase in commercial real estate loans due to the addition of one restaurant related credit and two small business loans adversely impacted by the economic slowdown caused by COVID-19, partially offset by a decrease to commercial loans of $0.4 million due to a partial charge off to one credit and principal payments. We believe the three credits added are all adequately secured. Total accruing loans past due ninety days or more decreased $0.3 million to partially offset the increases. For a further discussion of assets classified as nonperforming assets and potential problem loans, refer to the note entitled, "Loans, net and the allowance for loan losses," in the Notes to Consolidated Financial Statements to this Annual Report.

We maintain the allowance for loan losses at a level we believe adequate to absorb probable credit losses related to individually evaluated loans, as well as probable incurred losses inherent in the remainder of the loan portfolio as of the balance sheet date. The balance in the allowance for loan losses account is based on past events and current economic conditions. We employ the FFIEC Interagency Policy Statement, as amended, and GAAP in assessing the adequacy of the allowance account. Under GAAP, the adequacy of the allowance account is determined based on the provisions of FASB Accounting Standards Codification ("ASC") 310 for loans specifically identified to be individually evaluated for impairment and the requirements of FASB ASC 450, for large groups of smaller-balance homogeneous loans to be collectively evaluated for impairment.

We follow our systematic methodology in accordance with procedural discipline by applying it in the same manner regardless of whether the allowance is being determined at a high point or a low point in the economic cycle. Each quarter, our credit administration department identifies those loans to be individually evaluated for impairment and those to be collectively evaluated for impairment utilizing a standard criteria. We consistently use loss experience from the latest twelve quarters in determining the historical loss factor for each pool collectively evaluated for impairment. Qualitative factors are evaluated in the same manner each quarter and are adjusted within a relevant range of values based on current conditions to assure directional consistency of the allowance for loan loss account. Regulators, in reviewing the loan portfolio as part of the scope of a regulatory examination, may require us to increase our allowance for loan losses or take other actions that would require increases to our allowance for loan losses.

For a further discussion of our accounting policies for determining the amount of the allowance and a description of the systematic analysis and procedural discipline applied, refer to the note entitled, "Summary of significant accounting policies — Allowance for loan losses," in the Notes to Consolidated Financial Statements to this Annual Report.

A reconciliation of the allowance for loan losses including charge-offs and recoveries by major loan category for the past five years are summarized as follows:

Reconciliation of allowance for loan losses (Dollars in thousands)

December 31	2020	2019	2018	2017	2016
Allowance for loan losses at beginning of period	$ 22,677	$ 21,379	$ 18,960	$ 15,961	$ 12,975
Loans charged-off:					
Commercial	2,771	3,314	154	173	776
Real estate:					
Commercial	144	817	1,250	706	858
Residential	247	477	405	533	339
Consumer	317	459	545	737	495
Total	3,479	5,067	2,354	2,149	2,468
Loans recovered:					
Commercial	525	69	137	20	86
Real estate:					
Commercial	16	1	136	124	122
Residential	57	29	98	44	69
Consumer	148	166	202	160	177
Total	746	265	573	348	454
Net loans charged-off	2,733	4,802	1,781	1,801	2,014
Provision for loan losses	7,400	6,100	4,200	4,800	5,000
Allowance for loan losses at end of period	$ 27,344	$ 22,677	$ 21,379	$ 18,960	$ 15,961
Ratios:					
Net loans charged-off as a percentage of average loans outstanding	0.13 %	0.26 %	0.10 %	0.11 %	0.14 %
Allowance for loan losses as a percentage of period end loans	1.26 %	1.17 %	1.17 %	1.12 %	1.04 %

The allowance for loan losses increased $4.6 million to $27.3 million at December 31, 2020, from $22.7 million at the end of 2019. The increase resulted from a provision for loan losses of $7.4 million less net loans charged-off of $2.7 million. Changes made during the first six months of 2020 to the qualitative factors, which related to economic decline resulting from the adverse impact of the COVID-19 crisis, was the primary reason for the higher provision. Commercial loan charge-offs were $2.8 million and included a $1.1 partial write down of a specific credit relationship, which has been subsequently paid off in January 2021, a charge-off of $0.6 million to a specific commercial credit during the first quarter and $0.9 million related to a group of small business lines of credit in our Greater Delaware Valley market. Commercial loan recoveries increased $0.5 million and included $0.2 million related to the group of small business lines of credit in the Greater Delaware Valley market and $0.2 million on a separate credit. We charged-off $3.3 million of commercial loans in 2019 substantially all of which were in the fourth quarter. Included in this amount was $2.3 million related to certain small business lines of credit in our Greater Delaware Valley market and $1.0 million of other commercial loan relationships.

The allowance for loan losses, as a percentage of loans, net of unearned income, was 1.26 percent at the end of 2020, 1.17 percent at the end of 2019, respectively. Excluding PPP loans that do not carry an allowance for losses due to a 100 percent government guarantee, the ratio equaled 1.38 percent at December 31, 2020.

Past due loans not satisfied through repossession, foreclosure or related actions are evaluated individually to determine if all or part of the outstanding balance should be charged against the allowance for loan losses account. Any subsequent recoveries are credited to the allowance account. Net loans charged-off decreased $2.1 million to $2.7 million in 2020 from $4.8 million in 2019. Net charge-offs, as a percentage of average loans outstanding, equaled 0.13 percent in 2020 and 0.26 percent in 2019.

Allocation of the allowance for loan losses (Dollars in thousands)

The allocation of the allowance for loan losses for the past five years is summarized as follows:

	2020		2019		2018		2017		2016	
December 31	**Amount**	**%**	**Amount**	**%**	**Amount**	**%**	**Amount**	**%**	**Amount**	**%**
Specific:										
Commercial	$ 947	0.20 %	$ 363	0.24 %	$ 50	0.12 %	$ 159	0.15 %	$ 225	0.18 %
Real Estate:										
Commercial	180	0.18	279	0.16	403	0.17	263	0.25	1,197	0.47
Residential	75	0.07	135	0.11	666	0.23	336	0.22	520	0.23
Consumer					60	0.01	8	0.01		
Total specific	1,202	0.45	777	0.51	1,179	0.53	766	0.63	1,942	0.88
Formula:										
Commercial	7,787	30.99	6,525	26.74	5,466	26.98	4,893	27.98	3,574	26.49
Real Estate:										
Commercial	14,379	52.07	11,217	52.03	10,333	49.62	7,285	46.19	4,650	45.21
Residential	3,054	12.67	3,091	15.44	3,226	16.22	4,644	16.78	4,187	18.67
Consumer	922	3.82	1,067	5.28	1,175	6.65	1,372	8.42	1,608	8.75
Total formula	26,142	99.55	21,900	99.49	20,200	99.47	18,194	99.37	14,019	99.12
Total allowance	$ 27,344	100.00 %	$ 22,677	100.00 %	$ 21,379	100.00 %	$ 18,960	100.00 %	$ 15,961	100.00 %

The allowance for loan losses account increased $4.6 million to $27.3 million at December 31, 2020, compared to $22.7 million at December 31, 2019. The specific portion of the allowance for impairment of loans individually evaluated under FASB ASC 310 increased $0.4 million to $1.2 million at December 31, 2020, from $0.8 million at December 31, 2019 and the formula portion of the allowance for loans collectively evaluated for impairment under FASB ASC 450, increased $4.2 million to $26.1 million at December 31, 2020, from $21.9 million at December 31, 2019. The increase in the specific portion of the allowance was a result of a decrease in measured impairment for collateral dependent loans. The increase in the formula portion was primarily the result of a significant increase in volume and an increase in the historical loss factor for commercial loans, due to the increase in charge-offs during 2019.

The coverage ratio, the allowance for loan losses, as a percentage of nonperforming loans, is an industry ratio used to test the ability of the allowance account to absorb potential losses arising from nonperforming loans. The coverage ratio was 277.0 percent at December 31, 2020 and 225.0 percent at December 31, 2019. We believe that our allowance was adequate to absorb probable credit losses at December 31, 2020.

Deposits:

Our deposit base is the primary source of funds to support our operations. We offer a variety of deposit products to meet the needs of our individual and commercial customers. Total deposits grew $465.6 million or 23.6 percent to $2.4 billion at the end of 2020. The increase in deposits is due to organic growth in customer relationships throughout all our markets, higher customer savings rates, and PPP loan proceeds retained coupled with additional deposits by our commercial borrowers. Total deposits include $23.0 million of brokered certificates of deposit. Noninterest-bearing deposits grew $159.2 million or 34.4 percent while interest-bearing deposits increased $306.4 million or 20.3 percent in 2020. Noninterest-bearing deposits represented 25.5 percent of total deposits while interest-bearing deposits accounted for 74.5 percent of total deposits at December 31, 2020. Comparatively, noninterest-bearing deposits and interest-bearing deposits represented 23.5 percent and 76.5 percent of total deposits at year end 2019. With regard to noninterest-bearing deposits, personal checking accounts increased $61.1 million or 28.8 percent, while commercial checking accounts increased $98.6 million or 39.3 percent. The increase in noninterest-bearing deposits is essential in attempting to keep our overall cost of funds low given the pressure on our net interest margin from the decrease in short-term market rates.

With regard to interest-bearing deposits, interest-bearing transaction accounts, which include money market accounts and NOW accounts, and savings accounts, increased $356.2 million in 2020. Commercial interest-bearing transaction accounts increased $215.8 million, while personal interest-bearing transaction accounts increased $79.5 million. Savings accounts increased $61.0 million during 2020 as customers saved a higher percentage of the government stimulus in safe liquid accounts. The strong growth in our non-maturity deposits was due to continuing our strategic initiative to grow our public fund deposits and continued organic growth in all our markets. Total time deposits decreased $49.8 million to $319.7 million at December 31, 2020 from $369.5 million at December 31, 2019. The decrease was due to depositors shifting funds to more liquid accounts and the redemption of a few large municipal accounts.

The average amount of, and the rate paid on, the major classifications of deposits for the past three years are summarized as follows:

Deposit distribution (Dollars in thousands)

	2020		2019		2018	
Year ended December 31	**Average Balance**	**Average Rate**	**Average Balance**	**Average Rate**	**Average Balance**	**Average Rate**
Interest-bearing:						
Money market accounts	$ 432,621	0.81 %	$ 349,668	1.31 %	$ 296,331	0.86 %
NOW accounts	470,701	0.58	394,494	0.75	388,334	0.60
Savings accounts	404,628	0.12	380,175	0.13	389,557	0.13
Time deposits	355,030	1.40	367,666	1.90	291,499	1.36
Total interest-bearing	1,662,980	0.71 %	1,492,003	1.01 %	1,365,721	0.68 %
Noninterest-bearing	555,459		434,676		395,287	
Total deposits	$ 2,218,439		$ 1,926,679		$ 1,761,008	

Total deposits averaged $2.2 billion in 2020 and $1.9 billion in 2019, increasing $291.8 million or 15.1 percent comparing 2020 to 2019. Average noninterest-bearing deposits increased $120.8 million, while average interest-bearing accounts grew $171.0 million. Average interest-bearing transaction deposits, including money market and NOW, and savings accounts, increased $183.6 million while average total time deposits decreased $12.6 million when comparing 2020 and 2019.

Our cost of interest-bearing deposits decreased 30 basis points to 0.71 percent in 2020 from 1.01 percent in 2019. Specifically, the cost of money market accounts decreased 50 basis points to 0.81 percent from 1.31 percent, NOW accounts decreased 17 basis points and the cost of time deposits decreased 50 basis points to 1.40 percent comparing 2020 and 2019. The decreases to the cost of our interest-bearing deposits was the result of our initiative to reduce premium rates being paid on core deposit relationships and the reduction of stated rates across all deposit products. The reductions are directly related to the FOMC's decision to decrease the target federal funds rate 225 basis points from July

2019 to March 2020, first in response to economic slowdown and most recently due to the COVID-19 crisis. We expect our cost of funds to continue to decline as time deposits mature and reinvest into lower rates and we continue to lower all our interest-bearing deposit rates to mitigate compression to our net interest margin.

Volatile deposits, time deposits $100 or more, averaged $200.3 million in 2020, a decrease of $30.3 million or 13.2 percent from $230.6 million in 2019. Our average cost of these funds decreased 70 basis points to 1.46 percent in 2020, from 2.16 percent in 2019. This type of funding is susceptible to withdrawal by the depositor as they are particularly price sensitive and are therefore not considered to be a strong source of liquidity.

Maturities of time deposits $100 thousand or more, which entirely consist of certificates of deposits, for the past three years are summarized as follows:

Maturity distribution of time deposits $100 thousand or more (Dollars in thousands)

December 31	2020	2019	2018
Within three months	$ 41,569	$ 72,825	$ 27,659
After three months but within six months	65,863	80,707	21,546
After six months but within twelve months	53,660	46,582	48,904
After twelve months	50,997	56,144	124,933
Total	$ 212,089	$ 256,258	$ 223,042

In addition to deposit gathering, we have a secondary source of liquidity through existing credit arrangements with the FHLB-Pgh. During the first four months of 2020 we relied on this type of funding due to seasonal outflows of municipal deposits. As deposit balances surged during the final six months of 2020 due to government stimulus and increases in commercial and municipal accounts, short-term borrowings with the FHLB were paid down. At year end 2020, we maintained a high on-balance sheet liquidity position and expect limited utilization of the credit facility during 2021. For a further discussion of our borrowings and their terms, refer to the notes entitled, “Short-term borrowings” and “Long-term debt,” in the Notes to Consolidated Financial Statements included in Part II, Item 8 of this Annual Report.

Subordinated Debt:

On June 1, 2020, the Company sold $33,000 aggregate principal amount of Subordinated Notes due 2030 (the “2020 Notes”) to accredited investors. The 2020 Notes are intended to be treated as Tier 2 capital for regulatory capital purposes.

The 2020 Notes bear interest at a rate of 5.375% per year for the first five years and then float based on a benchmark rate (as defined), provided that the interest rate applicable to the outstanding principal balance during the period the 2020 Notes are floating will at no time be less the 4.75%. Interest will be payable semi-annually in arrears on June 1 and December 1 of each year, beginning on June 1, 2020, for the first five years after issuance and will be payable quarterly in arrears thereafter on March 1, June 1, September 1, and December 1. The 2020 Notes will mature on June 1, 2030 and are redeemable in whole or in part, without premium or penalty, at any time on or after June 1, 2025 and prior to June 1, 2030. Additionally, if all or any portion of the 2020 Notes cease to be deemed Tier 2 Capital, the Company may redeem, in whole and not in part, at any time upon giving not less than ten days’ notice, an amount equal to one hundred percent (100%) of the principal amount outstanding plus accrued but unpaid interest to but excluding the date fixed for redemption.

Holders of the 2020 Notes may not accelerate the maturity of the 2020 Notes, except upon the bankruptcy, insolvency, liquidation, receivership or similar proceeding by or against the Company.

Market Risk Sensitivity:

Market risk is the risk to our earnings and/or financial position resulting from adverse changes in market rates or prices, such as interest rates, foreign exchange rates or equity prices. Our exposure to market risk is primarily IRR associated with our lending, investing and deposit gathering activities. During the normal course of business, we are not exposed to foreign exchange risk or commodity price risk. Our exposure to IRR can be explained as the potential for change in our reported earnings and/or the market value of our net worth. Variations in interest rates affect the underlying economic value of our assets, liabilities and off-balance sheet items. These changes arise because the present value of future cash flows, and often the cash flows themselves, change with interest rates. The effects of the changes in these present values reflect the change in our underlying economic value, and provide a basis for the expected change in future earnings related to interest rates. Interest rate changes affect earnings by changing net interest income and the level of other interest-sensitive income and operating expenses. IRR is inherent in the role of banks as financial intermediaries. However, a bank with a high degree of IRR may experience lower earnings, impaired liquidity and capital positions, and most likely, a greater risk of insolvency. Therefore, banks must carefully evaluate IRR to promote safety and soundness in their activities.

The FOMC, in response to the uncertainty of the pandemic, cut the federal funds target rate 150 basis points during the first quarter of 2020 to a targeted range of 0.00 to 0.25 percent after the target rate 75 basis points during the second half of 2019 due to economic weakness. The timing and the magnitude of future monetary policy actions that will impact the current interest rate environment are uncertain. Given these conditions, IRR and the ability to effectively manage it, are extremely critical to both bank management and regulators. The FFIEC through its advisory guidance reiterates the importance of effective corporate governance, policies and procedures, risk measuring and monitoring systems, stress testing and internal controls related to the IRR exposure of depository institutions. According to the advisory, the bank regulators believe that the current financial market and economic conditions present significant risk management challenges to all financial institutions. Although the bank regulators recognize that some degree of IRR is inherent in banking, they expect institutions to have sound risk management practices in place to measure, monitor and control IRR exposure. The advisory states that the adequacy and effectiveness of an institution’s IRR management process and the level of IRR exposure are critical factors in the bank regulators’ evaluation of an institution’s sensitivity to changes in interest rates and capital adequacy. Material weaknesses in risk management processes or high levels of IRR exposure relative to capital will require corrective action. We believe our risk management practices with regard to IRR were suitable and adequate given the level of IRR exposure at December 31, 2020.

The Asset/Liability Committee (“ALCO”), comprised of members of our bank’s board of directors, senior management and other appropriate officers, oversees our IRR management program. Specifically, ALCO analyzes economic data and market interest rate trends, as well as competitive pressures, and utilizes several computerized modeling techniques to reveal potential exposure to IRR. This allows us to monitor and attempt to control the influence these factors may have on our rate sensitive assets (“RSA”), rate sensitive liabilities (“RSL”) and overall operating results and financial position.

With respect to evaluating our exposure to IRR on earnings, we utilize a gap analysis model that considers repricing frequencies of RSA and RSL. Gap analysis attempts to measure our interest rate exposure by calculating the net amount of RSA and RSL that reprice within specific time intervals. A positive gap occurs when the amount of RSA repricing in a specific period is greater than the amount of RSL repricing within that same time frame and is indicated by a RSA/RSL ratio greater than 1.0. A negative gap occurs when the amount of RSL repricing is greater than the amount of RSA and is indicated by a RSA/RSL ratio less than 1.0. A positive gap implies that earnings will be impacted favorably if interest rates rise and adversely if interest rates fall during the period. A negative gap tends to indicate that earnings will be affected inversely to interest rate changes.

Our interest rate sensitivity gap position, illustrating RSA and RSL at their related carrying values, is summarized as follows. The distributions in the table are based on a combination of maturities, call provisions, repricing frequencies and prepayment patterns. Adjustable-rate assets and liabilities are distributed based on the repricing frequency of the instrument. Mortgage instruments are distributed in accordance with estimated cash flows, assuming there is no change in the current interest rate environment.

Interest rate sensitivity (Dollars in thousands)

December 31, 2020	Due within three months	Due after three months but within twelve months	Due after one year but within five years	Due after five years	Total
Rate-sensitive assets:					
Interest-bearing deposits in other banks	$ 15,905				$ 15,905
Federal funds sold	183,000				183,000
Investment securities	15,008	$ 51,033	$ 121,014	$ 116,219	303,274
Total loans	768,837	320,990	882,966	205,189	2,177,982
Loans held for sale	837				837
Total rate-sensitive assets	$ 983,587	$ 372,023	$ 1,003,980	$ 321,408	$ 2,680,998
Rate-sensitive liabilities:					
Money market accounts	$ 496,634				$ 496,634
NOW accounts	201,833		$ 365,254		567,087
Savings accounts			431,224		431,224
Time deposits less than $100 thousand	13,223	$ 42,262	45,445	$ 6,674	107,604
Time deposits $100 thousand or more	41,569	119,523	45,948	5,049	212,089
Short-term borrowings	50,000				50,000
Long-term debt	526	11,615	2,628		14,769
Subordinated debt			33,000		33,000
Total rate-sensitive liabilities	$ 803,785	$ 173,400	$ 923,499	$ 11,723	$ 1,912,407
Rate-sensitivity gap:					
Period	$ 179,802	$ 198,623	$ 80,481	$ 309,685	
Cumulative	$ 179,802	$ 378,425	$ 458,906	$ 768,591	
RSA/RSL ratio:					
Period	1.22	2.15	1.09	27.42	
Cumulative	1.22	1.39	1.24	1.40	1.40

At December 31, 2020, we had cumulative one-year RSA/RSL ratio of 1.39, a positive gap. At December 31, 2019, we had cumulative one-year RSA/RSL of 0.98, a negative gap. As previously mentioned, a positive gap indicates that if interest rates increase, our earnings would likely be favorably impacted. Given the current economic conditions and the action of the FOMC to cut short-term rates to near zero during the first quarter of 2020 and their commitment to hold rates near zero for the foreseeable future, the focus of ALCO has been to maintain a well-balanced IRR position in order to safeguard future earnings during this historical low-rate environment and from potential risk to falling interest rates. During 2020 ALCO took steps to reduce our positive gap position and guard against rates unchanged or down through the origination of fixed rate loans and the investment in longer term, fixed rate municipal securities and longer duration U.S. government-sponsored mortgage-backed securities. Additionally, an initiative to reduce funding costs was executed to mitigate the adverse impact to net interest income from the low rates ALCO will continue to focus efforts on strategies in 2021 in an attempt to maintain a positive gap position between RSA and RSL. However, these forward-looking statements are qualified in the aforementioned section entitled "Forward-Looking Discussion" in this Management's Discussion and Analysis.

The change in our cumulative one-year ratio from the previous year-end resulted from a $427.4 million or 46.0 percent increase in RSA partially offset by a $30.6 million or 3.2 percent increase in RSL maturing or repricing within one year. The increase in RSA resulted primarily from a $247.7 million increase in total loans, net of unearned income, resulting from an increase in commercial lending, which primarily involves loans with adjustable-rate terms that reprice in the near term. An increase of $183.0 million in federal funds sold from a surge in non-maturity deposits and a cautious approach to adding longer term assets at historically low rates also resulted in the higher RSA when comparing 2020 to 2019.

With respect to the $30.6 million increase in RSL maturing or repricing within a twelve month time horizon, non-maturity deposits increased $181.0 million due to customers seeking liquid accounts and saving at a higher percentage due to the economic uncertainty of the pandemic. The growth in deposits resulted in lower short-term borrowings of $102.1 million. Time deposits $100 thousand or more also declined when comparing year end 2020 to 2019 as a number of large accounts matured and customers sought more liquid alternatives.

Static gap analysis, although a credible measuring tool, does not fully illustrate the impact of interest rate changes on future earnings. First, market rate changes normally do not equally or simultaneously affect all categories of assets and liabilities. Second, assets and liabilities that can contractually reprice within the same period may not do so at the same time or to the same magnitude. Third, the interest rate sensitivity table presents a one-day position and variations occur daily as we adjust our rate sensitivity throughout the year. Finally, assumptions must be made in constructing such a table. For example, the conservative nature of our Asset/Liability Management Policy assigns personal NOW accounts to the “Due after three months but within twelve months” repricing interval. In reality, these accounts may reprice less frequently and in different magnitudes than changes in general market interest rate levels.

We utilize a simulation model to address the failure of the static gap model to address the dynamic changes in the balance sheet composition or prevailing interest rates and to enhance our asset/liability management. This model creates pro forma net interest income scenarios under various interest rate shocks. Given instantaneous and parallel shifts in general market rates of plus 100 basis points, our projected net interest income for the 12 months ending December 31, 2021, would increase at 4.3 percent from model results using current interest rates.

We will continue to monitor our IRR position in 2021 and anticipate employing deposit and loan pricing strategies and directing the reinvestment of loan and investment payments and prepayments in order to maintain our target IRR position.

Financial institutions are affected differently by inflation than commercial and industrial companies that have significant investments in fixed assets and inventories. Most of our assets are monetary in nature and change correspondingly with variations in the inflation rate. It is difficult to precisely measure the impact inflation has on us, however, we believe that our exposure to inflation can be mitigated through our asset/liability management program.

Liquidity:

Liquidity management is essential to our continuing operations as it gives us the ability to meet our financial obligations as they come due, as well as to take advantage of new business opportunities as they arise. Our financial obligations include, but are not limited to, the following:

- Funding new and existing loan commitments;
- Payment of deposits on demand or at their contractual maturity;
- Repayment of borrowings as they mature;
- Payment of lease obligations; and
- Payment of operating expenses.

Our liquidity position is impacted by several factors which include, among others, loan origination volumes, loan and investment maturity structure and cash flows, demand for core deposits and certificate of deposit maturity structure and retention. We manage these liquidity risks daily, thus enabling us to monitor fluctuations in our position and to adapt our position according to market influence and balance sheet trends. We also forecast future liquidity needs and develop strategies to ensure adequate liquidity at all times.

Historically, core deposits have been our primary source of liquidity because of their stability and lower cost, in general, than other types of funding. Providing additional sources of funds are loan and investment payments and prepayments and the ability to sell both available-for-sale securities and mortgage loans held for sale. As a final source of liquidity, we have available borrowing arrangements with various financial intermediaries, including the FHLB-Pgh. At December 31, 2020, our maximum borrowing capacity with the FHLB-Pgh was $807.0 million of which $64.8 million was outstanding in borrowings and $218.4 million outstanding in the form of irrevocable standby letters of credit. We believe our liquidity is adequate to meet both present and future financial obligations and commitments on a timely basis.

We maintain a contingency funding plan to address liquidity in the event of a funding crisis. Examples of some of the causes of a liquidity crisis include, among others, natural disasters, pandemics, war, events causing reputational harm and severe and prolonged asset quality problems. The plan recognizes the need to provide alternative funding sources in times of crisis that go beyond our core deposit base. As a result, we have created a funding program that ensures the availability of various alternative wholesale funding sources that can be used whenever appropriate. Identified alternative funding sources include:

- FHLB-Pgh liquidity contingency line of credit;
- Federal Reserve discount window;
- Internet certificates of deposit;
- Brokered deposits;
- Institutional Deposit Corporation deposits;
- Repurchase agreements; and
- Federal funds purchased.

We have increased our borrowing capacity at the Federal Reserve by establishing a borrower-in-custody of collateral arrangement that enables us to pledge certain loans, not being used as collateral at the FHLB-Pgh, as collateral for borrowings at the Federal Reserve. At December 31, 2020 our borrowing capacity at the Federal Reserve related to this program was $156.6 million and there were no amounts outstanding. Additionally, we may utilize the Federal Reserve's Paycheck Protection Program Liquidity Facility ("PPPLF") by pledging PPP loans as collateral. At December 31, 2020, $189.7 million would be available to borrow for a term equal to the maturity date of the loan pledged. However, no new extensions of credit will be made under the PPPLF after March 31, 2021 unless the Federal Reserve Board and the Department of Treasury determine to extend the PPPLF. There are no amounts outstanding under the PPPLF at December 31, 2020.

Based on our liquidity position at December 31, 2020, we do not anticipate the need to utilize any of these sources in the near term.

We employ a number of analytical techniques in assessing the adequacy of our liquidity position. One such technique is the use of ratio analysis to illustrate our reliance on noncore funds to fund our investments and loans maturing after 2020. At December 31, 2020, our noncore funds consisted of time deposits in denominations of $100 thousand or more, short-term borrowings, and long-term and subordinated debt. Large denomination time deposits are particularly not considered to be a strong source of liquidity since they are very interest rate sensitive and are considered to be highly volatile. At December 31, 2020, our net noncore funding dependence ratio, the difference between noncore funds and short-term investments to long-term assets, was 2.8 percent. Our net short-term noncore funding dependence ratio, noncore funds maturing within one year, less short-term investments to long-term assets equaled negative 1.3 percent due to our short-term investments being greater than the non-core funding. Comparatively, our ratios equaled 17.8 percent and 14.4 percent at the end of 2019, which indicates a significant decrease in our reliance on noncore funds in 2020. Moreover, our basic liquidity surplus ratio, defined as liquid assets less short-term potentially volatile liabilities as a percentage of total assets, increased to 8.7 percent at December 31, 2020, from 5.7 percent at December 31, 2019. We believe that by supplying adequate volumes of short-term investments and implementing competitive pricing strategies on deposits, we can ensure adequate liquidity to support future growth.

The Consolidated Statements of Cash Flows present the change in cash and cash equivalents from operating, investing and financing activities. Cash and cash equivalents consist of cash on hand, cash items in the process of collection, noninterest-bearing and interest-bearing deposits with other banks and federal funds sold. Cash and cash equivalents increased $197.0 million for the year ended December 31, 2020. For the year ended December 31, 2019, cash and cash equivalents decreased $1.5 million. During 2020, cash provided by operating and financing activities more than offset cash used in investing activities.

Operating activities provided net cash of $37.2 million in 2020 and $37.1 million in 2019. Net income, adjusted for the effects of noncash expenses such as depreciation, amortization and accretion of tangible and intangible assets and investment securities, and the provision for loan losses, is the primary source of funds from operations.

Net cash provided by financing activities equaled $361.1 million in 2020. Net cash provided by financing activities was $146.2 million in 2019. Deposit gathering, which is our predominant financing activity, increased in both 2020 and 2019. Deposit gathering provided a net cash inflow in 2020 of $465.6 million and $96.5 million in 2019. Short-term borrowings decreased net cash by $102.2 million in 2020 while a net increase in short-term borrowings of $65.6 million increased net cash provided by financing activities in 2019. Deposit gathering in 2020 was also partially offset by a $18.0 million net decrease in long-term debt as well as cash dividends paid of $10.5 million. The issuance of $33.0 million of subordinated debt in 2020 also contributed to the increase. In 2019, deposit gathering was partially offset by a net $5.2 million repayments of long-term debt and cash dividends paid of $10.1 million.

Our primary investing activities involve transactions related to our investment and loan portfolios. Net cash used in investing activities totaled $201.2 million in 2020. Net cash used in investing activities was $184.7 million in 2019. Net cash used in lending activities was $241.3 million in 2020, an increase from $120.0 million in 2019. Activities related to our investment portfolio provided net cash of $43.0 million in 2020 and used cash of $56.6 million in 2019.

We anticipate maintaining a relatively stable liquidity position in 2021. Our continued growth in the expanding Lehigh Valley and King of Prussia markets coupled with our maturing Lebanon County office and expected growth in Doylestown, Bucks County is expected to produce strong loan demand throughout 2021. We expect to fund such demand through deposit gathering initiatives, payments and prepayments on loans and investments and advances from the FHLB. Moreover, if economic conditions were to weaken, as they did during 2020, it may result in increased interest in bank deposits, as consumers seek safety for their balances. However, we cannot predict the economic climate or the savings habits of consumers. Should economic conditions continue to improve, deposit gathering may be negatively impacted as depositors seek alternative investments or increase spending. Regardless of economic conditions and stock market fluctuations, we believe that through constant monitoring and adherence to our liquidity plan, we will have the means to provide adequate cash to fund our normal operations in 2021.

Capital Adequacy:

We believe a strong capital position is essential to our continued growth and profitability. We strive to maintain a relatively high level of capital to provide our depositors and stockholders with a margin of safety. In addition, a strong capital base allows us to take advantage of profitable opportunities, support future growth and provide protection against any unforeseen losses.

Our ALCO reviews our capital position, generally, quarterly. As part of its review, the ALCO considers: (i) the current and expected capital requirements, including the maintenance of capital ratios in excess of minimum regulatory guidelines; (ii) potential changes in the market value of our securities due to interest rates changes and effect on capital; (iii) projected organic and inorganic asset growth; (iv) the anticipated level of net earnings and capital position, taking into account the projected asset/liability position and exposure to changes in interest rates; (v) significant deteriorations in asset quality; and (vi) the source and timing of additional funds to fulfill future capital requirements.

Based on the recent regulatory emphasis placed on banks to assure capital adequacy, our board of directors annually reviews and approves a capital plan. Among other specific objectives, this comprehensive plan: (i) attempts to ensure that we and Peoples Bank remain well capitalized under the regulatory framework for prompt corrective action; (ii) evaluates our capital adequacy exposure through a comprehensive risk assessment; (iii) incorporates periodic stress testing in accordance with the Federal Reserve Board's Supervisory Capital Assessment Program ("SCAP"); (iv) establishes event triggers and action plans to ensure capital adequacy; and (v) identifies realistic and readily available alternative sources for augmenting capital if higher capital levels are required.

Bank regulatory agencies consider capital to be a significant factor in ensuring the safety of a depositor's accounts. These agencies have adopted minimum capital adequacy requirements that include mandatory and discretionary supervisory actions for noncompliance. Our and Peoples Bank's risk-based capital ratios are strong and have consistently exceeded the minimum regulatory capital ratios required for adequately capitalized institutions. Our ratio of Tier 1 capital to risk-weighted assets and off-balance sheet items was 12.2 percent and 11.9 percent at December 31, 2020 and 2019, respectively. Our Total capital ratio was 15.1 percent and 13.0 percent at December 31, 2020 and 2019, respectively. The increase in the total capital ratio is due to the issuance of $33.0 million of subordinated debt which qualified as Tier 2 capital. Our and Peoples Bank's common equity Tier I capital to risk-weighted assets ratios were 12.2 percent and 13.7 percent at December 31, 2020 and 11.9 percent and 11.6 percent at December 31, 2019. Our Leverage ratio, which equaled 9.3 percent at December 31, 2020 and 10.1 percent at December 31, 2019, exceeded the minimum of 4.0 percent for capital adequacy purposes. Peoples Bank reported Tier 1 capital, Total capital and Leverage ratios of 13.7 percent, 15.0 percent and 10.1 percent at December 31, 2020, and 11.6 percent, 12.8 percent and 9.9 percent at December 31, 2019. Based on the most recent notification from the FDIC, Peoples Bank was categorized as well capitalized at December 31, 2020. There are no conditions or events since this notification that we believe have changed Peoples Bank's category. For a further discussion of these risk-based capital standards and supervisory actions for noncompliance, refer to the note entitled, "Regulatory matters," in the Notes to Consolidated Financial Statements to this Annual Report.

Stockholders' equity was $316.9 million or $43.92 per share at December 31, 2020, and $299.0 million or $40.47 per share at December 31, 2019. Stockholders' equity grew $17.9 million in 2020 as net income and a decrease in accumulated other comprehensive loss offset the payment of dividends and the Company's repurchase of its shares.

We declared dividends of $1.44 per share in 2020, $1.37 per share in 2019, and $1.31 per share in 2018. The dividend payout ratio, dividends declared as a percent of net income, equaled 35.8 percent in 2020, 39.4 percent in 2019 and 38.9 percent in 2018. Our board of directors intends to continue paying cash dividends in the future and has declared a cash dividend in the first quarter of 2021 of $0.37 per share. Our ability to declare and pay dividends in the future is based on our operating results, financial and economic conditions, capital and growth objectives, dividend restrictions and other relevant factors. We rely on dividends received from our subsidiary, Peoples Bank, for payment of dividends to stockholders. Peoples Bank's ability to pay dividends is subject to federal and state regulations. For a further discussion on our ability to declare and pay dividends in the future and dividend restrictions, refer to the note entitled, "Regulatory matters," in the Notes to Consolidated Financial Statements included in Part II, Item 8 of this Annual Report.

Since 2014, our Board of Directors has adopted various common stock repurchase plans whereby we were authorized to repurchase shares of our outstanding common stock through open market purchases. During 2020 we repurchased and retired 181,417 shares for $6.9 million under the then current plan. We purchased and retired 14,428 shares for $0.6 million during 2019. There were no shares purchased or retired in 2018.

Review of Financial Performance:

Net income totaled $29.4 million or $4.00 per diluted share in 2020 an increase of 14.1% when compared to $25.7 million or $3.47 per diluted share in 2019. The increase in earnings in 2020 is the result of higher pre-provision net interest income of $4.3 million due primarily to lower funding costs, higher noninterest income of $1.5 million and lower noninterest expense of $0.7 million which were partially offset by an increase of $1.3 million to the provision for loan losses and a $1.7 million increase to the income tax provision. The results for 2020 include a $0.9 million net gain on the sale of debt securities included in noninterest income. Return on average assets ("ROAA") and return on average equity

("ROAE") were 1.09 percent and 9.48 percent for the year ended December 31, 2020. ROAA was 1.10 percent and ROAE was 8.87 percent for the year ended December 31, 2019.

Tax-equivalent net interest income, a non-GAAP measure, was $81.1 million in 2020 and $77.2 million in 2019. Our net interest margin equaled 3.25 percent in 2020 and 3.58 percent in 2019. Noninterest income totaled $16.6 million in 2020 and $15.1 million in 2019. Noninterest expense was $54.9 million for the year ended December 31, 2020 compared to $55.6 million for the year ended December 31, 2019. Our productivity is measured by the operating efficiency ratio, a non-GAAP measure, defined as noninterest expense less amortization of intangible assets divided by the total of tax-equivalent net interest income and noninterest income. Our operating efficiency ratio was 56.0 percent in 2020 and 59.6 percent in 2019.

Non-GAAP Financial Measures (Dollars in thousands)

The following are non-GAAP financial measures which provide useful insight to the reader of the consolidated financial statements but should be supplemental to GAAP used to prepare Peoples' financial statements and should not be read in isolation or relied upon as a substitute for GAAP measures. In addition, Peoples' non-GAAP measures may not be comparable to non-GAAP measures of other companies. The tax rate used to calculate the fully-taxable equivalent (FTE) adjustment was 21% for 2020, 2019, and 2018.

The following table reconciles the non-GAAP financial measures of FTE net interest income for the years ended 2020, 2019 and 2018:

Year ended December 31	2020	2019	2018
Interest income (GAAP)	$ 94,125	$ 93,381	$ 84,661
Adjustment to FTE	1,306	1,644	1,672
Interest income adjusted to FTE (non-GAAP)	95,431	95,025	86,333
Interest expense	14,324	17,868	13,322
Net interest income adjusted to FTE (non-GAAP)	$ 81,107	$ 77,157	$ 73,011

The efficiency ratio is noninterest expenses, less amortization of intangible assets, as a percentage of FTE net interest income plus noninterest income less gains on equity securities and gains on sale of assets. The following table reconciles the non-GAAP financial measures of the efficiency ratio to GAAP for the years ended 2020, 2019, and 2018:

Year ended December 31	2020	2019	2018
Efficiency ratio (non-GAAP):			
Noninterest expense (GAAP)	$ 54,868	$ 55,642	$ 52,487
Less: amortization of intangible assets expense	606	730	881
Noninterest expense adjusted for amortization of assets expense (non-GAAP)	54,262	54,912	51,606
Net interest income (GAAP)	79,801	75,513	71,339
Plus: taxable equivalent adjustment	1,306	1,644	1,672
Noninterest income (GAAP)	16,642	15,120	13,659
Less: net gains (losses) on equity securities	(6)	132	
Less: net gains on sale of assets	918	23	291
Net interest income (FTE) plus noninterest income (non-GAAP)	$ 96,837	$ 92,122	$ 86,379
Efficiency ratio (non-GAAP)	56.0 %	59.6 %	59.7 %

Net Interest Income:

Net interest income is the fundamental source of earnings for commercial banks. Moreover, fluctuations in the level of net interest income can have the greatest impact on net profits. Net interest income is defined as the difference between interest revenue, interest and fees earned on interest-earning assets, and interest expense, the cost of interest-bearing liabilities supporting those assets. The primary sources of earning assets are loans and investment securities, while interest-bearing deposits and borrowings comprise interest-bearing liabilities. Net interest income is impacted by:

- Variations in the volume, rate and composition of earning assets and interest-bearing liabilities;

- Changes in general market interest rates; and

- The level of nonperforming assets.

Changes in net interest income are measured by the net interest spread and net interest margin. Net interest spread, the difference between the average yield earned on earning assets and the average rate incurred on interest-bearing liabilities, illustrates the effects changing interest rates have on profitability. Net interest margin, net interest income as a percentage of average earning assets, is a more comprehensive ratio, as it reflects not only the spread, but also the change in the composition of interest-earning assets and interest-bearing liabilities. Tax-exempt loans and investments carry pretax yields lower than their taxable counterparts. Therefore, in order to make the net interest margin analysis more comparable, tax-exempt income and yields are reported in this analysis on a tax-equivalent basis using the prevailing federal statutory tax rate.

Similar to all banks, we consider the maintenance of an adequate net interest margin to be of primary concern. The current economic environment has been very challenging for the banking industry given the adverse impact of the pandemic and interest rates at historical lows. In addition to market rates and competition, nonperforming asset levels are of particular concern for the banking industry and may place additional pressure on net interest margins. Nonperforming assets may stabilize or worsen given the uncertainty of the national and global economies, particularly the labor markets. No assurance can be given as to how general market conditions will change or how such changes will affect net interest income. Therefore, we believe through prudent deposit and loan pricing practices, careful investing, and constant monitoring of nonperforming assets, our net interest margin will remain strong.

We analyze interest income and interest expense by segregating rate and volume components of earning assets and interest-bearing liabilities. The impact changes in the interest rates earned and paid on assets and liabilities, along with changes in the volumes of earning assets and interest-bearing liabilities, have on net interest income are summarized as follows. The net change or mix component, attributable to the combined impact of rate and volume changes within earning assets and interest-bearing liabilities' categories, has been allocated proportionately to the change due to rate and the change due to volume.

Net interest income changes due to rate and volume (Dollars in thousands)

	2020 vs 2019 Increase (decrease) attributable to			2019 vs 2018 Increase (decrease) attributable to		
	Total	Rate	Volume	Total	Rate	Volume
Interest income:						
Loans:						
Taxable	$ 1,195	$ (10,883)	$ 12,078	$ 8,136	$ 3,469	$ 4,667
Tax-exempt	(725)	(187)	(538)	813	320	493
Investments:						
Taxable	904	(111)	1,015	505	22	483
Tax-exempt	(886)	203	(1,089)	(941)	(202)	(739)
Interest-bearing deposits	(26)	(98)	72	57	1	56
Federal funds sold	(56)	(216)	160	122		122
Total interest income	406	(11,292)	11,698	8,692	3,610	5,082
Interest expense:						
Money market accounts	(1,073)	(2,001)	928	2,028	1,507	521
NOW accounts	(200)	(710)	510	609	571	38
Savings accounts	8	(23)	31	9	21	(12)
Time deposits less than $100	71	(174)	245	276	368	(92)
Time deposits $100 or more	(2,062)	(1,468)	(594)	2,727	1,143	1,584
Short-term borrowings	(794)	(1,220)	426	(1,096)	617	(1,713)
Long-term debt	(529)	(366)	(163)	(7)	71	(78)
Subordinated debt	1,035		1,035			
Total interest expense	(3,544)	(5,962)	2,418	4,546	4,298	248
Net interest income - non-GAAP	$ 3,950	$ (5,330)	$ 9,280	$ 4,146	$ (688)	$ 4,834

Tax-equivalent net interest income, a non-GAAP measure, was $81.1 million in 2020 and $77.2 million in 2019. Interest and net fees earned on the PPP loans totaled $3.8 million in 2020. There was a positive volume variance that was partially offset by a negative rate variance. The growth in average earning assets exceeded that of interest-bearing liabilities, and resulted in additional tax-equivalent net interest income, a non-GAAP measure, of $9.3 million. A rate variance resulted in a decrease in net interest income of $5.3 million as assets repriced quicker than liabilities.

Average earning assets increased $340.6 million to $2.5 billion in 2020 from $2.2 billion in 2019 and accounted for a $11.7 million increase in interest income. Average loans, net increased $257.5 million, including $148.3 million of PPP loans, which caused interest income to increase $11.5 million. Average taxable investments increased $46.3 million comparing 2020 and 2019, which resulted in increased interest income of $1.0 million while average tax-exempt investments decreased $33.1 million, which resulted in a decrease to interest income of $1.1 million.

Average interest-bearing liabilities grew $204.4 million to $1.8 billion in 2020 from $1.6 billion in 2019 resulting in a net increase in interest expense of $2.4 million. Large denomination time deposits averaged $30.3 million less in 2020 and caused interest expense to decrease $0.6 million. An increase of $17.7 million in average time deposits less than $100 thousand increased interest expense by $0.2 million. In addition, interest-bearing transaction accounts, including money market, NOW and savings accounts grew $183.6 million, which in aggregate caused a $1.5 million increase in interest expense. Short-term borrowings averaged $20.8 million more and increased interest expense $0.4 million while long-term debt averaged $6.7 million less and decreased interest expense by $0.2 million comparing 2020 and 2019. The issuance of $33.0 million of subordinated debt during June 2020 caused interest expense to increase $1.0 million.

An unfavorable rate variance occurred, as the tax-equivalent yield on earning assets decreased 59 basis points while there was a 33 basis point decrease in the cost of funds. As a result, tax-equivalent net interest income decreased $5.3 million comparing 2020 and 2019. The tax-equivalent yield on earning assets was 3.82 percent in 2020 compared to 4.41 percent in 2019 resulting in a decrease in interest income of $11.3 million. With the tax-equivalent yield on the investment portfolio decreasing 11 basis points to 2.36 percent in 2020 from 2.47 percent in 2019, interest income decreased $0.1 million. The tax-equivalent yield on the loan portfolio decreased 55 basis points to 4.16 percent in 2020 from 4.71 percent in 2019 and resulted in a decrease to interest income of $11.1 million.

A favorable rate variance was experienced in the cost of funds. We experienced decreases in the rates paid on all major categories of interest-bearing liabilities. Specifically, the cost of money market and NOW accounts decreased 50 basis points and 17 basis points comparing 2020 and 2019. These decreases resulted in a decrease in interest expense of $2.7 million. With regard to time deposits, the average rate paid for time deposits less than $100 thousand decreased 13 basis points while time deposits $100 thousand or more decreased 70 basis points, which together resulted in a $1.6 million decrease in interest expense. The average rate paid on short-term borrowings decreased 160 basis points in 2020 when compared to 2019, causing a $1.2 million decrease in interest expense. Interest expense decreased $0.4 million from a 90 basis point decrease in the average rate paid on long-term debt.

The average balances of assets and liabilities, corresponding interest income and expense and resulting average yields or rates paid are summarized as follows. Averages for earning assets include nonaccrual loans. Investment averages include available-for-sale securities at amortized cost. Income on investment securities and loans is adjusted to a tax-equivalent basis, a non-GAAP measure, using the prevailing federal statutory tax rate of 21.0 percent in 2020, 2019 and 2018.

Summary of net interest income (Dollars in thousands)

	2020			2019		
	Average Balance	Interest Income/ Expense	Average Interest Rate	Average Balance	Interest Income/ Expense	Average Interest Rate
Assets:						
Earning assets:						
Loans:						
Taxable	$ 1,998,178	$ 83,683	4.19 %	$ 1,726,582	$ 82,488	4.78 %
Tax-exempt	124,898	4,729	3.79	138,975	5,454	3.92
Investments:						
Taxable	248,059	5,423	2.19	201,743	4,519	2.24
Tax-exempt	44,607	1,491	3.34	77,693	2,377	3.06
Interest-bearing deposits	17,288	39	0.23	3,493	65	1.86
Federal funds sold	62,072	66	0.11	6,023	122	2.03
Total interest earning assets	2,495,102	95,431	3.82 %	2,154,509	95,025	4.41 %
Less: allowance for loan losses	25,848			22,145		
Other assets	227,695			212,989		
Total assets	$ 2,696,949			$ 2,345,353		
Liabilities and Stockholders' Equity:						
Interest-bearing liabilities:						
Money market accounts	$ 432,621	3,510	0.81 %	$ 349,668	4,583	1.31 %
NOW accounts	470,701	2,741	0.58	394,494	2,941	0.75
Savings accounts	404,628	504	0.12	380,175	496	0.13
Time deposits less than $100	154,772	2,066	1.33	137,059	1,995	1.46
Time deposits $100 or more	200,258	2,918	1.46	230,607	4,980	2.16
Short-term borrowings	83,716	848	1.01	62,941	1,642	2.61
Long-term debt	38,560	702	1.82	45,253	1,231	2.72
Subordinated debt	19,295	1,035	5.36			
Total interest-bearing liabilities	1,804,551	14,324	0.79 %	1,600,197	17,868	1.12 %
Noninterest-bearing deposits	555,459			434,676		
Other liabilities	27,389			20,290		
Stockholders' equity	309,550			290,190		
Total liabilities and stockholders' equity	$ 2,696,949			$ 2,345,353		
Net interest income/spread (non-GAAP)		$ 81,107	3.03 %		$ 77,157	3.29 %
Net interest margin			3.25 %			3.58 %
Tax-equivalent adjustments:						
Loans		$ 993			$ 1,145	
Investments		313			499	
Total adjustments		$ 1,306			$ 1,644	

Note: Average balances were calculated using average daily balances. Interest income on loans includes fees of $3,833 in 2020, $1,622 in 2019 and $1,528 in 2018. The increase in 2020 is primarily due to net fees from PPP loans.

	2018		
(Dollars in thousands)	**Average Balance**	**Interest Income/ Expense**	**Average Interest Rate**
Assets:			
Earning assets:			
Loans:			
Taxable	$ 1,627,062	$ 74,352	4.57 %
Tax-exempt	126,088	4,641	3.68
Investments:			
Taxable	180,182	4,014	2.23
Tax-exempt	101,475	3,318	3.27
Interest-bearing deposits	478	8	1.67
Federal funds sold			
Total interest earning assets	2,035,285	86,333	4.24 %
Less: allowance for loan losses	20,013		
Other assets	213,617		
Total assets	$ 2,228,889		
Liabilities and Stockholders' Equity:			
Interest-bearing liabilities:			
Money market accounts	$ 296,331	2,555	0.86 %
NOW accounts	388,334	2,332	0.60
Savings accounts	389,557	487	0.13
Time deposits less than $100	144,445	1,719	1.19
Time deposits $100 or more	147,054	2,253	1.53
Short-term borrowings	133,834	2,738	2.05
Long-term debt	48,189	1,238	2.57
Total interest-bearing liabilities	1,547,744	13,322	0.86 %
Noninterest-bearing deposits	395,287		
Other liabilities	15,202		
Stockholders' equity	270,656		
Total liabilities and stockholders' equity	$ 2,228,889		
Net interest income/spread		$ 73,011	3.38 %
Net interest margin (non-GAAP)			3.59 %
Tax-equivalent adjustments:			
Loans		$ 975	
Investments		697	
Total adjustments		$ 1,672	

Provision for Loan Losses:

We evaluate the adequacy of the allowance for loan losses account on a quarterly basis utilizing our systematic analysis in accordance with procedural discipline. We take into consideration certain factors such as composition of the loan portfolio, volume of nonperforming loans, volumes of net charge-offs, prevailing economic conditions and other relevant factors when determining the adequacy of the allowance for loan losses account. We make monthly provisions to the allowance for loan losses account in order to maintain the allowance at an appropriate level. The provision for loan losses equaled $7.4 million in 2020 and $6.1 million in 2019. The higher provision for loan losses in 2020 resulted from changes made during the first six months to the qualitative factors, which related to economic decline resulting from the adverse impact of the COVID-19 crisis. Based on our most recent evaluation at

December 31, 2020, we believe that the allowance was adequate to absorb any known or potential losses in our portfolio as of such date.

Noninterest Income:

Our noninterest income increased $1.5 million or 10.1 percent to $16.6 million in 2020 from $15.1 million in 2019. The increase in 2020 was driven primarily by higher mortgage banking revenue of $1.0 million due to increased refinance activity from low market rates which resulted in higher volume of loans sold into the secondary market. We also realized a $0.9 million net gain on the sale of investment securities in 2020 while the 2019 results included gains of $0.2 million. Commercial loan interest rate swap revenue was higher by $0.5 million due to an increased number and volume of transactions during 2020 compared to 2019. Service charges, fees and commissions decreased $0.4 million due to lower service charges on consumer and commercial deposit accounts of $0.8 million from a noticeable reduction in transaction volumes related to COVID-19. Bank owned life insurance (BOLI) death benefit proceeds included in service charges, fees and commissions for 2020 totaling $0.6 million partially offset the reduction. Merchant revenue declined $0.1 million or 15.3% and wealth management revenue declined $0.2 million or 15.9% due to lower transaction volumes in part to COVID-19.

Noninterest Expense:

In general, our noninterest expense is categorized into three main groups, including employee-related expense, occupancy and equipment expense and other expenses. Employee-related expenses are costs associated with providing salaries, including payroll taxes and benefits to our employees. Occupancy and equipment expenses, the costs related to the maintenance of facilities and equipment, include depreciation, general maintenance and repairs, real estate taxes, rental expense offset by any rental income and utility costs. Other expenses include general operating expenses such as marketing, other taxes, stationery and supplies, contractual services, insurance, including FDIC assessment and loan collection costs. Several of these costs and expenses are variable while the remainder is fixed. We utilize budgets and other related strategies in an effort to control the variable expenses.

The major components of noninterest expense for the past three years are summarized as follows:

Noninterest expense (Dollars in thousands)

Year ended December 31	2020	2019	2018
Salaries and employee benefits expense:			
Salaries and payroll taxes	$ 24,912	$ 25,930	$ 23,557
Employee benefits	5,223	5,444	4,850
Salaries and employee benefits expense	30,135	31,374	28,407
Occupancy and equipment expenses:			
Occupancy expense	5,960	5,994	6,236
Equipment expense	6,880	5,917	4,661
Occupancy and equipment expenses	12,840	11,911	10,897
Other expenses:			
Merchant transaction expense	4	3	9
FDIC insurance and assessments	873	651	1,093
Professional fees and outside services	2,091	1,758	2,414
Other taxes	990	968	619
Stationery and supplies	697	753	773
Advertising	463	873	720
Amortization of intangible assets	606	730	881
Donations	1,357	1,441	1,339
Other	4,812	5,180	5,335
Other expenses	11,893	12,357	13,183
Total noninterest expense	$ 54,868	$ 55,642	$ 52,487

Salaries and employee benefits expense constitute the majority of our noninterest expenses accounting for 54.9 percent of the total noninterest expense. Salaries and employee benefits expense decreased $1.2 million or 3.9 percent to $30.1 million in 2020 from $31.4 million in 2019. Salaries and payroll taxes decreased $1.0 million or 3.9 percent and employee benefits expense decreased $0.2 million or 4.1 percent. The lower salary expense in 2020 was primarily due to deferred loan origination cost benefit which increased $1.4 million due to our origination of PPP loans in 2020. This higher benefit was partially offset by increases due to annual performance-based salary adjustments and additional lending professionals in our expansion markets. Employee benefits expense was lower due to lower health insurance costs and lower pension expense.

Occupancy and equipment expense increased $0.9 million or 7.8 percent to $12.8 million in 2020 from $11.9 million in 2019 due specifically to a 16.3 percent increase in equipment expense. The increase in equipment-related expenses was due in part to an investment in a software solution to streamline our PPP loan origination process, additional computer hardware to enable a larger percentage of our workforce to work remotely, and an investment in a new mobile/digital banking solution.

Other expenses, which consist of merchant transaction expense, FDIC insurance and assessments, professional fees and outside services, other taxes, stationary and supplies, advertising, amortization of intangible assets and all other expenses were $11.9 million in 2020 and $12.4 million in 2019. FDIC insurance and assessments was higher by $0.2 million or 34.1 percent primarily attributed to the receipt of a credit in 2019 related to the Deposit Insurance Fund's (DIF) minimum reserve ratio assessment. Professional fees and outside services increased $0.3 million due to legal work related to loan workouts and PPP loans. Advertising expenses decreased $0.4 million and other expenses, which include employee education, travel and entertainment expenses, decreased $0.4 million due to COVID-19.

Income Taxes:

Our income tax expense was $4.8 million in 2020 and $3.2 million in 2019. We utilize loans and investments of tax-exempt organizations to mitigate our tax burden, as interest revenue from these sources is not taxable by the federal government. As a result, our effective tax rate was 14.1 percent in 2020 and 10.9 percent in 2019.

The effective tax rate in 2020 and 2019 was also influenced by the recognition of investment tax credits related to our limited partnership investments in elderly and low- to- moderate-income residential housing programs which allow us to mitigate our tax burden. By utilizing these credits, we reduced our income tax expense by $1.1 million in both 2020 and 2019. We anticipate investment tax credits from these investments to be $1.1 million again in 2021. Over the next five years, we will recognize aggregate tax credits from our investments in these projects of $3.4 million.

Management's Discussion and Analysis 2019 versus 2018
(Dollars in thousands, except per share data)

Operating Environment:

The United States economy continued to show signs of expansion in 2019, as the real gross domestic product ("GDP"), the value of all goods and services produced in the nation, grew at an annual rate of 2.1 percent (estimated) in the fourth quarter. This followed third quarter growth of 2.1 percent in real GDP. The economy grew at a solid 2.3 percent for all of 2019. GDP grew at a rate of 2.9 percent in 2018 by comparison. The Federal Reserve Board's Federal Open Market Committee ("FOMC") decreased the federal funds rate three times in 2019 ending the year at a range of 1.50 percent to 1.75 percent. In lowering the key target range for the federal funds rate, the FOMC noted that the labor market remained strong and that economic activity had been rising at a moderate rate. Job gains had been solid and the unemployment rate has remained low. On the inflation front, it remains below the target rate of 2.0 percent and expectations for longer-term inflation remained little changed. The median forecast was for a federal funds rate of 1.3 percent by year-end 2020, implying that there would have been one additional rate cut in 2020.

On a national level, employment conditions improved in 2019. The civilian labor force increased 1.4 million, while the number of people employed increased 2.0 million in 2019. As a result, the annual unemployment rate for the U.S. fell in 2019 when compared to 2018. All sectors of employment, reported employment gains from the end of 2018.

National, Pennsylvania, New York and our market area's non-seasonally-adjusted annual unemployment rates in 2019 and 2018, are summarized as follows:

	2019	2018
United States	3.7 %	3.9 %
New York	4.0	4.1
Pennsylvania	4.1	4.3
Broome County	4.6	4.9
Bucks County	3.6	3.8
Lackawanna County	4.6	4.6
Lehigh County	4.3	4.6
Luzerne County	5.4	5.4
Monroe County	5.1	5.3
Montgomery County	3.3	3.4
Northampton County	4.2	4.4
Schuylkill County	5.1	5.2
Susquehanna County	4.1	4.0
Wayne County	4.4	4.8
Wyoming County	4.6 %	4.5 %

Employment conditions improved for both the Commonwealth of Pennsylvania and New York State in 2019 as evidenced by a decrease in their respective unemployment rates. With respect to the markets we serve, the unemployment rate decreased in nine of the thirteen counties in which we have branches or ATM locations. The unemployment rate remained the same year over year in two of the remaining counties and increased nominally in the other two counties. The lowest unemployment rate in 2019, for all of the counties we serve, was Montgomery County at 3.3 percent.

With respect to the banking industry, net income for all FDIC-insured banks in 2019 totaled $233.1 billion, a decrease of $3.6 billion or 1.5 percent from 2018. Approximately 64.3 percent of all institutions reported higher net income in 2019, while only 3.6 percent reported net losses, up slightly from last year's reported 3.2 percent unprofitable institutions. Loan loss provisions of $55.0 billion in 2019 were $5.0 billion or 10.0 percent more than banks set aside in 2018. Net interest income increased for the sixth year in a row, by $5.5 billion or 1.0 percent. Noninterest income was $1.7 billion or 0.6 percent below the level of 2018. Realized gains on sales of investments were $4.0 billion compared to $328.0 million in

2018. Total noninterest expense increased $6.6 billion or 1.4 percent comparing 2019 and 2018. The return on average assets for 2019 was 1.29 percent compared to 1.35 percent in 2018.

Review of Financial Position:

Total assets, loans and deposits were $2.5 billion, $1.9 billion and $2.0 billion, respectively, at December 31, 2019. Total assets, loans and deposits grew 8.1 percent, 6.3 percent and 5.1 percent, respectively, compared to 2018 year-end balances.

The loan portfolio consisted of $1.5 billion of business loans, including commercial and commercial real estate loans, and $403.9 million in retail loans, including residential mortgage and consumer loans at December 31, 2019. Total investment securities were $338.6 million at December 31, 2019, including $330.5 million of investment securities classified as available-for sale and $7.7 million classified as held-to-maturity. Total deposits consisted of $463.2 million in noninterest-bearing deposits and $1.5 billion in interest-bearing deposits at December 31, 2019.

Stockholders' equity equaled $299.0 million, or $40.47 per share, at December 31, 2019, and $278.6 million, or $37.66 per share, at December 31, 2018. Our equity to asset ratio was 12.08 percent and 12.17 percent at those respective period ends. Dividends declared for the 2019 amounted to $1.37 per share representing 39.4 percent of net income.

Nonperforming assets equaled $10.5 million or 0.54 percent of loans, net and foreclosed assets at December 31, 2019, an increase in balance but lower percentage when compared to $10.0 million or 0.55 percent at December 31, 2018. The allowance for loan losses equaled $22.7 million or 1.17 percent of loans, net, at December 31, 2019, compared to $21.4 million or 1.17 percent at year-end 2018. Loans charged-off, net of recoveries equaled $4.8 million or 0.26 percent of average loans in 2019, compared to $1.8 million or 0.10 percent of average loans in 2018.

Investment Portfolio:

Primarily, our investment portfolio provides a source of liquidity needed to meet expected loan demand and generates a reasonable return in order to increase our profitability. Additionally, we utilize the investment portfolio to meet pledging requirements and reduce income taxes. At December 31, 2019, our portfolio consisted primarily of short-term U.S. Treasury and government agency securities, which provide a source of liquidity and intermediate-term, tax-exempt state and municipal obligations, which mitigate our tax burden.

Investment securities increased $60.3 million, to $338.6 million at December 31, 2019, from $278.3 million at December 31, 2018. At December 31, 2019, the investment portfolio consisted of $330.5 million of investment securities classified as available-for-sale and $7.7 million classified as held-to-maturity. Investment cash flow was directed back into the investment portfolio primarily during the third and fourth quarters of 2019. Additionally during the fourth quarter, $55.0 of residential mortgage-backed securities were purchased with overnight borrowings to mitigate interest rate risk in a flat or down rate environment. Security purchases totaled $124.5 million in 2019, with purchases consisting of longer term taxable and tax-exempt municipal securities and mortgage-backed securities. Investment purchases in 2018 amounted to $32.7 million.

Repayments of investment securities totaled $58.2 million in 2019 and $32.0 million in 2018. During 2019, the Company sold $9.7 million of low-yielding short-term municipal bonds resulting in a gain of $23 thousand. The proceeds were used to reinvest back into longer duration and higher yielding bonds. There were no sales of investment securities during 2018. We continually analyze the investment portfolio with respect to its exposure to various risk elements.

Investment securities averaged $279.4 million and equaled 13.0 percent of average earning assets in 2019, compared to $281.7 million and 13.8 percent of average earning assets in 2018. The tax-equivalent yield on the investment portfolio decreased thirteen basis points to 2.47 percent in 2019 from 2.60 percent in 2018. The decrease in the tax-equivalent yield is due primarily to cash flow from maturing and called bonds being reinvested into lower market rates.

Loan Portfolio:

Total loans increased $115.0 million or 6.3 percent in 2019 to $1.9 billion at December 31, 2019. Business loans, including commercial loans and commercial real estate loans, were $1.5 billion or 79.2 percent of total loans at December 31, 2019, and $1.4 billion or 76.9 percent at year-end 2018. Residential mortgages and consumer loans totaled $403.9 million or 20.8 percent of total loans at year-end 2019 and $421.3 million or 23.1 percent at year-end 2018. Loan growth remained strong throughout 2019. Total loans grew at an annual rate of 6.3 percent in 2019 which includes $18.2 million of run-off in our indirect automobile portfolio due to pricing changes. The majority of the increase in loans in 2019 was primarily attributable to the continued growth fostered by our entrance into the Lehigh Valley market during the fourth quarter of 2014 by establishing a community banking office with a dedicated team of commercial and retail lenders. We have expanded our presence in the greater Lehigh Valley with the addition of two community banking offices, the most recent during the third quarter of 2017, complemented with additional lending teams to continue the growth. Additional growth was attained through our entrance into the King of Prussia market initially by establishing a loan production office and then by opening a retail branch in the fourth quarter of 2016. The remainder of such growth was generated from improved demand for business lending in existing markets. Based on the customer service oriented philosophy of our organization along with the commitment of these employees, we continue to be well received in these new markets as we are in our existing markets.

Loans averaged $1.9 billion in 2019, compared to $1.8 billion in 2018. Taxable loans averaged $1.7 billion, while tax-exempt loans averaged $139.0 million in 2019. Due to improving loan demand, the loan portfolio continues to play the prominent role in our earning asset mix. As a percentage of earning assets, average loans equaled 86.6 percent in 2019, an increase from 86.1 percent in 2018.

Asset Quality:

Our nonperforming assets increased $559 thousand or 5.6 percent at December 31, 2019 when compared to the end of 2018, however, we experienced improvement in our asset quality ratios as evidenced by a decrease in nonperforming assets as a percentage of loans, net and foreclosed assets to 0.54 percent from 0.55 percent, and nonperforming loans as a percentage of loans, net to 0.52 percent from 0.53 percent. The increase in balances resulted from a $1.6 million increase in nonaccrual loans due to the addition of one large commercial relationship and an increase in foreclosed assets of $0.1 million. A decrease of $0.6 million in troubled debt restructured loans due to the charge-off of $0.3 million of commercial real estate loans coupled with principal payments received on outstanding loans and a decrease of $0.6 million of accruing loans past due ninety days partially offset the increases. For a further discussion of assets classified as nonperforming assets and potential problem loans, refer to the note entitled, “Loans, net and the allowance for loan losses,” in the Notes to Consolidated Financial Statements to this Annual Report.

We maintain the allowance for loan losses at a level we believe adequate to absorb probable credit losses related to individually evaluated loans, as well as probable incurred losses inherent in the remainder of the loan portfolio as of the balance sheet date. The balance in the allowance for loan losses account is based on past events and current economic conditions. We employ the FFIEC Interagency Policy Statement, as amended, and GAAP in assessing the adequacy of the allowance account. Under GAAP, the adequacy of the allowance account is determined based on the provisions of FASB Accounting Standards Codification (“ASC”) 310 for loans specifically identified to be individually evaluated for impairment and the requirements of FASB ASC 450, for large groups of smaller-balance homogeneous loans to be collectively evaluated for impairment.

The allowance for loan losses increased $1.3 million to $22.7 million at December 31, 2019, from $21.4 million at the end of 2018. The increase resulted from a provision for loan losses of $6.1 million less net loans charged-off of $4.8 million. The charge-offs for fiscal 2019 primarily occurred in the fourth quarter. We charged-off $3.3 million of commercial loans in 2019 substantially all of which were in the fourth quarter. Included in this amount was $2.3 million related to certain small business lines of credit in our Greater Delaware Valley market and $1.0 million of other commercial loan relationships.

Past due loans not satisfied through repossession, foreclosure or related actions are evaluated individually to determine if all or part of the outstanding balance should be charged against the allowance for loan losses account. Any subsequent recoveries are credited to the allowance account. Net loans charged-off increased $3.0 million to $4.8 million in 2019 from $1.8 million in 2018. Net charge-offs, as a percentage of average loans outstanding, equaled 0.26 percent in 2019 and 0.10 percent in 2018.

The allocated element of the allowance for loan losses account increased $1.3 million to $22.7 million at December 31, 2019, compared to $21.4 million at December 31, 2018. The specific portion of the allowance for impairment of loans individually evaluated under FASB ASC 310 decreased $402 thousand to $777 thousand at December 31, 2019, from $1.2 million at December 31, 2018 and the formula portion of the allowance for loans collectively evaluated for impairment under FASB ASC 450, increased $1.7 million to $21.9 million at December 31, 2019, from $20.2 million at December 31, 2018. The decrease in the specific portion of the allowance was a result of a decrease in measured impairment for collateral dependent loans. The increase in the formula portion was primarily the result of a significant increase in volume and an increase in the historical loss factor for commercial loans, due to the increase in charge-offs during 2019.

There was no unallocated element of the total allowance for loan losses at December 31, 2019. As is inherent with all estimates, the allowance for loan losses methodology is subject to a certain level of imprecision as it provides reasonable, but not absolute, assurance that the allowance will be able to absorb probable losses, in their entirety, as of the financial statement date. Factors, among others, including judgments made in identifying those loans considered impaired, appraisals of collateral values and measurements of certain qualitative factors, all cause this imprecision and support the establishment of the unallocated element.

The coverage ratio, the allowance for loan losses account, as a percentage of nonperforming loans, is an industry ratio used to test the ability of the allowance account to absorb potential losses arising from nonperforming loans. The coverage ratio was 225.0 percent at December 31, 2019 and 222.9 percent at December 31, 2018. We believe that our allowance was adequate to absorb probable credit losses at December 31, 2019.

Deposits:

Our deposit base is the primary source of funds to support our operations. We offer a variety of deposit products to meet the needs of our individual and commercial customers. Total deposits grew $96.5 million or 5.1 percent to $2.0 billion at the end of 2019. Total deposits include $23.0 million of brokered certificates of deposit. Noninterest-bearing deposits grew $53.0 million or 12.9% while interest-bearing deposits increased $43.5 million or 3.0% in 2019. Noninterest-bearing deposits represented 23.5 percent of total deposits while interest-bearing deposits accounted for 76.5 percent of total deposits at December 31, 2019. Comparatively, noninterest-bearing deposits and interest-bearing deposits represented 21.9 percent and 78.1 percent of total deposits at year end 2018. With regard to noninterest-bearing deposits, personal checking accounts increased $10.4 million or 5.1 percent, while commercial checking accounts increased $42.7 million or 20.5 percent. The increase in noninterest-bearing deposits is essential in attempting to keep our overall cost of funds low given the pressure on our net interest margin from the increase in short-term market rates.

With regard to interest-bearing deposits, interest-bearing transaction accounts, which include money market accounts and NOW accounts, and savings accounts, increased $10.2 million in 2019. Commercial interest-bearing transaction accounts decreased $3.4 million, while personal interest-bearing transaction accounts increased $21.5 million. Savings accounts decreased $7.9 million during 2019 as price sensitive depositors shifted balances to more attractive premium rates being offered on time deposits by us and our competitors. The strong growth in our non-maturity deposits was due to continuing our strategic initiative to grow our public fund deposits and our continued penetration in our expansion markets. Total time deposits increased $33.3 million to $369.5 million at December 31, 2019 from $336.2 million at December 31, 2018. The increase was primarily due to rate conscious consumer and commercial depositors seeking higher yields.

Total deposits averaged $1.9 billion in 2019 and $1.8 billion in 2018, increasing $165.7 million or 9.4 percent comparing 2019 to 2018. Average noninterest-bearing deposits increased $39.4 million, while average interest-bearing accounts grew $126.3 million. Average interest-bearing transaction deposits, including money market and NOW, and savings accounts, increased $50.1 million while average total time deposits increased $76.2 million when comparing 2019 and 2018.

Our cost of interest-bearing deposits increased 33 basis points to 1.01 percent in 2019 from 0.68 percent in 2018. Specifically, the cost of money market accounts increased 45 basis points to 1.31 percent from 0.86 percent and NOW accounts increased 15 basis points while the cost of time deposits increased 54 basis points to 1.90 percent comparing 2019 and 2018. The increases to the cost of interest-bearing transaction deposits and time deposits was the result of the increase in short-term market rates resulting from the FOMC's action to raise the targeted federal funds rate four times during 2018 and the continued elevated short term market rates as the yield curve remained flat despite the FOMC's action in the second half of 2019 to cut the federal funds rate three times. In response to the FOMC's actions in 2019, we have decreased rates on time deposits and engaged in an initiative to reduce premium rates being paid to retain our core deposit relationships both in our legacy market and expansion markets in order to reduce our overall deposit costs.

Volatile deposits, time deposits $100 or more, averaged $230.6 million in 2019, an increase of $83.5 million or 56.8 percent from $147.1 million in 2018. Our average cost of these funds increased 63 basis points to 2.16 percent in 2019, from 1.53 percent in 2018. This type of funding is susceptible to withdrawal by the depositor as they are particularly price sensitive and are therefore not considered to be a strong source of liquidity.

Market Risk Sensitivity:

With respect to evaluating our exposure to IRR on earnings, we utilize a gap analysis model that considers repricing frequencies of RSA and RSL. Gap analysis attempts to measure our interest rate exposure by calculating the net amount of RSA and RSL that reprice within specific time intervals. A positive gap occurs when the amount of RSA repricing in a specific period is greater than the amount of RSL repricing within that same time frame and is indicated by a RSA/RSL ratio greater than 1.0. A negative gap occurs when the amount of RSL repricing is greater than the amount of RSA and is indicated by a RSA/RSL ratio less than 1.0. A positive gap implies that earnings will be impacted favorably if interest rates rise and adversely if interest rates fall during the period. A negative gap tends to indicate that earnings will be affected inversely to interest rate changes.

At December 31, 2019, we had cumulative one-year RSA/RSL ratio of 0.98, a slightly negative gap. At December 31, 2018, we had cumulative one-year RSA/RSL of 1.07, a positive gap. As previously mentioned, a negative gap indicated that if interest rates increase, our earnings would likely be adversely impacted. Given the then current economic conditions and the action of the FOMC to cut short-term rates during the second half of 2019 and the uncertainty of future actions to either cut or raise short-term rates in 2020, the focus of ALCO had been to maintain a well-balanced IRR position in order to safeguard future earnings from potential risk to falling interest rates. During 2019 ALCO took steps to reduce the magnitude of our positive gap position and guard against rates unchanged or down through the origination of five year fixed rate loans and the investment in longer term, fixed rate municipal securities and longer duration U.S. government-sponsored mortgage-backed securities.

The change in our cumulative one-year ratio from the 2018 year-end resulted from a $168.5 million or 21.7 percent increase in RSL coupled with a $91.9 million or 11.0 percent increase in RSA maturing or repricing within one year. The increase in RSL resulted primarily from a $102.0 million increase in time deposits $100 thousand or more and an increase in short-term borrowings of $65.6 million. The majority of the increase in the time deposit balances was due to rate sensitive customers seeking higher rates with terms less than twelve months. The increase in short-term borrowings was due to purchasing $55.0 million of mortgage-backed securities with short-term funding during the fourth quarter of 2019.

With respect to the increase in RSA maturing or repricing within a twelve month time horizon, loans, net increased $64.3 million while investment securities increased $22.5 million. The increase in total loans, net of unearned income, resulted from an increase in commercial lending, which primarily involves loans with adjustable-rate terms that reprice in the near term. The increase in investment securities was due to higher prepayment estimates as a result of the FOMC's action to cut the targeted federal funds rate during 2019 and the flat yield curve.

Liquidity:

We employ a number of analytical techniques in assessing the adequacy of our liquidity position. One such technique is the use of ratio analysis to illustrate our reliance on noncore funds to fund our investments and loans maturing after 2019. At December 31, 2019, our noncore funds consisted of time deposits in denominations of $100 thousand or more, short-term borrowings and long-term debt. Large denomination time deposits are particularly not considered to be a strong source of liquidity since they are very interest rate sensitive and are considered to be highly volatile. At December 31, 2019, our net noncore funding dependence ratio, the difference between noncore funds and short-term investments to long-term assets, was 17.8 percent. Our net short-term noncore funding dependence ratio, noncore funds maturing within one year, less short-term investments to long-term assets equaled 14.4 percent. Comparatively, our ratios equaled 15.0 percent and 6.3 percent at the end of 2018, which indicated an increase in our reliance on noncore funds in 2019. Moreover, our basic liquidity surplus ratio, defined as liquid assets less short-term potentially volatile liabilities as a percentage of total assets, increased to 5.7 percent at December 31, 2019, from 4.1 percent at December 31, 2018. We believe that by supplying adequate volumes of short-term investments and implementing competitive pricing strategies on deposits, we can ensure adequate liquidity to support future growth.

The Consolidated Statements of Cash Flows present the change in cash and cash equivalents from operating, investing and financing activities. Cash and cash equivalents consist of cash on hand, cash items in the process of collection, noninterest-bearing and interest-bearing deposits with other banks and federal funds sold. Cash and cash equivalents decreased $1.5 million for the year ended December 31, 2019. For the year ended December 31, 2018, cash and cash equivalents decreased $4.9 million. During 2019, cash provided by operating and financing activities were more than offset by cash used in investing activities.

Operating activities provided net cash of $37.1 million in 2019 and $32.6 million in 2018. Net income, adjusted for the effects of noncash expenses such as depreciation, amortization and accretion of tangible and intangible assets and investment securities, and the provision for loan losses, is the primary source of funds from operations.

Net cash provided by financing activities equaled $146.2 million in 2019. Net cash provided by financing activities was $97.3 million in 2018. Deposit gathering, which is our predominant financing activity, increased in both 2019 and 2018. Deposit gathering provided a net cash inflow in 2019 of $96.5 million and $156.0 million in 2018. Short-term borrowings increased net cash by $65.6 million in 2019 while a net decrease in short-term borrowings of $37.2 million reduced net cash provided by financing activities in 2018. Deposit gathering in 2019 was also partially offset by a $5.2 million net decrease in long-term debt as well as cash dividends paid of $10.1 million. In 2018, deposit gathering was partially offset by $11.8 million repayments of long-term debt and cash dividends paid of $9.7 million.

Our primary investing activities involve transactions related to our investment and loan portfolios. Net cash used in investing activities totaled $184.7 million in 2019. Net cash used in investing activities was $134.8 million in 2018. Net cash used in lending activities was $120.0 million in 2019, a decrease from $141.3 million in 2018. Activities related to our investment portfolio used net cash of $66.3 million in 2019 and $0.7 million in 2018.

Capital Adequacy:

Bank regulatory agencies consider capital to be a significant factor in ensuring the safety of a depositor's accounts. These agencies have adopted minimum capital adequacy requirements that include mandatory and discretionary supervisory actions for noncompliance. Our and Peoples Bank's risk-based capital ratios are strong and have consistently exceeded the minimum regulatory capital ratios required for adequately capitalized institutions. Our ratio of Tier 1 capital to risk-weighted assets and off-balance sheet items was 11.9 percent and 12.0 percent at December 31, 2019 and 2018, respectively. Our Total capital ratio was 13.0 percent and 13.1 percent at December 31, 2019 and 2018, respectively. Our and Peoples Bank's common equity Tier I capital to risk-weighted assets ratios were 11.9 percent and 11.6 percent at December 31, 2019 and 12.0 percent and 11.6 percent at December 31, 2018. Our Leverage ratio, which equaled 10.1 percent at December 31, 2019 and 10.0 percent at December 31, 2018, exceeded the minimum of 4.0 percent for capital adequacy purposes. Peoples Bank reported Tier 1 capital, Total capital and Leverage ratios of 11.6 percent, 12.8 percent and 9.9 percent at December 31, 2019, and 11.6 percent, 12.8 percent and 9.8 percent at

December 31, 2018. Based on the most recent notification from the FDIC, Peoples Bank was categorized as well capitalized at December 31, 2019. For a further discussion of these risk-based capital standards and supervisory actions for noncompliance, refer to the note entitled, "Regulatory matters," in the Notes to Consolidated Financial Statements to this Annual Report.

Stockholders' equity was $299.0 million or $40.47 per share at December 31, 2019, and $278.6 million or $37.66 per share at December 31, 2018. Stockholders' equity grew $20.4 million in 2019 as net income and a decrease in accumulated other comprehensive loss partially offset the payment of dividends.

Review of Financial Performance:

Net income was $25.7 million or $3.48 per share in 2019 and $24.9 million or $3.37 per share in 2018. The increase in earnings in 2019 is the result of higher net interest income of $4.2 million due to growth of our earning assets and higher noninterest income of $1.5 million which were partially offset by an increase of $1.9 million in the provision for loan losses and higher noninterest expenses of $3.2 million. The results for 2018 include a $0.3 million net gain on the sale of our credit card portfolio. Return on average assets ("ROAA") and return on average equity ("ROAE") were 1.10 percent and 8.87 percent for the year ended December 31, 2019. ROAA was 1.12 percent and ROAE was 9.21 percent for the year ended December 31, 2018.

Tax-equivalent net interest income, a non-GAAP measure, was $77.2 million in 2019 and $73.0 million in 2018. Our net interest margin equaled 3.58 percent in 2019 and 3.59 percent in 2018. Noninterest income totaled $15.1 million in 2019 and $13.7 million in 2018. Noninterest expense was $56.0 million for the year ended December 31, 2019 compared to $52.5 million for the year ended December 31, 2018. Our productivity is measured by the operating efficiency ratio, a non-GAAP measure, defined as noninterest expense less amortization of intangible assets divided by the total of tax-equivalent net interest income and noninterest income. Our operating efficiency ratio was 59.6 percent in 2019 and 59.8 percent in 2018.

Net Interest Income:

Tax-equivalent net interest income, a non-GAAP measure, was $77.2 million in 2019 and $73.0 million in 2018. There was a positive volume variance that was partially offset by a negative rate variance. The growth in average earning assets exceeded that of interest-bearing liabilities, and resulted in additional tax-equivalent net interest income, a non-GAAP measure, of $4.8 million. A rate variance resulted in a decrease in net interest income of $0.7 million.

Average earning assets increased $119.2 million to $2,154.5 million in 2019 from $2,035.3 million in 2018 and accounted for a $5.1 million increase in interest income. Average loans, net increased $112.4 million, which caused interest income to increase $5.2 million. Average taxable investments increased $21.6 million comparing 2019 and 2018, which resulted in increased interest income of $483 thousand while average tax-exempt investments decreased $23.8 million, which resulted in a decrease to interest income of $739 thousand.

Average interest-bearing liabilities rose $52.5 million to $1,600.2 million in 2019 from $1,547.7 million in 2018 resulting in a net increase in interest expense of $248 thousand. Large denomination time deposits averaged $83.6 million more in 2019 and caused interest expense to increase $1.6 million. A decrease of $7.4 million in average time deposits less than $100 thousand reduced interest expense by $92 thousand. In addition, interest-bearing transaction accounts, including money market, NOW and savings accounts grew $50.1 million, which in aggregate caused a $547 thousand increase in interest expense. Short-term borrowings averaged $70.9 million less and decreased interest expense $1.7 million while long-term debt averaged $2.9 million less and decreased interest expense by $78 thousand comparing 2019 and 2018.

An unfavorable rate variance occurred, as the tax-equivalent yield on earning assets increased 17 basis points while there was a 26 basis point increase in the cost of funds. As a result, tax-equivalent net interest income decreased $688 thousand comparing 2019 and 2018. The tax-equivalent yield on earning assets was 4.41 percent in 2019 compared to 4.24 percent in 2018 resulting in an increase in interest income of $3.6 million. With the tax-equivalent yield on the investment portfolio decreasing 13 basis points to 2.47 percent in 2019 from 2.60 percent in 2018, interest income decreased $180 thousand. The tax-equivalent yield on the loan portfolio increased 20 basis points to 4.71 percent in 2019 from 4.51 percent in 2018 and resulted in an increase to interest income of $3.8 million.

An unfavorable rate variance was experienced in the cost of funds. We experienced increases in the rates paid on all major categories of interest-bearing liabilities with the exception of savings accounts. Specifically, the cost of money market and NOW accounts increased 45 basis points and 15 basis points comparing 2019 and 2018. These increases resulted in an increase in interest expense of $2.1 million. The cost of savings accounts remained level at 13 basis points and had no significant change in interest expense. With regard to time deposits, the average rate paid for time deposits less than $100 thousand increased 27 basis points while time deposits $100 thousand or more increased 63 basis points, which together resulted in a $1.5 million increase in interest expense. The average rate paid on short-term borrowings increased 56 basis points in 2019 when compared to 2018, causing a $617 thousand increase in interest expense. Interest expense increased $71 thousand from a 15 basis point increase in the average rate paid on long-term debt.

Provision for Loan Losses:

We evaluate the adequacy of the allowance for loan losses account on a quarterly basis utilizing our systematic analysis in accordance with procedural discipline. We take into consideration certain factors such as composition of the loan portfolio, volume of nonperforming loans, volumes of net charge-offs, prevailing economic conditions and other relevant factors when determining the adequacy of the allowance for loan losses account. We make monthly provisions to the allowance for loan losses account in order to maintain the allowance at an appropriate level. The provision for loan losses equaled $6.1 million in 2019 and $4.2 million in 2018. The higher provision for loan losses in 2019 was a direct result of significant loan growth and an increase in charge-offs, which created an increase in our calculated allowance. As previously discussed, the increase in charge-offs in 2019 was primarily related to commercial loans and specifically to small business lines of credit originated in our Greater Delaware Valley market. Based on our evaluation at December 31, 2019, we believe that the allowance was adequate to absorb any known or potential losses in our portfolio as of such date.

Noninterest Income:

Our noninterest income increased $1.5 million or 10.7 percent to $15.1 million in 2019 from $13.7 million in 2018. The increase in 2019 was driven primarily by higher service charges, fees, and commissions which includes an increase in fee income of $1.7 million generated from the higher number and increased volume of commercial loan interest rate swap transactions originated in 2019 versus 2018. Excluding the swap revenue, service charges, fees, and commissions decreased $339 thousand or 4.5 percent comparing 2019 and 2018, due in part to death benefit proceeds on a bank owned life insurance (BOLI) policy totaling $368 thousand in 2018 with no comparable amount in 2019, and a lower dividend on our FHLB-Pgh stock of $96 thousand due to lower borrowing volume in 2019. We realized a $23 thousand net gain on the sale of debt securities in 2019 while the 2018 results include a $291 thousand net gain on the sale of our credit card portfolio. Merchant services revenue increased $164 thousand or 20.3 percent in 2019 when compared to 2018 due to higher pricing. Commissions and fees on fiduciary activities increased $51 thousand or 2.5 percent comparing 2019 and 2018 due to market appreciation and increased business. Wealth management income increased $77 thousand or 5.3 percent comparing 2019 to 2018 due to increased growth. Mortgage banking income decreased $27 thousand or 4.3 percent in 2019 compared to 2018 as the volume of saleable loans originated declined.

Noninterest Expense:

Noninterest expense was $55.6 million for the year ended December 31, 2019 compared to $52.5 million for the year ended December 31, 2018.

Salaries and employee benefits expense constitute the majority of our noninterest expenses accounting for 56.4 percent of the total noninterest expense in 2019. Salaries and employee benefits expense increased $3.0 million or 10.4 percent to $31.4 million in 2019 from $28.4 million in 2018. Salaries and payroll taxes increased $2.4 million or 10.1 percent, while employee benefits expense increased $594 thousand or 12.2 percent. Annual performance-based salary adjustments as well as costs associated with our expansion into south central Pennsylvania and the addition of seasoned lending and support personnel in the region provided the majority of the increase.

Occupancy and equipment expense increased $1.0 million or 9.3 percent to $11.9 million in 2019 from $10.9 million in 2018. Specifically, equipment-related costs increased $1.3 million or 26.9 percent while building-related costs decreased $242 thousand or 3.9 percent. The increase in equipment-related expenses was driven by costs associated with expansion into the south central Pennsylvania market area and higher depreciation expenses due to the revitalization of two of our branches.

Other expenses, which consist of merchant transaction expense, FDIC insurance and assessments, professional fees and outside services, other taxes, stationary and supplies, advertising, amortization of intangible assets and all other expenses were $12.4 million in 2019 and $13.2 million in 2018. FDIC insurance and assessments was lower by $442 thousand or 40.4 percent as the bank received a FDIC small bank assessment credit of $358 thousand recognized in the second half of 2019. All other expenses, including professional fees and outside services, other taxes, stationery and supplies, advertising, amortization of intangible assets and other expenses totaled $12.4 million in 2019, a decrease of $820 thousand or 6.2 percent, compared to $13.2 million in 2018.

Income Taxes:

Our income tax expense was $3.2 million in 2019 and $3.4 million in 2018. We utilize loans and investments of tax-exempt organizations to mitigate our tax burden, as interest revenue from these sources is not taxable by the federal government. As a result, our effective tax rate was 10.9 percent in 2019 and 12.0 percent in 2018.

The effective tax rate in 2019 and 2018 was also influenced by the recognition of investment tax credits related to our limited partnership investments in elderly and low- to moderate-income residential housing programs which allow us to mitigate our tax burden. By utilizing these credits, we reduced our income tax expense by $1.1 million in both 2019 and 2018. We anticipate investment tax credits from these investments to be $1.1 million again in 2020. Over the years 2020-2024, we will recognize aggregate tax credits from our investments in these projects of $4.5 million.

Item 7A. Quantitative and Qualitative Disclosures About Market Risk.

Market risk is the risk to our earnings and/or financial position resulting from adverse changes in market rates or prices, such as interest rates, foreign exchange rates or equity prices. Our exposure to market risk is primarily interest rate risk ("IRR"), which arises from our lending, investing and deposit gathering activities. Our market risk sensitive instruments consist of derivative and non-derivative financial instruments, none of which are entered into for trading purposes. During the normal course of business, we are not exposed to foreign exchange risk or commodity price risk. Our exposure to IRR can be explained as the potential for change in reported earnings and/or the market value of net worth. Variations in interest rates affect the underlying economic value of assets, liabilities and off-balance sheet items. These changes arise because the present value of future cash flows, and often the cash flows themselves, change with interest rates. The effects of the changes in these present values reflect the change in our underlying economic value, and provide a basis for the expected change in future earnings related to interest rates. Interest rate changes affect earnings by changing net interest income and the level of other interest-sensitive income and operating expenses. IRR is inherent in the role of banks as financial intermediaries.

A bank with a high degree of IRR may experience lower earnings, impaired liquidity and capital positions, and most likely, a greater risk of insolvency. Therefore, banks must carefully evaluate IRR to promote safety and soundness in their activities. Interest rate risk is the risk of loss to future earnings due to changes in interest rates. The Asset Liability Committee ("ALCO") is responsible for establishing policy guidelines on liquidity and acceptable exposure to interest rate risk. Generally quarterly, ALCO reports on the status of liquidity and interest rate risk matters to the Company's board of directors. The objective of the ALCO is to manage assets and funding sources to produce results that are consistent with the Company's liquidity, capital adequacy, growth, risk and profitability goals and are within policy limits.

The Company utilizes the pricing and structure of loans and deposits, the size and duration of the investment securities portfolio, the size and duration of the wholesale funding portfolio, and off-balance sheet interest rate contracts to manage interest rate risk. The off-balance sheet interest rate contracts may include interest rate swaps, caps and floors. These interest rate contracts involve, to varying degrees, credit risk and interest rate risk. Credit risk is the possibility that a loss may occur if a counterparty to a transaction fails to perform according to terms of the contract. The notional amount of the interest rate contracts is the amount upon which interest and other payments are based. The notional amount is not exchanged, and therefore, should not be taken as a measure of credit risk. See Note 15 to the Audited Consolidated Financial Statements for additional information.

The ALCO uses income simulation to measure interest rate risk inherent in the Company's on-balance sheet and off-balance sheet financial instruments at a given point in time by showing the effect of interest rate shifts on net interest income over a 24-month horizon and a 60-month horizon. The simulations assume that the size and general composition of the Company's balance sheet remain static over the simulation horizons, with the exception of certain deposit mix shifts from low-cost time deposits to higher-cost time deposits in selected interest rate scenarios. Additionally, the simulations take into account the specific repricing, maturity, call options, and prepayment characteristics of differing financial instruments that may vary under different interest rate scenarios. The characteristics of financial instrument classes are reviewed typically quarterly by the ALCO to ensure their accuracy and consistency.

The ALCO reviews simulation results to determine whether the Company's exposure to a decline in net interest income remains within established tolerance levels over the simulation horizons and to develop appropriate strategies to manage this exposure. As of December 31, 2020 and December 31, 2019, net interest income simulations indicated that exposure to changing interest rates over the simulation horizons remained within tolerance levels established by the Company. All changes are measured in comparison to the projected net interest income that would result from an "unchanged" rate scenario where both interest rates and the composition of the Company's balance sheet remain stable for a 24-month and 60-month period. In addition to measuring the change in net interest income as compared to an unchanged interest rate scenario, the ALCO also measures the trend of both net interest income and net interest margin over a 24-month and 60-month horizon to ensure the stability and adequacy of this source of earnings in different interest rate scenarios.

Model results at December 31, 2020 indicated a lower starting level of net interest income ("NII") compared to the December 31, 2019 model as the balance sheet spread contracted 46 basis points due primarily to lower asset yields resulting from the action of the FOMC to cut the targeted federal funds rate 225 basis points since the second half of 2019. Our interest rate profile depicts a relatively well matched position in the near term. As the simulation timeline progresses, a benefit to rising rates emerges while a flat to falling rate scenario presents challenges to the annual run rate of NII. This position at December 31, 2020 was similar to the position indicated by simulation as of December 31, 2019.

The ALCO regularly reviews a wide variety of interest rate shift scenario results to evaluate interest rate risk exposure, including scenarios showing the effect of steepening or flattening changes in the yield curve as well as parallel changes in interest rates of up to 400 basis points. Because income simulations assume that the Company's balance sheet will remain static over the simulation horizon, the results do not reflect adjustments in strategy that the ALCO could implement in response to rate shifts.

With rates having fallen materially in 2020, the down 100 basis point scenario would result in market rates reaching floored values which can produce a distorted view of interest rate risk metrics.

In response to the economic disruption and uncertainty brought on by the COVID-19 pandemic, the FOMC lowered the federal funds target rate a total of 150 basis points in two emergency actions during March 2020 with an expectation that the Committee will maintain a low interest rate environment for the foreseeable future. Given the Company's current asset/liability position, the significantly lower market interest rates have had and may continue to have a negative impact on our earning asset yields and variable-rate loans indexed to prime, LIBOR or other market rates.

The projected impact of instantaneous changes in interest rates on our net interest income and economic value of equity at December 31, 2020, based on our simulation model, is summarized as follows:

	December 31, 2020 % Change in			
Changes in Interest Rates (basis points)	**Net Interest Income**		**Economic Value of Equity**	
	Metric	**Policy**	**Metric**	**Policy**
+400	18.7	(20.0)	33.6	(40.0)
+300	13.7	(20.0)	27.1	(30.0)
+200	8.8	(10.0)	19.6	(20.0)
+100	4.3	(10.0)	11.7	(10.0)
Static				
-100	0.7	(10.0)	(24.1)	(10.0)

Our simulation model creates pro forma net interest income scenarios under various interest rate shocks. Given instantaneous and parallel shifts in general market rates of plus 100 basis points, our projected net interest income for the 12 months ending December 31, 2020, would increase at 4.3 percent from model results using current interest rates. Additional disclosures about market risk are included in Part II, Item 7 of this Annual Report, under the heading "Market Risk Sensitivity," and are incorporated into this Item 7A by reference.

The Company has certain loans and derivative instruments whose interest rate is indexed to the London Inter Bank Offered Rate (LIBOR). The United Kingdom's Financial Conduct Authority, which is responsible for regulating LIBOR, has announced that the publication of one week and two month U.S. dollar (USD) LIBOR settings is not guaranteed beyond December 31, 2021 and the remaining USD LIBOR settings beyond June 30, 2023. At this time, no consensus exists as to what reference rate or rates or benchmarks may become acceptable alternatives to LIBOR, although the Alternative Reference Rates Committee (a group of private-market participants convened by the Federal Reserve Board and the Federal Reserve Bank of New York) has identified the Secured Overnight Financing Rate, or SOFR, as the recommend alternative to LIBOR. The Company has material contracts that are indexed to USD-LIBOR. Industry organizations are currently working on the transition plan. The Company is currently monitoring this activity and evaluating the risks involved.

Item 8. Financial Statements.

REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

To the Stockholders and Board of Directors of
Peoples Financial Services Corp. and Subsidiaries

Opinions on the Financial Statements and Internal Control over Financial Reporting

We have audited the accompanying consolidated balance sheets of Peoples Financial Services Corp. and Subsidiaries (Company) as of December 31, 2020 and 2019, and the related consolidated statements of income and comprehensive income, changes in stockholders' equity, and cash flows, for each of the three years in the period ended December 31, 2020, and the related notes (collectively, the consolidated financial statements). We also have audited the Company's internal control over financial reporting as of December 31, 2020, based on criteria established in *Internal Control – Integrated Framework: (2013)* issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO).

In our opinion, the consolidated financial statements present fairly, in all material respects, the financial position of the Company as of December 31, 2020 and 2019, and the results of its operations and its cash flows for each of the three years in the period ended December 31, 2020, in conformity with accounting principles generally accepted in the United States of America. Also in our opinion, the Company maintained, in all material respects, effective internal control over financial reporting as of December 31, 2020, based on criteria established in *Internal Control – Integrated Framework: (2013)* issued by COSO.

Basis for Opinions

The Company's management is responsible for these consolidated financial statements, for maintaining effective internal control over financial reporting, and for its assessment of the effectiveness of internal control over financial reporting, included in the accompanying Management's Report on Internal Control over Financial Reporting. Our responsibility is to express an opinion on the Company's consolidated financial statements and an opinion on the Company's internal control over financial reporting 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 audit to obtain reasonable assurance about whether the consolidated financial statements are free of material misstatement, whether due to error or fraud and whether effective internal control over financial reporting was maintained in all material respects.

Our audits of the consolidated financial statements included performing procedures to assess the risks of material misstatement of the consolidated 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 consolidated 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 consolidated financial statements. Our audit of internal control over financial reporting included obtaining an understanding of internal control over financial reporting, assessing the risk that a material weakness exists, and testing and evaluating the design and operating effectiveness of internal control based on the assessed risk. Our audits also included performing such other procedures as we considered necessary in the circumstances. We believe that our audits provide a reasonable basis for our opinions.

Definition and Limitations of Internal Control Over Financial Reporting

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

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

Critical Audit Matters

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

Allowance for Loan Losses – General Component Qualitative Factors

As discussed in Notes 1 and 4 to the consolidated financial statements, the allowance for loan losses is established through a provision for loan losses and represents an amount, which, in management’s judgment, will be adequate to absorb losses in the loan portfolio. The Company’s allowance for loan losses was $27.3 million at December 31, 2020 and consists of specific and general components of $1.2 million and $26.1 million, respectively. Management develops the general component based on historical loan loss experience adjusted for qualitative factors not reflected in the historical loss experience. Historical loss ratios are measured on a rolling twelve-quarter basis for all loans. The qualitative factors used by the Company include factors such as national and local economic conditions, levels of and trends in classified loans, delinquency rates and nonaccrual loans, trends in volumes and terms of loans, changes in lending policies, lending personnel, and collateral, as well as concentrations in loan types, industry, and geography. The adjustments for qualitative factors require a significant amount of judgment by management and involve a high degree of estimation uncertainty.

We identified the qualitative factor component of the allowance for loan losses as a critical audit matter as auditing the underlying qualitative factors required significant auditor judgment as amounts determined by management rely on analysis that is highly subjective and includes significant estimation uncertainty.

Our audit procedures related to the qualitative factor component of the allowance for loan losses included the following, among others:

- Obtaining an understanding of the relevant controls related to the allowance for loan losses and tested such controls for design and operating effectiveness, including controls related to management’s establishment, review, and approval of the qualitative factors, and the completeness and accuracy of data used in determining qualitative factors.

- Evaluation of the appropriateness of management's methodology for estimating the allowance for loan losses.
- Testing of the completeness and accuracy of data used by management in determining qualitative factor adjustments by agreeing them to internal and external source data.
- Testing of management's conclusions regarding the appropriateness of the qualitative factor adjustments and agreement of any changes therein to the allowance for loan losses calculation.

Goodwill Impairment Evaluation

The Company has recorded goodwill of $63.4 million. As discussed in Note 1 to the consolidated financial statements, goodwill is not amortized but is tested for impairment at least annually. Impairment exists when the fair value of the reporting unit is less than its carrying amount. Due to volatility in its stock price and economic conditions resulting from the COVID-19 pandemic, the Company engaged a third-party valuation specialist to perform a quantitative test of goodwill impairment at June 30, 2020 using a discounted cash flow analysis (income approach) and estimates of selected market information (market approach). Each approach was weighted 50%. The determination of the fair value of the Company requires management to make significant estimates and assumptions including, among other things, the selection of appropriate discount rates, the identification of relevant market comparables and the development of cash flow projections. At December 31, 2020, its annual impairment testing date, the Company performed a qualitative review to determine if changes since June 30, 2020 resulted in a conclusion that it was more likely than not that fair value was less than carrying value. The Company concluded fair value continued to be in excess of carrying value at December 31, 2020.

We identified the goodwill impairment assessment as a critical audit matter due to the degree of auditor judgment in performing procedures over the key assumptions noted above.

Our audit procedures performed to address this critical matter included the following, among others:

- Obtaining an understanding of internal controls relevant to the goodwill impairment assessment and testing such controls for design and operating effectiveness, including controls related to management's establishment, review, and approval of the assumptions, including those used by the third-party valuation specialist, and the completeness and accuracy of data used.
- Evaluation of the methodologies used in management's analysis, including the weightings assigned to each approach and testing the completeness and accuracy of data used in management's calculations.
- Evaluation of management's ability to forecast cash flows by comparing actual results to historical annual budgets.
- Involvement of an employed valuation specialist to (1) evaluate the key assumptions and inputs used by the management's third-party valuation specialist, including discount rate, terminal growth rate, control premium, and market comparable entities; and (2) test the overall reasonableness of fair value and conclusion of no impairment by calculating an independent expectation as of December 31, 2020.

/s/ Baker Tilly US, LLP

We have served as the Company's auditor since 2017.

Baker Tilly US, LLP (formerly known as Baker Tilly Virchow Krause, LLP)
Wilkes-Barre, Pennsylvania
March 16, 2021

Peoples Financial Services Corp.
CONSOLIDATED BALANCE SHEETS
(Dollars in thousands, except share data)

December 31		2020		2019
Assets:				
Cash and due from banks:				
Cash and due from banks	$	29,287	$	26,943
Interest-bearing deposits in other banks		15,905		4,210
Federal funds sold		183,000		
Total cash and due from banks		228,192		31,153
Investment securities:				
Available-for-sale		295,911		330,478
Equity investments carried at fair value		138		423
Held-to-maturity: Fair value December 31, 2020, $7,513; December 31, 2019, $7,889		7,225		7,656
Total investment securities		303,274		338,557
Loans		2,177,982		1,938,240
Less: allowance for loan losses		27,344		22,677
Net loans		2,150,638		1,915,563
Loans held for sale		837		986
Premises and equipment, net		47,045		47,932
Accrued interest receivable		8,255		6,981
Goodwill		63,370		63,370
Intangible assets, net		960		1,565
Bank owned life insurance		42,316		35,041
Other assets		38,915		34,179
Total assets	$	2,883,802	$	2,475,327
Liabilities:				
Deposits:				
Noninterest-bearing	$	622,475	$	463,238
Interest-bearing		1,814,638		1,508,251
Total deposits		2,437,113		1,971,489
Short-term borrowings		50,000		152,150
Long-term debt		14,769		32,733
Subordinated debentures		33,000		
Accrued interest payable		736		1,277
Other liabilities		31,307		18,668
Total liabilities		2,566,925		2,176,317
Stockholders' equity:				
Common stock, par value $2.00, authorized 25,000,000 shares, issued and outstanding 7,215,202 shares at December 31, 2020 and 7,388,480 shares at December 31, 2019		14,431		14,777
Capital surplus		129,274		135,251
Retained earnings		171,023		152,187
Accumulated other comprehensive income (loss)		2,149		(3,205)
Total stockholders' equity		316,877		299,010
Total liabilities and stockholders' equity	$	2,883,802	$	2,475,327

See notes to consolidated financial statements.

Peoples Financial Services Corp.
CONSOLIDATED STATEMENTS OF INCOME AND COMPREHENSIVE INCOME
(Dollars in thousands, except per share data)

Year Ended December 31	**2020**	**2019**	**2018**
Interest income:			
Interest and fees on loans:			
Taxable	$ 83,683	$ 82,488	$ 74,352
Tax-exempt	3,736	4,309	3,666
Interest and dividends on investment securities:			
Taxable	5,334	4,435	3,799
Tax-exempt	1,178	1,878	2,621
Dividends	97	84	72
Interest on interest-bearing deposits in other banks	31	65	151
Interest on federal funds sold	66	122	
Total interest income	94,125	93,381	84,661
Interest expense:			
Interest on deposits	11,739	14,995	9,346
Interest on short-term borrowings	848	1,642	2,738
Interest on long-term debt	702	1,231	1,238
Interest on subordinated debt	1,035		
Total interest expense	14,324	17,868	13,322
Net interest income	79,801	75,513	71,339
Provision for loan losses	7,400	6,100	4,200
Net interest income after provision for loan losses	72,401	69,413	67,139
Noninterest income:			
Service charges, fees, commissions and other	6,809	7,236	7,575
Merchant services income	824	973	809
Commission and fees on fiduciary activities	2,125	2,087	2,036
Wealth management income	1,282	1,524	1,447
Mortgage banking income	1,595	600	627
Increase in cash surrender value of life insurance	774	755	757
Interest rate swap revenue	2,321	1,790	103
Net gains (losses) on equity investment securities	(6)	132	14
Net gains on sale of investment securities available-for-sale	918	23	
Net gain on sale of credit card loans			291
Total noninterest income	16,642	15,120	13,659
Salaries and employee benefits expense	30,135	31,374	28,407
Net occupancy and equipment expense	12,840	11,911	10,897
Amortization of intangible assets	606	730	881
Professional fees and outside services	2,091	1,758	2,414
FDIC insurance and assessments	873	651	1,093
Donations	1,357	1,441	1,339
Other expenses	6,966	7,777	7,456
Total noninterest expense	54,868	55,642	52,487
Income before income taxes	34,175	28,891	28,311
Income tax expense	4,821	3,155	3,391
Net income	29,354	25,736	24,920
Other comprehensive income (loss):			
Unrealized gain (loss) on investment securities available-for-sale	8,779	5,109	(2,014)
Reclassification adjustment for net gain on sales included in net income	(918)	(23)	
Change in benefit plan liabilities	(1,398)	639	(591)
Change in derivative fair value	315	441	246
Other comprehensive income (loss)	6,778	6,166	(2,359)
Income tax expense (benefit)	1,424	1,295	(496)
Other comprehensive income (loss), net of income taxes	5,354	4,871	(1,863)
Comprehensive income	$ 34,708	$ 30,607	$ 23,648
Per share data:			
Net income:			
Basic	$ 4.02	$ 3.48	$ 3.37
Diluted	$ 4.00	$ 3.47	$ 3.37
Average common shares outstanding:			
Basic	7,304,956	7,395,429	7,397,797
Diluted	7,337,843	7,412,369	7,402,900
Dividends declared	$ 1.44	$ 1.37	$ 1.31

See notes to consolidated financial statements

Peoples Financial Services Corp.
CONSOLIDATED STATEMENTS OF CHANGES IN STOCKHOLDERS' EQUITY
(Dollars in thousands, except per share data)

For the Three Years Ended December 31, 2020	Common Stock	Capital Surplus	Retained Earnings	Accumulated Other Comprehensive Loss	Total
Balance, January 1, 2018	$ 14,793	$ 135,043	$ 121,353	$ (6,213)	$ 264,976
Net income			24,920		24,920
Other comprehensive loss, net of income taxes				(1,861)	(1,861)
Reclassification related to adoption of ASU 2016-01			2	(2)	
Dividends declared: $1.31 per share			(9,693)		(9,693)
Stock based compensation		272			272
Common stock grants awarded, net of unearned compensation of $92: 2,548 shares	5	(5)			
Balance, December 31, 2018	14,798	135,310	136,582	(8,076)	278,614
Net income			25,736		25,736
Other comprehensive income, net of income taxes				4,871	4,871
Dividends declared: $1.37 per share			(10,131)		(10,131)
Stock based compensation		554			554
Common stock grants awarded, net of unearned compensation of $147: 3,854 shares	8	(8)			
Share retirement: 14,428 shares	(29)	(605)			(634)
Balance, December 31, 2019	14,777	135,251	152,187	(3,205)	299,010
Net income			29,354		29,354
Other comprehensive income, net of income taxes				5,354	5,354
Dividends declared: $1.44 per share			(10,518)		(10,518)
Stock based compensation		570			570
Common stock grants awarded, net of unearned compensation of $520: 8,506 shares	17	(17)			
Share retirement: 181,417 shares	(363)	(6,530)			(6,893)
Balance, December 31, 2020	$ 14,431	$ 129,274	$ 171,023	$ 2,149	$ 316,877

See notes to consolidated financial statements

Peoples Financial Services Corp.
CONSOLIDATED STATEMENTS OF CASH FLOWS
(Dollars in thousands, except per share data)

Year Ended December 31,	2020	2019	2018
Cash flows from operating activities:			
Net income	$ 29,354	$ 25,736	$ 24,920
Adjustments to reconcile net income to net cash provided by operating activities:			
Depreciation of premises and equipment	2,900	3,083	2,333
Amortization of right-of-use lease asset	744	398	
Amortization of deferred loan fees, net	(2,236)	(164)	525
Amortization of intangibles	606	730	881
Amortization of low income housing partnerships	569	476	465
Provision for loan losses	7,400	6,100	4,200
Net unrealized (gain) loss on equity investment securities	35	(132)	(14)
Net (gain) loss on sale of other real estate owned	39	9	(21)
Net gain on sale of equity securities	(29)		
Gain from bank owned life insurance			(368)
Loans originated for sale	(43,780)	(15,901)	(13,194)
Proceeds from sale of loans originated for sale	44,832	15,753	12,650
Net gain on sale of loans originated for sale	(903)	(89)	(99)
Net amortization of investment securities	1,084	1,668	2,206
Net gain on sale of investment securities available-for-sale	(918)	(23)	
Net gain on sale of credit card loans held for sale			(291)
Increase in cash surrender value of life insurance	(774)	(755)	(757)
Deferred income tax expense (benefit)	(1,779)	394	(681)
Stock based compensation	570	554	272
Net change in:			
Accrued interest receivable	(1,274)	134	(179)
Other assets	(12,268)	(3,363)	816
Accrued interest payable	(541)	82	698
Other liabilities	13,549	2,389	(1,736)
Net cash provided by operating activities	37,180	37,079	32,626
Cash flows from investing activities:			
Proceeds from sales of investment securities available-for-sale	65,120	9,677	
Proceeds from repayments of investment securities:			
Available-for-sale	84,622	57,477	31,093
Held-to-maturity	427	697	898
Purchases of investment securities:			
Available-for-sale	(107,196)	(124,501)	(32,709)
Net redemption of restricted equity securities	4,804	(2,739)	1,100
Proceeds from sale of student loan portfolio			5,103
Proceeds from sale of credit card loan portfolio			2,698
Net increase in lending activities	(241,307)	(119,998)	(141,277)
Investment in bank owned life insurance	(6,500)		
Purchases of premises and equipment	(2,292)	(5,603)	(4,069)
Proceeds from the sale of premises and equipment	435		404
Proceeds from bank owned life insurance			672
Proceeds from sale of other real estate owned	647	269	1,281
Net cash used in investing activities	(201,240)	(184,721)	(134,806)
Cash flows from financing activities:			
Net increase in deposits	465,624	96,467	156,004
Proceeds from long-term debt		16,000	
Proceeds from Paycheck Protection Program Liquidity Facility	103,650		
Repayment of Paycheck Protection Program Liquidity Facility	(103,650)		
Proceeds from subordinated debentures	33,000		
Repayment of long-term debt	(17,964)	(21,173)	(11,828)
Net increase (decrease) in short-term borrowings	(102,150)	65,650	(37,175)
Retirement of common stock	(6,893)	(634)	
Cash dividends paid	(10,518)	(10,131)	(9,693)
Net cash provided by financing activities	361,099	146,179	97,308
Net increase in cash and cash equivalents	197,039	(1,463)	(4,872)
Cash and cash equivalents at beginning of period	31,153	32,616	37,488
Cash and cash equivalents at end of period	$ 228,192	$ 31,153	$ 32,616

Peoples Financial Services Corp.
CONSOLIDATED STATEMENTS OF CASH FLOWS
(Dollars in thousands, except per share data)

Year Ended December 31,	2020	2019	2018
Supplemental disclosures:			
Cash paid during the period for:			
Interest	$ 14,865	$ 17,786	$ 12,624
Income taxes	6,250	4,550	2,650
Noncash items:			
Transfers of loans to other real estate	$ 1,163	$ 421	$ 1,432
Origination of mortgage servicing rights	318	172	141
Initial recognition of right-of-use assets	899	6,523	
Initial recognition of lease liability	899	6,523	

See notes to consolidated financial statements

Peoples Financial Services Corp.
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
(Dollars in thousands, except per share data)

1. Summary of significant accounting policies:

Nature of operations:

Peoples Financial Services Corp., a bank holding company incorporated under the laws of Pennsylvania, provides a full range of financial services through its wholly-owned subsidiary, Peoples Security Bank and Trust Company ("Peoples Bank"), collectively, the "Company" or "Peoples". The Company services its retail and commercial customers through twenty-six full-service community banking offices located within Bucks, Lackawanna, Lebanon, Lehigh, Luzerne, Monroe, Montgomery, Northampton, Susquehanna and Wyoming Counties of Pennsylvania and Broome County of New York.

Peoples Bank is a state-chartered bank and trust company under the jurisdiction of the Pennsylvania Department of Banking and Securities and the Federal Deposit Insurance Corporation. Peoples Bank's primary product is loans to small and medium-sized businesses. Other lending products include one-to-four family residential mortgages and consumer loans. Peoples Bank primarily funds its loans by offering deposits to commercial enterprises and individuals. Deposit product offerings include checking accounts, savings accounts, money market accounts and certificates of deposits.

The Company faces competition primarily from commercial banks, thrift institutions and credit unions within its market, many of which are larger in terms of assets and capital. In addition, mutual funds and security brokers compete for various types of deposits, and consumer, mortgage, leasing and insurance companies compete for various types of loans and leases. Principal methods of competing for banking and permitted nonbanking services include price, nature of product, quality of service and convenience of location.

Peoples Financial Services Corp. and Peoples Bank are subject to regulations of certain federal and state regulatory agencies and undergo periodic examinations.

Basis of presentation:

The consolidated financial statements of the Company have been prepared in conformity with accounting principles generally accepted in the United States of America ("GAAP"), Regulation S-X and reporting practices applied in the banking industry. All significant intercompany balances and transactions have been eliminated in consolidation. The Company also presents herein condensed parent company only financial information regarding Peoples Financial Services Corp. ("Parent Company"). Prior period amounts are reclassified when necessary to conform with the current year's presentation. Such reclassifications had no effect on financial position or results of operations.

The Company has evaluated events and transactions occurring subsequent to the balance sheet date of December 31, 2020, for items that should potentially be recognized or disclosed in these consolidated financial statements. The evaluation was conducted through the date these consolidated financial statements were issued.

Estimates:

The preparation of consolidated financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the consolidated financial statements and the reported amounts of revenues and expenses during the reporting period. Significant estimates that are particularly susceptible to material change in the near term relate to the determination of the allowance for loan losses, fair value of financial instruments, the valuation of real estate acquired in connection with foreclosures or in satisfaction of loans, the valuation of deferred tax assets, the valuation of derivative instruments, determination of other-than-temporary impairment losses on securities and impairment of goodwill. Actual results could differ from those estimates.

Investment securities:

Investment securities are classified and accounted for as either held-to-maturity or available-for-sale securities based on management's intent at the time of acquisition. Management is required to reassess the appropriateness of such classifications at each reporting date. The Company classifies debt securities as held-to maturity when management has the positive intent and ability to hold such securities to maturity. Held-to-maturity securities are stated at cost, adjusted for amortization of premium and accretion of discount. Investment securities are designated as available-for-sale when they are to be held for indefinite periods of time as management intends to use such securities to implement asset/liability strategies or to sell them in response to changes in interest rates, prepayment risk, liquidity requirements, or other circumstances identified by management. Available-for-sale securities are reported at fair value, with unrealized gains and losses, net of income taxes, excluded from earnings and reported in a separate component of stockholders' equity. All marketable equity securities are accounted for at fair value with unrealized gains and losses reported in earnings. Estimated fair values for investment securities are based on quoted market prices from a national pricing service. Realized gains and losses are computed using the specific identification method and are included in noninterest income. Premiums on callable debt securities are amortized to the earliest call date from the maturity date. Premiums on non-callable securities are amortized and discounts are accreted using the interest method over the expected life of the security. Investment securities that are bought and held principally for the purpose of selling them in the near term, in order to generate profits from market appreciation, are classified as trading account securities. Transfers of securities between categories are recorded at fair value at the date of the transfer, with the accounting treatment of unrealized gains or losses determined by the category into which the security is transferred.

Management evaluates each investment security to determine if a decline in fair value below its amortized cost is an other-than-temporary impairment ("OTTI") at least quarterly, and more frequently when economic or market concerns warrant an evaluation. Factors considered in determining whether an other-than-temporary impairment was incurred include: (i) the length of time and the extent to which the fair value has been less than amortized cost; (ii) the financial condition and near-term prospects of the issuer; (iii) whether a decline in fair value is attributable to adverse conditions specifically related to the security or specific conditions in an industry or geographic area; (iv) the credit-worthiness of the issuer of the security; (v) whether dividend or interest payments have been reduced or have not been made; (vi) an adverse change in the remaining expected cash flows from the security such that the Company will not recover the amortized cost of the security; (vii) whether management intends to sell the security; and (viii) if it is more likely than not that management will be required to sell the security before recovery. If a decline is judged to be other-than-temporary, the individual security is written-down to fair value with the credit related component of the write-down included in earnings and the non-credit related component included in other comprehensive income or loss. The assessment of whether an other-than-temporary impairment exists involves a high degree of subjectivity and judgment and is based on information available to management at a point in time.

Transfers of Financial Assets

Transfers of financial assets are accounted for as sales, when control over the assets has been surrendered. Control over transferred assets is deemed to be surrendered when (1) the assets have been isolated from the Company, (2) the transferee obtains the right (free of conditions that constrain it from taking advantage of that right) to pledge or exchange the transferred assets, and (3) the Company does not maintain effective control over the transferred assets through an agreement to repurchase them before their maturity.

Loans held for sale:

Loans held for sale consist of one-to-four family residential mortgages originated and intended for sale in the secondary market. The loans are carried in aggregate at the lower of cost or estimated market value, based upon current delivery prices in the secondary mortgage market. Net unrealized losses are recognized through a valuation allowance by corresponding charges to income. Gains or losses on the sale of these loans are recognized in noninterest income at the time of sale using the specific identification method. Loan origination fees, net of certain direct loan origination costs, are included in net gains or losses upon the sale of the related mortgage loan.

Loans, net:

Loans that management has the intent and ability to hold for the foreseeable future or until maturity or payoff are stated at their outstanding unpaid principal balances, net of deferred fees or costs. Interest income is accrued on the principal amount outstanding. Loan origination fees, net of certain direct origination costs, are deferred and recognized over the contractual life of the related loan as an adjustment to yield using the effective interest method. Premiums and discounts on purchased loans are amortized as adjustments to interest income using the effective interest method. Delinquency fees are recognized in income at the time when they are paid by customer.

Transfers of financial assets, which include loan participation sales, are accounted for as sales, when control over the assets has been surrendered. Control over transferred assets is deemed to be surrendered when: (i) the assets have been isolated from the Company; (ii) the transferee obtains the right, free of conditions that constrain it from taking advantage of that right, to pledge or exchange the transferred assets and (iii) the Company does not maintain effective control over the transferred assets through an agreement to repurchase them before their maturity.

The loan portfolio is segmented into commercial and retail loans. Commercial loans consist of commercial, commercial real estate, municipal and other related tax free loans. Retail loans consist of residential real estate and other consumer loans.

The Company makes commercial loans for real estate development and other business purposes required by the customer base. The Company's credit policies establish advance rates against the different forms of collateral that can be pledged against various commercial loans. Typically, the majority of loans will be underwritten to a percentage of their underlying collateral values such as real estate values, equipment, eligible accounts receivable and inventory. Individual loan advance rates may be higher or lower depending upon the financial strength of the borrower and/or term of the loan. Generally, assets financed through commercial loans are used for the operations of the business. Repayment for these types of loans generally comes from the cash flow of the business or the ongoing conversion of assets. Commercial real estate loans include construction, mini-perm, or longer term loans financing commercial properties. Repayment of these loans are generally dependent upon either the ongoing business cash flow from an owner occupied property or the lease/rental income or sale of a non-owner occupied property. Commercial real estate loans typically require a loan to value of not greater than 80% and vary in terms. Commercial and commercial real estate loans generally have higher credit risk compared to residential mortgage loans and consumer loans, as they typically involve larger loan balances concentrated with single borrowers or groups of borrowers. In addition, the payment expectations on loans secured by income-producing properties typically depend on the successful operations of the related business and thus may be subject to a greater extent to adverse conditions in the real estate market and in the general economy.

Loans secured by commercial real estate generally have larger balances and involve a greater degree of risk than one-to-four family residential mortgage loans. Of primary concern in commercial real estate lending is the borrower's and any guarantor's creditworthiness and the feasibility and cash flow potential of the financed project. Additional considerations include: location, market and geographic concentration risks, loan to value, strength of guarantors and quality of tenants. Payments on loans secured by income properties often depend on successful operation and management of the properties. As a result, repayment of such loans may be subject to a higher level of risk than residential real estate loans, which could be caused by unfavorable conditions in the real estate market or the economy. To effectively monitor loans on income properties, the Company requires borrowers and loan guarantors, if any, to provide annual financial statements on commercial real estate loans and rent rolls where applicable. In reaching a decision on whether to make a commercial real estate loan, the Company considers and reviews a cash flow analysis of the borrower and guarantor, when applicable. In addition, the Company evaluates business cash flows, if applicable, net operating income of the property, the borrower's expertise, credit history and the value of the underlying property. The Company has generally required that the properties securing these real estate loans have debt service coverage ratios, which is net cash flow before debt service to debt service, of at least 1.2 times. An environmental report is obtained when the possibility exists that hazardous materials may have existed on the site, or the site may have been impacted by adjoining properties that handled hazardous materials.

Commercial loans are generally made on the basis of a business entity or individual borrower's ability to make repayment from business cash flows or individual borrowers' employment and other income. Commercial business loans tend to have a slightly higher risk than commercial real estate loans because collateral usually consists of business assets versus real estate. Further, any collateral securing such loans may depreciate over time and could be difficult to appraise and liquidate. As a result, repayment of commercial business loans may depend substantially on the success of the business itself.

Residential mortgages, including home equity loans, are secured by the borrower's residential real estate in either a first or second lien position. Residential mortgages have varying loan rates depending on the financial condition of the borrower, loan to value ratio and term. Residential mortgages may have amortizations up to 30 years.

Consumer loans include installment loans, car loans, and overdraft lines of credit. These loans are both secured and unsecured. Consumer loans may entail greater risk than do residential mortgage loans, particularly in the case of consumer loans that are unsecured. Repossessed collateral for a defaulted consumer loan may not provide an adequate source of repayment for the outstanding loan and a small remaining deficiency often does not warrant further substantial collection efforts against the borrower. Consumer loan collections depend on the borrower's continuing financial stability, and therefore are likely to be adversely affected by various factors, including job loss, divorce, illness or personal bankruptcy. Furthermore, the application of various federal and state laws, including federal and state insolvency laws, may limit the amount that can be recovered on such loans.

Off-balance sheet financial instruments:

In the ordinary course of business, the Company has entered into off-balance sheet financial instruments consisting of commitments to extend credit, unused portions of lines of credit and standby letters of credit. These financial instruments are recorded in the consolidated financial statements when they are funded. Fees on commercial letters of credit and on unused available lines of credit are recorded as interest and fees on loans and are included in interest income when paid. The Company records an allowance for off-balance sheet credit losses, if deemed necessary, separately as a liability.

Nonperforming assets:

Nonperforming assets consist of nonperforming loans and other real estate owned. Nonperforming loans include nonaccrual loans, troubled debt restructured loans and accruing loans past due 90 days or more. Past due status is based on contractual terms of the loan. Generally, a loan is classified as nonaccrual when it is determined that the collection of all or a portion of interest or principal is doubtful or when a default of interest or principal has existed for 90 days or more, unless the loan is well secured and in the process of collection. When a loan is placed on nonaccrual, interest accruals discontinue and uncollected accrued interest is reversed against income in the current period. Interest collections after a loan has been placed on nonaccrual status are credited to a suspense account until either the loan is returned to performing status or charged-off. The interest accumulated in the suspense account is credited to income over the remaining life of the loan using the effective yield method if the nonaccrual loan is returned to performing status. However, if the nonaccrual loan is charged-off, the accumulated interest is applied as a reduction to principal at the time the loan is charged-off. A nonaccrual loan is returned to performing status when the loan is current as to principal and interest and has performed according to the contractual terms for a minimum of six months.

Troubled debt restructured loans are loans with original terms, interest rate, or both, that have been modified as a result of a deterioration in the borrower's financial condition and a concession has been granted that the Company would not otherwise consider. Unless on nonaccrual, interest income on these loans is recognized when earned, using the interest method. The Company offers a variety of modifications to borrowers that would be considered concessions. The modification categories offered can generally fall within the following categories:

- Rate Modification — A modification in which the interest rate is changed to a below market rate.
- Term Modification — A modification in which the maturity date, timing of payments or frequency of payments is changed.

- Interest Only Modification — A modification in which the loan is converted to interest only payments for a period of time.

- Payment Modification — A modification in which the dollar amount of the payment is changed, other than an interest only modification described above.

- Combination Modification — Any other type of modification, including the use of multiple categories above.

The Company segments loans into risk categories based on relevant information about the ability of borrowers to service their debt such as current financial information, historical payment experience, credit documentation, public information, and current economic trends, among other factors. Loans are individually analyzed for credit risk by classifying them within the Company's internal risk rating system. The Company's risk rating classifications are defined as follows:

- Pass — A loan to borrowers with acceptable credit quality and risk that is not adversely classified as Substandard, Doubtful, Loss nor designated as Special Mention.

- Special Mention — A loan that has potential weaknesses that deserves management's close attention. If left uncorrected, these potential weaknesses may result in deterioration of the repayment prospects for the loan or in the institution's credit position at some future date. Special Mention loans are not adversely classified since they do not expose the Company to sufficient risk to warrant adverse classification.

- Substandard — A loan that is inadequately protected by the current sound worth and paying capacity of the obligor or of the collateral pledged, if any. Loans so classified must have a well-defined weakness or weaknesses that jeopardize the liquidation of the debt. They are characterized by the distinct possibility that the bank will sustain some loss if the deficiencies are not corrected.

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

- Loss — A loan classified as Loss is considered uncollectible and of such little value that its continuance as bankable loans is not warranted. This classification does not mean that the loan has absolutely no recovery or salvage value, but rather it is not practical or desirable to defer writing off this basically worthless asset even though partial recovery may be effected in the future.

Other real estate owned is comprised of properties acquired through foreclosure proceedings or in-substance foreclosures. A loan is classified as in-substance foreclosure when the Company has taken possession of the collateral regardless of whether formal foreclosure proceedings take place. Other real estate owned is included in other assets and recorded at fair value less cost to sell at the time of acquisition, establishing a new cost basis. Any excess of the loan balance over the recorded value is charged to the allowance for loan losses. Subsequent declines in the recorded values of the properties prior to their disposal and costs to maintain the assets are included in other expenses. Any gain or loss realized upon disposal of other real estate owned is included in noninterest expense.

Allowance for loan losses:

The allowance for loan losses represents management's estimate of losses inherent in the loan portfolio as of the balance sheet date. The allowance for loan losses account is maintained through a provision for loan losses charged to earnings. Loans, or portions of loans, determined to be confirmed losses are charged against the allowance account and subsequent recoveries, if any, are credited to the account. A loss is considered confirmed when information available at the financial statement date indicates the loan, or a portion thereof, is uncollectible. Nonaccrual, troubled debt restructured and loans deemed impaired at the time of acquisition are reviewed monthly to determine if carrying value reductions are warranted or if these classifications should be changed. Consumer loans are considered losses and charged-off when they are 120 days past due.

Management evaluates the adequacy of the allowance for loan losses account quarterly. This assessment is based on past charge-off experience, known and inherent risks in the portfolio, adverse situations that may affect the borrower's ability to repay, the estimated value of underlying collateral, composition of the loan portfolio, current economic conditions and other relevant factors. This evaluation is inherently subjective as it requires material estimates that may be susceptible to significant revision as more information becomes available. Regulators, in reviewing the loan portfolio as part of the scope of a regulatory examination, may require the Company to increase its allowance for loan losses or take other actions that would require the Company to increase its allowance for loan losses.

The allowance for loan losses is maintained at a level believed to be adequate to absorb probable credit losses related to specifically identified loans, as well as probable incurred losses inherent in the remainder of the loan portfolio as of the balance sheet date. The allowance for loan losses consists of an allocated element and an unallocated element. The allocated element consists of a specific allowance for impaired loans individually evaluated and a formula portion for loss contingencies on those loans collectively evaluated.

A loan is considered impaired when, based on current information and events, it is probable that the Company will be unable to collect all amounts due according to the contractual terms of the loan agreement. All amounts due according to the contractual terms means that both the contractual interest and principal payments of a loan will be collected as scheduled in the loan agreement. Factors considered by management in determining impairment include payment status, ability to pay and the probability of collecting scheduled principal and interest payments when due. Loans that experience insignificant payment delays and payment shortfalls generally are not classified as impaired. Management determines the significance of payment delays and payment shortfalls on a case-by-case basis, taking into consideration all of the circumstances surrounding the loan and the borrower, including the length of the delay, the reasons for the delay, the borrower's prior payment record, and the amount of the shortfall in relation to the principal and interest owed. The Company recognizes interest income on impaired loans, including the recording of cash receipts, for nonaccrual, restructured loans or accruing loans depending on the status of the impaired loan. Loans considered impaired are measured for impairment based on the present value of expected future cash flows discounted at the loan's effective interest rate or the fair value of the collateral if the loan is collateral dependent. If the present value of expected future cash flows discounted at the loan's effective interest rate or the fair value of the collateral, if the loan is collateral dependent, is less than the recorded investment in the loan, a specific allowance for the loan will be established.

The formula portion of the allowance for loan losses relates to large pools of smaller-balance homogeneous loans and those identified loans considered not individually impaired having similar characteristics as these loan pools. Loss contingencies for each of the major loan pools are determined by applying a total loss factor to the current balance outstanding for each individual pool. The total loss factor is comprised of a historical loss factor using a loss migration method plus qualitative factors, which adjusts the historical loss factor for changes in trends, conditions and other relevant factors that may affect repayment of the loans in these pools as of the evaluation date. Loss migration involves determining the percentage of each pool that is expected to ultimately result in loss based on historical loss experience. The historical loss factor for each pool is a weighted average of the Company's historical net charge-off ratio for the most recent rolling twelve quarters. Management adjusts these historical loss factors by qualitative factors that represents a number of environmental risks that may cause estimated credit losses associated with the current portfolio to differ from historical loss experience. These environmental risks include: (i) changes in lending policies and procedures including underwriting standards and collection, charge-off and recovery practices; (ii) changes in the composition and volume of the portfolio; (iii) changes in national, local and industry conditions, including the effects of such changes on the value of underlying collateral for collateral-dependent loans; (iv) changes in the volume and severity of classified loans, including past due, nonaccrual, troubled debt restructures and other loan modifications; (v) changes in the levels of, and trends in, charge-offs and recoveries; (vi) the existence and effect of any concentrations of credit and changes in the level of such concentrations; (vii) changes in the experience, ability and depth of lending management and other relevant staff; (viii) changes in the quality of the loan review system and the degree of oversight by the board of directors; and (ix) the effect of external factors such as competition, pandemics and legal and regulatory requirements on the level of estimated credit losses in the current loan portfolio. Each environmental risk factor is assigned a value to reflect improving, stable or declining conditions based on management's best judgment using relevant information available at the time of the evaluation. Adjustments to the factors are supported through documentation of changes in conditions in a narrative accompanying the allowance for loan loss calculation.

Management believes the level of the allowance for loan losses was adequate to absorb probable credit losses inherent in the loan portfolio as of December 31, 2020.

Revenue from Contracts with Customers:

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

The Company's primary sources of revenue are derived from interest and dividends earned on loans, investment securities, and other financial instruments that are not within the scope of Topic 606. The Company has evaluated the nature of its contracts with customers and determined that further disaggregation of revenue from contracts with customers into more granular categories beyond what is presented in the consolidated statements of income was not necessary. The Company generally fully satisfies its performance obligations on its contracts with customers as services are rendered and the transaction prices are typically fixed; charged either on a periodic basis or based on activity. The following is a discussion of revenues within the scope of the guidance:

- *Service charges, fees, commissions and other*. Service charges, fees and commissions on deposit accounts include fees for banking services provided, overdrafts and non-sufficient funds. Revenue is generally recognized in accordance with published deposit account agreements for retail accounts or contractual agreements for commercial accounts. The Company's deposit services also include our ATM and debit card interchange revenue that is presented gross of the associated costs. Interchange revenue is generated by the Company's deposit customers' usage and volume of activity. Interchange rates are not controlled by the Company, which effectively acts as processor that collects and remits payments associated with customer debit card transactions.
- *Commission and fees on fiduciary activities.* Commission and fees on fiduciary activities includes fees and commissions from investment management, administrative and advisory services primarily for individuals, and to a lesser extent, partnerships and corporations. Revenue is recognized on an accrual basis at the time the services are performed and when the Company has a right to invoice and are based on either the market value of the assets managed or the services provided.
- *Wealth management income.* Wealth management income includes fees and commissions charged when the Company arranges for another party to transfer brokerage services to a customer. The fees and commissions under this agent relationship are based upon stated fee schedules based upon the type of transaction, volume, and value of the services provided.
- *Merchant services income*. Merchant services revenue is derived from a third party vendor that processes credit card transactions on behalf of the Company's merchant customers. Merchant services revenue is primarily comprised of residual fee income based on the referred merchant's processing volumes and/or margin.

Premises and equipment, net:

Land is stated at cost. Premises, equipment and leasehold improvements are stated at cost less accumulated depreciation and amortization. The cost of routine maintenance and repairs is expensed as incurred. The cost of major replacements, renewals and betterments is capitalized. When assets are retired or otherwise disposed of, the cost and related accumulated depreciation and amortization are eliminated and any resulting gain or loss is reflected in noninterest income. Depreciation and amortization are computed principally using the straight-line method based on the following estimated useful lives of the related assets, or in the case of leasehold improvements, to the expected terms of the leases, if shorter:

Premises and leasehold improvements	7 – 40 years
Furniture, fixtures and equipment	3 – 10 years

Goodwill and other intangible assets, net:

The Company accounts for its acquisitions using the purchase accounting method. Purchase accounting requires the total purchase price to be allocated to the estimated fair values of assets acquired and liabilities assumed, including certain intangible assets that must be recognized. Typically, this allocation results in the purchase price exceeding the fair value of net assets acquired, which is recorded as goodwill. Core deposit intangibles are a measure of the value of checking, money market and savings deposits acquired in business combinations accounted for under the purchase method. Core deposit intangibles and other identified intangibles with finite useful lives are amortized using the sum of the year's digits over their estimated useful lives of up to ten years.

Goodwill and other intangible assets are tested for impairment annually or when circumstances arise indicating impairment may have occurred. In making this assessment that impairment has occurred, management considers a number of factors including, but not limited to, operating results, business plans, economic projections, anticipated future cash flows, and current market data. There are inherent uncertainties related to these factors and management's judgment in applying them to the analysis of impairment. Changes in economic and operating conditions, as well as other factors, could result in impairment in future periods. Any impairment losses arising from such testing would be reported in the consolidated statements of income and comprehensive income as a separate line item within operations. There were no impairment losses recognized as a result of periodic impairment testing in each of the three-years ended December 31, 2020.

Mortgage servicing rights:

Mortgage servicing rights are recognized as a separate asset when acquired through sales of loan originations. The Company determines a mortgage servicing right by allocating the total costs incurred between the loan sold and the servicing right, based on their relative fair values at the date of the sale. Mortgage servicing rights are included in other assets and are amortized into noninterest income in proportion to, and over the period of, the estimated future net servicing income of the underlying mortgage loans. In addition, mortgage servicing rights are evaluated for impairment at each reporting date based on the fair value of those rights. For purposes of measuring impairment, the rights are stratified by loan type, term and interest rate. The amount of impairment recognized, through a valuation allowance, is the amount by which the mortgage servicing rights for a stratum exceed their fair value.

Restricted equity securities:

As a member of the Federal Home Loan Bank of Pittsburgh ("FHLB"), the Company is required to purchase and hold stock in the FHLB to satisfy membership and borrowing requirements. This stock is restricted in that it can only be redeemed by the FHLB or transferred to another member institution, and all redemptions of FHLB stock must be at par. As a result of these restrictions, FHLB stock is unlike other investment securities as there is no trading market for FHLB stock and the transfer price is determined by FHLB membership rules and not by market participants. The carrying value of restricted stock is included in other assets.

Bank owned life insurance:

The Company invests in bank owned life insurance ("BOLI") as a source of funding for employee benefit expenses. BOLI involves the purchasing of life insurance on certain employees. The Company is the owner and beneficiary of the policies. This life insurance investment is carried at the cash surrender value of the underlying policies. Income from increases in cash surrender value of the policies is included in noninterest income. The policies can be liquidated, if necessary, with associated tax costs. However, the Company intends to hold these policies and, accordingly, the Company has not provided for income taxes on the earnings from the increase in cash surrender value.

Pension and post-retirement benefit plans:

The Company sponsors a separate Employee Stock Ownership Plan ("ESOP") and Retirement Profit Sharing 401(k) Plan and maintains Supplemental Executive Retirement Plans ("SERPs") and an employee pension plan, which is currently frozen. The Company also provides post-retirement benefit plans other than pensions, consisting principally of life insurance benefits, to eligible retirees. The liabilities and annual income or expense of the Company's pension and other post-retirement benefit plans are determined using methodologies that involve several actuarial assumptions, the most significant of which are the discount rate and the long-term rate of asset return, based on the market-related value of assets. The fair values of plan assets are determined based on prevailing market prices or estimated fair value for investments with no available quoted prices.

Statements of Cash Flows:

Cash and cash equivalents include cash on hand, cash items in the process of collection, noninterest-bearing and interest-bearing deposits in other banks and federal funds sold.

Derivative Instruments and Hedging Activities:

The Company records all derivatives on the balance sheet at fair value. The accounting for changes in the fair value of derivatives depends on the intended use of the derivative, whether the Company has elected to designate a derivative in a hedging relationship and apply hedge accounting and whether the hedging relationship has satisfied the criteria necessary to apply hedge accounting. Derivatives designated and qualifying as a hedge of the exposure to changes in the fair value of an asset, liability, or firm commitment attributable to a particular risk, such as interest rate risk, are considered fair value hedges. Derivatives designated and qualifying as a hedge of the exposure to variability in expected future cash flows, or other types of forecasted transactions, are considered cash flow hedges. Derivatives may also be designated as hedges of the foreign currency exposure of a net investment in a foreign operation. Hedge accounting generally provides for the matching of the timing of gain or loss recognition on the hedging instrument with the recognition of the changes in the fair value of the hedged asset or liability that are attributable to the hedged risk in a fair value hedge or the earnings effect of the hedged forecasted transactions in a cash flow hedge. The Company may enter into derivative contracts that are intended to economically hedge certain of its risk, even though hedge accounting does not apply or the Company elects not to apply hedge accounting.

The Company has elected to measure the credit risk of its derivative financial instruments that are subject to master netting agreements on a net basis by counterparty portfolio.

Fair value of financial instruments:

The Company uses fair value measurements to record fair value adjustments to certain assets and liabilities and to determine fair value disclosure under GAAP. Fair value estimates are calculated without attempting to estimate the value of anticipated future business and the value of certain assets and liabilities that are not considered financial. Accordingly, such assets and liabilities are excluded from disclosure requirements.

Fair value is the price that would be received to sell an asset or transfer a liability in an orderly transaction between market participants at the measurement date. Fair value is best determined based upon quoted market prices. In cases where quoted market prices are not available, fair values are based on estimates using present value or other valuation techniques. Those techniques are significantly affected by the assumptions used, including the discount rate and estimates of future cash flows. In that regard, the derived fair value estimates cannot be substantiated by comparison to independent markets. In many cases, these values cannot be realized in immediate settlement of the instrument.

Current fair value guidance provides a consistent definition of fair value, which focuses on exit price in an orderly transaction that is not a forced liquidation or distressed sale between participants at the measurement date under current market conditions. If there has been a significant decrease in the volume and level of activity for the asset or liability, a change in valuation technique or the use of multiple valuation techniques may be appropriate. In such instances, determining the price at which willing market participants would transact at the measurement date under current market conditions depends on the facts and circumstances and requires the use of significant judgment. The fair value is a reasonable point within the range that is most representative of fair value under current market conditions.

In accordance with GAAP, the Company groups its assets and liabilities generally measured at fair value into three levels based on market information or other fair value estimates in which the assets and liabilities are traded or valued and the reliability of the assumptions used to determine fair value. These levels include:

- Level 1: Unadjusted quoted prices of identical assets or liabilities in active markets that the entity has the ability to access as of the measurement date.

- Level 2: Significant other observable inputs other than Level 1 prices such as quoted prices for similar assets or liabilities; quoted prices in markets that are not active; or other inputs that are observable or can be corroborated by observable market data.

- Level 3: Significant unobservable inputs that reflect a reporting entity's own assumptions about the assumptions that market participants would use in pricing an asset or liability.

The following methods and assumptions were used by the Company to construct the summary table in Note 14 containing the fair values and related carrying amounts of financial instruments measured at fair value:

Investment securities: The fair values of marketable equity securities are based on quoted market prices from active exchange markets. The fair values of debt securities are based on pricing from a matrix pricing model and quoted market prices.

Impaired loans: Fair values for impaired loans are estimated using discounted cash flow analysis determined by the loan review function or underlying collateral values, where applicable.

Interest rate swaps and floors: Values of these instruments are obtained through an independent pricing source utilizing information which may include market observed quotations for swaps, Libor rates, forward rates and rate volatility. Derivative contracts create exposure to interest rate movements as well as risks from the potential of non-performance of the counterparty.

Advertising:

The Company follows the policy of charging marketing and advertising costs to expense as incurred. Advertising expense for the years ended December 31, 2020, 2019 and 2018 was $462, $873 and $720, respectively.

Income taxes:

Deferred income taxes are provided on the balance sheet method whereby deferred tax assets are recognized for deductible temporary differences and deferred tax liabilities are recognized for taxable temporary differences. Temporary differences are the differences between the reported amounts of assets and liabilities and their tax basis. Deferred tax assets are reduced by a valuation allowance when, in the opinion of management, it is more likely than not that some portion of the deferred tax assets will not be realized. Deferred tax assets and liabilities are adjusted for the effects of changes in tax laws and rates on the effective date. A tax position is recognized as a benefit only if it is more likely than not that the tax position would be sustained in a tax examination, with a tax examination being presumed to occur. The amount recognized is the largest amount of tax benefit that has a likelihood of being realized on examination of more than 50 percent. For tax positions not meeting the more likely than not threshold, no tax benefit is recorded. Under the more likely than not threshold guidelines, the Company believes no significant uncertain tax positions exist, either individually or in the aggregate, that would give rise to the non-recognition of an existing tax benefit. The Company had no material unrecognized tax benefits or accrued interest and penalties for any year in the three-year period ended December 31, 2020.

As applicable, the Company recognizes accrued interest and penalties assessed as a result of a taxing authority examination through income tax expense. The Company files consolidated income tax returns in the United States of America and various state jurisdictions. With limited exception, the Company is no longer subject to federal and state income tax examinations by taxing authorities for years before 2017.

Other comprehensive income (loss):

The components of other comprehensive income (loss) and their related tax effects are reported in the consolidated statements of income and comprehensive income. The accumulated other comprehensive income (loss) included in the Consolidated Balance Sheets relates to net unrealized gains and losses on investment securities available-for-sale, the net change in derivative fair value and the unfunded benefit plan amounts which include prior service costs and unrealized net losses.

Earnings per share:

Basic earnings per share represent income available to common stockholders divided by the weighted-average number of common shares outstanding during the period. Diluted earnings per share reflect 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 that may be issued by the Company relate to awards of restricted stock units, and are determined using the treasury stock method.

	2020		2019		2018	
For the Year Ended December 31	**Basic**	**Diluted**	**Basic**	**Diluted**	**Basic**	**Diluted**
Net income	$ 29,354	$ 29,354	$ 25,736	$ 25,736	$ 24,920	$ 24,920
Average common shares outstanding	7,304,956	7,337,843	7,395,429	7,412,369	7,397,797	7,402,900
Earnings per share	$ 4.02	$ 4.00	$ 3.48	$ 3.47	$ 3.37	$ 3.37

Stock-based compensation:

The Company recognizes all share-based payments to employees in the consolidated statements of income and comprehensive income based on their fair values. The fair value of such equity instruments is recognized as an expense in the consolidated financial statements as services are performed. The Company has granted restricted stock awards and units to employees at a price equal to the fair value of the shares underlying the awards at the date of grant. The fair value of restricted stock awards and units are equivalent to the fair value on the date of grant and is amortized over the vesting period.

Recent accounting standards:

In June 2016, the Financial Accounting Standards Board ("FASB") issued Accounting Standards Update ("ASU") 2016-13, "Financial Instruments-Credit Losses (Topic 326): Measurement of Credit Losses on Financial Instruments." This ASU will have a material impact on the Company's calculation and accounting for its allowance for loan losses as well as credit losses related to investment securities available-for-sale. A summary of significant provisions of this ASU is as follows:

- The ASU requires that a financial asset (or a group of financial assets) measured at amortized cost basis be presented, net of a valuation allowance for credit losses, at an amount expected to be collected on the financial asset(s), and that the income statement include the measurement of credit losses for newly recognized financial assets as well as changes in expected losses on previously recognized financial assets. The provisions of this ASU require measurement of expected credit losses based on relevant information including past events, historical experience, current conditions, and reasonable and supportive forecasts that affect the collectability of the asset. The provisions of this ASU differ from current GAAP in that current GAAP generally delays recognition of the full amount of credit losses until the loss is probable of occurring.

- The amendments in the ASU retain many of the disclosure requirements related to credit quality in current GAAP, updated to reflect the change from an incurred loss methodology to an expected credit loss methodology. In addition, the ASU requires that disclosure of credit quality indicators in relation to the amortized cost of financing receivables, a current requirement, be further disaggregated by year of origination.
- This ASU requires that credit losses on available-for-sale debt securities be presented as an allowance rather than as a write-down, and limits the amount of the allowance for credit losses to the amount by which the fair value is below amortized cost. For purchased investment securities available-for-sale with a more-than-insignifcant amount of credit deterioration since origination, the ASU requires an allowance be determined in a manner similar to other investment securities available-for-sale; however, the initial allowance would be added to the purchase price, with only subsequent changes in the allowance recorded in credit loss expense, and interest income recognized at the effective rate excluding the discount embedded in the purchase price related to estimated credit losses at acquisition.
- In November 2019, the FASB voted to defer the adoption date for smaller reporting companies from 2020 to 2023. The Company qualified as a smaller reporting company at that time and therefore guidance is effective for the Company in 2023. The Company will record the effect of implementing this ASU through a cumulative-effect adjustment through retained earnings as of the beginning of the reporting period in which Topic 326 is effective.

We are evaluating the impact of the ASU on our consolidated financial statements. In addition to our allowance for loan losses, we will also record an allowance for credit losses on debt securities instead of applying the impairment model currently utilized. The amount of the adjustments will be impacted by each portfolio's composition and credit quality at the adoption date as well as economic conditions and forecasts at that time.

In January 2017, the FASB issued ASU 2017-04, "Simplifying the Test for Goodwill Impairment," - Intangibles - Goodwill and Other (Topic 350): Simplifying the Test for Goodwill Impairment. The amendments in this ASU simplify how an entity is required to test goodwill for impairment by eliminating the requirement to calculate the implied fair value of goodwill to measure a goodwill impairment charge. The Company adopted this guidance effective January 1, 2020. Adoption of this ASU did not have a material impact on the Company's consolidated financial statements.

In August 2018, the FASB issued ASU 2018-14, "Compensation - Retirement Benefits - Defined Benefit Plans - General (Subtopic 715-20)", which provides changes to the disclosure requirements for defined benefit plans. The amended guidance modifies the disclosure requirements for employers that sponsor defined benefit pension or other postretirement plans. The amendments are a result of the disclosure framework project that focuses on improvements to the effectiveness of disclosures in the notes to financial statements. The amendments remove and add certain disclosure requirements. The disclosure requirements being removed relating to public companies are (1) the amounts in accumulated other comprehensive income expected to be recognized as components of net periodic benefit cost over the next fiscal year, (2) the amount and timing of plan assets expected to be returned to the employer, (3) the 2001 disclosure requirement relating to Japanese Welfare Pension Insurance Law, (4) related party disclosures about the amount of future annual benefits covered by insurance, and (5) the effects of a one-percentage-point change in assumed health care cost trends on the benefit cost and obligation. The disclosure requirements being added relating to public companies are (1) the weighted-average interest crediting rates for cash balance plans, and (2) an explanation of the reasons for significant gains and losses related to changes in the benefit obligation for the period. The Company adopted this guidance effective January 1, 2020. Adoption of this ASU did not have a material impact on its disclosures to the consolidated financial statements.

In December 2019, the FASB issued ASU 2019-12, "Income Taxes (Topic 740): Simplifying the Accounting for Income Taxes", which aims to simplify the accounting for income taxes by removing certain exceptions to the general principles and also simplification of areas such as franchise taxes, step-up in tax basis goodwill, separate entity financial statements and interim recognition of enactment of tax laws or rate changes. The ASU will be effective for the Company on January 1, 2021. The Company is currently evaluating the potential impact of ASU 2019-12 on the consolidated financial statements.

In March 2020, the FASB issued ASU 2020-04, "Reference Rate Reform (Topic 848): Facilitation of the Effects of Reference Rate Reform on Financial Reporting", which provides optional expedients and exceptions for a limited time period to ease the potential burden in accounting for reference rate reform on financial reporting. The amendments in ASU 2020-04 are elective for entities with contracts, including derivative contracts, that reference LIBOR or some other reference rate that are expected to be discontinued. For the Company's cash flow hedges, ASU 2020-04 allows: (i) an entity to change the reference rate without having to designate the hedging relationship; (ii) for cash flow hedges in which the designated hedged risk is LIBOR, allows an entity to assert that it remains probable that the hedged forecasted transaction will occur; and (iii) allows an entity to change the designated method used to assess hedge effectiveness and simplifies or temporarily suspends the assessment of hedge effectiveness for hedging relationships. ASU 2020-04 must be applied prospectively and was effective immediately upon issuance and remains effective through December 31, 2022.

The Company adopted the amendments in ASU 2020-04 as of the March 12, 2020 issuance date, on a prospective basis. The adoption did not have an immediate direct impact to the consolidated financial statements. As contracts are modified through December 2022, we will assess the impact based on this guidance. The Company does not expect there will be a material impact to the consolidated financial statements.

In October 2020, the FASB issued ASU 2020-08, Codification Improvements to Subtopic 310-20, Receivables-Nonrefundable Fees and Other Costs. ASU 2020-08 clarifies that the Company should reevaluate whether a callable debt security is within the scope of the guidance of premium amortization of purchased callable debt securities, at each reporting date. If there is no remaining premium or if there are no further call dates the Company shall reset the effective yield using the payment terms of the debt security. ASU 2020-08 is effective for fiscal years and interim periods within those fiscal years, beginning after December 15, 2020 and early application is not permitted. The guidance is not expected to have a material impact on the consolidated financial statements.

2. Cash and due from banks:

On March 26, 2020, the Board of Governors of the Federal Reserve System eliminated the reserve requirement for all depository institutions. Prior to this date, the Company was required to maintain average reserve balances as established by the Federal Reserve Bank. The required reserve balance was $2,545 at December 31, 2019.

3. Investment securities:

The amortized cost and fair value of investment securities aggregated by investment category at December 31, 2020 and 2019 are summarized as follows:

December 31, 2020	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
Available-for-sale:				
U.S. Treasury securities	$ 18,478	$ 427		$ 18,905
U.S. government-sponsored enterprises	63,834	1,354		65,188
State and municipals:				
Taxable	53,297	2,099	$ 30	55,366
Tax-exempt	53,977	3,054	37	56,994
Residential mortgage-backed securities:				
U.S. government agencies	3,553	154		3,707
U.S. government-sponsored enterprises	79,457	1,930	136	81,251
Commercial mortgage-backed securities:				
U.S. government-sponsored enterprises	12,619	881		13,500
Corporate debt securities	1,000			1,000
Total	$ 286,215	$ 9,899	$ 203	$ 295,911
Held-to-maturity:				
Tax-exempt state and municipals	$ 6,849	$ 275	$	$ 7,124
Residential mortgage-backed securities:				
U.S. government agencies	21			21
U.S. government-sponsored enterprises	355	13		368
Total	$ 7,225	$ 288	$	$ 7,513

December 31, 2019	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
Available-for-sale:				
U.S. Treasury securities	$ 23,966	$ 162		$ 24,128
U.S. government-sponsored enterprises	87,156	181	$ 227	87,110
State and municipals:				
Taxable	35,418	295	815	34,898
Tax-exempt	59,127	1,056	20	60,163
Residential mortgage-backed securities:				
U.S. government agencies	8,368	112	10	8,470
U.S. government-sponsored enterprises	101,914	1,011	77	102,848
Commercial mortgage-backed securities:				
U.S. government-sponsored enterprises	12,694	171	4	12,861
Total	$ 328,643	$ 2,988	$ 1,153	$ 330,478
Held-to-maturity:				
Tax-exempt state and municipals	$ 6,852	$ 208	$	$ 7,060
Residential mortgage-backed securities:				
U.S. government agencies	31			31
U.S. government-sponsored enterprises	773	25		798
Total	$ 7,656	$ 233	$	$ 7,889

The Company had net unrealized gains on available-for-sale securities of $7,660, net of deferred income taxes of $2,036 at December 31, 2020, and net unrealized gains on available-for-sale securities of $1,450, net of deferred income taxes of $385, at December 31, 2019. During 2020, the Company sold a pool of low-yielding short-term municipal bonds and two mortgage-backed securities and received proceeds totaling $64,841. Gross gains of $923 and gross losses of $5 were realized on the sale of investment securities in 2020. During 2019, the Company sold a pool of municipal bonds and received proceeds totaling $9,677 and realized gross gains of $66 and gross losses of $43.

At December 31, 2020, our equity security portfolio consisted of stock of one financial institution. During 2020, the Company sold its entire stock position in one other equity holding and received proceeds of $279 and recognized a gain of $29. At December 31, 2020 and December 31, 2019, we had $138 thousand and $423 thousand, respectively, in equity securities recorded at fair value. Prior to January 1, 2018, equity securities were stated at fair value with unrealized gains and losses reported as a separate component of Accumulated Other Comprehensive Income ("AOCI"), net of tax. At December 31, 2018, net unrealized gains of $3 thousand had been recognized in AOCI. On January 1, 2018, these unrealized gains, net of income tax were reclassified out of AOCI and into retained earnings with subsequent changes in fair value being recognized in net income. At December 31, 2020, the fair value of our equity portfolio was less than the cost basis by $15 thousand. The following is a summary of unrealized and realized gains and losses recognized in net income on equity securities during 2020 and 2019.

Year Ended December 31,	**2020**	**2019**
Net gain (loss) recognized during the period on equity securities	$ (6)	$ 132
Less: Net gain (loss) recognized during the period on equity securities sold during the period	29	
Unrealized gain (loss) recognized during the reporting period on equity securities still held at the reporting date	$ (35)	$ 132

The maturity distribution of the fair value, which is the net carrying amount, of the debt securities classified as available-for-sale at December 31, 2020, is summarized as follows:

December 31, 2020	**Fair Value**
Within one year	$ 37,351
After one but within five years	49,444
After five but within ten years	22,799
After ten years	84,357
	193,951
Mortgage-backed and other amortizing securities	101,960
Total	$ 295,911

Expected maturities will differ from contractual maturities because borrowers have the right to call or prepay obligations with or without call or prepayment penalties.

The maturity distribution of the amortized cost and fair value, of debt securities classified as held-to-maturity at December 31, 2020, is summarized as follows:

December 31, 2020	**Amortized Cost**	**Fair Value**
Within one year	$ 175	$ 178
After five but within ten years	324	344
After ten years	6,350	6,602
	6,849	7,124
Mortgage-backed securities	376	389
Total	$ 7,225	$ 7,513

Securities with a carrying value of $165,982 and $157,047 at December 31, 2020 and 2019, respectively, were pledged to secure public deposits and certain other deposits as required or permitted by law.

Securities and short-term investment activities are conducted with a diverse group of government entities, corporations and state and local municipalities. The counterparty's creditworthiness and type of collateral is evaluated on a case-by-case basis. At December 31, 2020 and 2019, there were no significant concentrations of credit risk from any one issuer, with the exception of U.S. government agencies and sponsored enterprises that exceeded 10.0 percent of stockholders' equity.

The fair value and gross unrealized losses of investment securities with unrealized losses for which an OTTI has not been recognized at December 31, 2020 and 2019, aggregated by investment category and length of time that the individual securities have been in a continuous unrealized loss position, are summarized as follows:

	Less Than 12 Months		12 Months or More		Total	
December 31, 2020	**Fair Value**	**Unrealized Losses**	**Fair Value**	**Unrealized Losses**	**Fair Value**	**Unrealized Losses**
State and municipals:						
Taxable	$ 9,246	$ 30	$	$	$ 9,246	$ 30
Tax-exempt	6,786	37			6,786	37
Residential mortgage-backed securities:						
U.S. government-sponsored enterprises	11,553	135	284	1	11,837	136
Total	$ 27,585	$ 202	$ 284	$ 1	$ 27,869	$ 203

	Less Than 12 Months		12 Months or More		Total	
December 31, 2019	**Fair Value**	**Unrealized Losses**	**Fair Value**	**Unrealized Losses**	**Fair Value**	**Unrealized Losses**
U.S. government-sponsored enterprises	$ 13,695	$ 149	$ 36,070	$ 78	$ 49,765	$ 227
State and municipals:						
Taxable	23,929	815			23,929	815
Tax-exempt	2,684	19	1,098	1	3,782	20
Residential mortgage-backed securities:						
U.S. government agencies	992	1	2,362	9	3,354	10
U.S. government-sponsored enterprises	36,939	51	3,751	30	40,690	81
Total	$ 78,239	$ 1,035	$ 43,281	$ 118	$ 121,520	$ 1,153

The Company had 26 investment securities, consisting of 12 tax-exempt and 8 taxable state and municipal obligations, and 6 mortgage-backed securities that were in unrealized loss positions at December 31, 2020. Of these securities, two mortgage-backed securities were in a continuous unrealized loss position for twelve months or more. Management does not consider the unrealized losses on the debt securities, as a result of changes in interest rates, to be OTTI based on historical evidence that indicates the cost of these securities is recoverable within a reasonable period of time in relation to normal cyclical changes in the market rates of interest. Moreover, because there has been no material change in the credit quality of the issuers or other events or circumstances that may cause a significant adverse impact on the fair value of these securities, and management does not intend to sell these securities and it is unlikely that the Company will be required to sell these securities before recovery of their amortized cost basis, which may be maturity, the Company does not consider the unrealized losses to be OTTI at December 31, 2020.

There was no OTTI recognized for each of the years in the three-year period ended December 31, 2020.

Other assets include the Company's investment in Visa Class B stock. The Company's ownership includes shares acquired at no cost related to the Company's prior ownership in Visa's network while Visa operated as a cooperative. The Company holds 44,982 shares of Visa Class B stock which, following resolution of Visa litigation, will be converted to Visa Class A shares (the conversion rate as of December 31, 2020 is 1.6228 shares of Class A stock for each share of Class B stock) for a total of 72,997 shares of Visa Class A stock.

There is a very limited market for this stock, as only current owners of Class B shares are permitted to transact in Class B. Due to the lack of orderly trades and public information of such trades, Visa Class B stock has no readily determinable fair value and is carried at cost.

4. Loans, net and allowance for loan losses:

The major classifications of loans outstanding, net of deferred loan origination fees and costs at December 31, 2020 and 2019 are summarized as follows. Included in the commercial balances at December 31, 2020 are $189,699 of Paycheck Protection Program ("PPP") loans. Net deferred loan fees of $2,058 were included in loan balances at December 31, 2020 and net deferred loan costs of $908 were included in the December 31, 2019 loan balances. The deferred loan fees in 2020 is a result of the origination of PPP loans.

	December 31, 2020	December 31, 2019
Commercial	$ 679,286	$ 522,957
Real estate:		
Commercial	1,137,990	1,011,423
Residential	277,414	301,378
Consumer	83,292	102,482
Total	$ 2,177,982	$ 1,938,240

Loans outstanding to directors, executive officers, principal stockholders or to their affiliates totaled $5,031 and $12,248 at December 31, 2020 and 2019, respectively. The decrease in loans outstanding is due to loan balances related to three former directors who retired in 2020. Advances and repayments during 2020 totaled $3,747 and $5,574, respectively, and during 2019 totaled $7,857 and $9,376, respectively. There were no related party loans that were classified as nonaccrual, past due, or restructured at December 31, 2020 and 2019.

Deposits from related parties amounted to $9.0 million at December 31, 2020 and $12.9 million at December 31, 2019.

At December 31, 2020, the majority of the Company's loans were at least partially secured by real estate in our market region. Therefore, a primary concentration of credit risk is directly related to the real estate market in these regions. Changes in the general economy, local economy or in the real estate market could affect the ultimate collectability of this portion of the loan portfolio. Management does not believe there are any other significant concentrations of credit risk that could affect the loan portfolio.

The changes in the allowance for loan losses account by major classification of loan for the year ended December 31, 2020, 2019, and 2018 were as follows:

		Real estate			
December 31, 2020	**Commercial**	**Commercial**	**Residential**	**Consumer**	**Total**
Allowance for loan losses:					
Beginning balance	$ 6,888	$ 11,496	$ 3,226	$ 1,067	$ 22,677
Charge-offs	(2,771)	(144)	(247)	(317)	(3,479)
Recoveries	525	16	57	148	746
Provisions	4,092	3,191	93	24	7,400
Ending balance	$ 8,734	$ 14,559	$ 3,129	$ 922	$ 27,344
Ending balance: individually evaluated for impairment	947	180	75		1,202
Ending balance: collectively evaluated for impairment	$ 7,787	$ 14,379	$ 3,054	$ 922	$ 26,142
Loans receivable:					
Ending balance	$ 679,286	$ 1,137,990	$ 277,414	$ 83,292	$ 2,177,982
Ending balance: individually evaluated for impairment	4,297	3,952	1,546	111	9,906
Ending balance: collectively evaluated for impairment	$ 674,989	$ 1,134,038	$ 275,868	$ 83,181	$ 2,168,076

The allowance for loan losses increased $4.6 million to $27.3 million at December 31, 2020, from $22.7 million at the end of 2019. The increase resulted from a provision for loan losses of $7.4 million less net loans charged-off of $2.7 million. Changes made during the first six months of 2020 to the qualitative factors, which related to economic decline resulting from the adverse impact of the COVID-19 crisis, was the primary reason for the higher provision. Commercial loan charge-offs were $2.8 million and included a $1.1 million partial write down of a specific credit relationship, which has been subsequently paid off in January 2021 and $0.9 million related to a group of small business lines of credit in our Greater Delaware Valley market. Commercial loan recoveries increased $0.5 million and included $0.2 million related to the group of small business lines of credit in the Greater Delaware Valley market and $0.2 million on a separate credit. We charged-off $3.3 million of commercial loans in 2019 substantially all of which were in the fourth quarter. Included in this amount was $2.3 million related to certain small business lines of credit in our Greater Delaware Valley market and $1.0 million of other commercial loan relationships.

In March 2020, we identified certain issues with a group of small business lines of credit, all of which had been originated by one of our lenders. All of these lines of credit were subject to credit review at origination and were considered satisfactory at such time. As a number of these lines of credit entered our annual renewal process, we identified changes in the credit quality of the borrowers which warranted action. We commenced a full review of this lender’s portfolio, as well as a review of other loans in our portfolio with similar characteristics. As a result of our review, we determined a number of the small business lines of credit originated by the particular lender to be impaired and collection doubtful at December 31, 2019. As such, we charged-off $2.3 million of these loans and established a specific reserve of $0.3 million on one other line of credit retrospectively to December 31, 2019. All remaining small business commercial lines of credit for this lender were downgraded to special mention. We believe that all of the other loans in our portfolio with similar characteristics that were subject to our review were properly reflected in our allowance methodology at December 31, 2020.

December 31, 2019	Commercial	Real estate Commercial	Real estate Residential	Consumer	Total
Allowance for loan losses:					
Beginning balance	$ 5,516	$ 10,736	$ 3,892	$ 1,235	$ 21,379
Charge-offs	(3,314)	(817)	(477)	(459)	(5,067)
Recoveries	69	1	29	166	265
Provisions	4,617	1,576	(218)	125	6,100
Ending balance	$ 6,888	$ 11,496	$ 3,226	$ 1,067	$ 22,677
Ending balance: individually evaluated for impairment	363	279	135		777
Ending balance: collectively evaluated for impairment	$ 6,525	$ 11,217	$ 3,091	$ 1,067	$ 21,900
Loans receivable:					
Ending balance	$ 522,957	$ 1,011,423	$ 301,378	$ 102,482	$ 1,938,240
Ending balance: individually evaluated for impairment	4,658	3,048	2,153	261	10,120
Ending balance: collectively evaluated for impairment	$ 518,299	$ 1,008,375	$ 299,225	$ 102,221	$ 1,928,120

December 31, 2018	Commercial	Real estate Commercial	Real estate Residential	Consumer	Total
Allowance for loan losses:					
Beginning balance	$ 5,513	$ 8,944	$ 3,111	$ 1,392	$ 18,960
Charge-offs	(154)	(1,250)	(405)	(545)	(2,354)
Recoveries	137	136	98	202	573
Provisions	20	2,906	1,088	186	4,200
Ending balance	$ 5,516	$ 10,736	$ 3,892	$ 1,235	$ 21,379
Ending balance: individually evaluated for impairment	50	403	666	60	1,179
Ending balance: collectively evaluated for impairment	$ 5,466	$ 10,333	$ 3,226	$ 1,175	$ 20,200
Loans receivable:					
Ending balance	$ 494,134	$ 907,803	$ 299,876	$ 121,453	$ 1,823,266
Ending balance: individually evaluated for impairment	2,237	3,121	4,071	212	9,641
Ending balance: collectively evaluated for impairment	$ 491,897	$ 904,682	$ 295,805	$ 121,241	$ 1,813,625

The following tables present the major classification of loans summarized by the aggregate pass rating and the classified ratings of special mention, substandard and doubtful within the Company's internal risk rating system at December 31, 2020 and 2019:

December 31, 2020	Pass	Special Mention	Substandard	Doubtful	Total
Commercial	$ 660,559	$ 14,305	$ 4,422	$	$ 679,286
Real estate:					
Commercial	1,107,699	17,517	12,774		1,137,990
Residential	274,327	144	2,943		277,414
Consumer	83,215		77		83,292
Total	$ 2,125,800	$ 31,966	$ 20,216	$	$ 2,177,982

December 31, 2019	Pass	Special Mention	Substandard	Doubtful	Total
Commercial	$ 513,994	$ 3,837	$ 5,126	$	$ 522,957
Real estate:					
Commercial	993,645	2,508	15,270		1,011,423
Residential	298,449	597	2,332		301,378
Consumer	102,145		337		102,482
Total	$ 1,908,233	$ 6,942	$ 23,065	$	$ 1,938,240

The increase in commercial special mention loans from December 31, 2019 to December 31, 2020 is primarily associated with a credit relationship to a public entity totaling $13.0 million which is experiencing short-term cash flow issues. The increase in commercial real estate special mention loans is due to the reclassification of four large credits. Two commercial real estate credits totaling $9.0 million were downgraded to special mention due to the loss of major tenants, while another credit totaling $4.5 million is related to the hospitality industry and is experiencing financial difficulties due to COVID-19. The decrease to commercial real estate substandard loans resulted in part from the payoff of a $5.1 million commercial real estate construction loan that had experienced significant construction delays.

Information concerning nonaccrual loans by major loan classification at December 31, 2020 and 2019 is summarized as follows:

	December 31, 2020	December 31, 2019
Commercial	$ 3,822	$ 3,336
Real estate:		
Commercial	3,262	2,765
Residential	922	1,148
Consumer	111	261
Total	$ 8,117	$ 7,510

The major classification of loans by past due status at December 31, 2020 and 2019 are summarized as follows:

December 31, 2020	30-59 Days Past Due	60-89 Days Past Due	Greater than 90 Days	Total Past Due	Current	Total Loans	Loans > 90 Days and Accruing
Commercial	$ 73		$ 3,822	$ 3,895	$ 675,391	$ 679,286	
Real estate:							
Commercial	344	$ 134	3,262	3,740	1,134,250	1,137,990	
Residential	2,072	480	993	3,545	273,869	277,414	$ 71
Consumer	374	63	111	548	82,744	83,292	
Total	$ 2,863	$ 677	$ 8,188	$ 11,728	$ 2,166,254	$ 2,177,982	$ 71

December 31, 2019	30-59 Days Past Due	60-89 Days Past Due	Greater than 90 Days	Total Past Due	Current	Total Loans	Loans > 90 Days and Accruing
Commercial	$ 75		$ 3,036	$ 3,111	$ 519,846	$ 522,957	
Real estate:							
Commercial	926	$ 175	2,765	3,866	1,007,557	1,011,423	
Residential	2,164	1,227	1,526	4,917	296,461	301,378	$ 378
Consumer	523	123	261	907	101,575	102,482	
Total	$ 3,688	$ 1,525	$ 7,588	$ 12,801	$ 1,925,439	$ 1,938,240	$ 378

The increase in the greater than 90 day category was due to a net increase in nonaccrual loans which are included in the category. Three large commercial loans added to non-accrual were partially offset by a partial charge-off of a non-accrual commercial relationship. The three loans added all have been individually measured for impairment. Two of the loans have specific reserves allocated, while the other credit was charged down to the SBA guaranteed amount.

The following tables summarize information concerning impaired loans as of and for the years ended December 31, 2020, 2019 and 2018 by major loan classification:

December 31, 2020	Recorded Investment	Unpaid Principal Balance	Related Allowance	For the Year Ended Average Recorded Investment	For the Year Ended Interest Income Recognized
With no related allowance:					
Commercial	$ 2,251	$ 3,421		$ 2,915	$ 30
Real estate:					
Commercial	2,372	2,964		2,148	28
Residential	1,086	1,263		1,223	21
Consumer	111	121		167	
Total	5,820	7,769		6,453	79
With an allowance recorded:					
Commercial	2,046	2,094	947	2,038	17
Real estate:					
Commercial	1,580	1,710	180	1,687	36
Residential	460	482	75	624	13
Consumer					
Total	4,086	4,286	1,202	4,349	66
Total impaired loans					
Commercial	4,297	5,515	947	4,953	47
Real estate:					
Commercial	3,952	4,674	180	3,835	64
Residential	1,546	1,745	75	1,847	34
Consumer	111	121		167	
Total	$ 9,906	$ 12,055	$ 1,202	$ 10,802	$ 145

December 31, 2019	Recorded Investment	Unpaid Principal Balance	Related Allowance	For the Year Ended Average Recorded Investment	For the Year Ended Interest Income Recognized
With no related allowance:					
Commercial	$ 3,638	$ 4,175		$ 3,907	$ 63
Real estate:					
Commercial	1,918	2,205		2,385	38
Residential	1,718	2,060		1,362	25
Consumer	261	274		233	
Total	7,535	8,714		7,887	126
With an allowance recorded:					
Commercial	1,020	1,038	363	1,012	32
Real estate:					
Commercial	1,130	1,811	279	1,050	10
Residential	435	450	135	1,408	29
Consumer				20	
Total	2,585	3,299	777	3,490	71
Total impaired loans					
Commercial	4,658	5,213	363	4,919	95
Real estate:					
Commercial	3,048	4,016	279	3,435	48
Residential	2,153	2,510	135	2,770	54
Consumer	261	274		253	
Total	$ 10,120	$ 12,013	$ 777	$ 11,377	$ 197

December 31, 2018	Recorded Investment	Unpaid Principal Balance	Related Allowance	For the Year Ended Average Recorded Investment	For the Year Ended Interest Income Recognized
With no related allowance:					
Commercial	$ 1,562	$ 1,900		$ 1,318	$ 67
Real estate:					
Commercial	1,969	2,299		2,822	28
Residential	1,970	2,658		2,193	22
Consumer	152	160		135	
Total	5,653	7,017		6,468	117
With an allowance recorded:					
Commercial	675	675	$ 50	1,006	30
Real estate:					
Commercial	1,152	1,323	403	1,676	18
Residential	2,101	2,328	666	1,585	22
Consumer	60	60	60	21	
Total	3,988	4,386	1,179	4,288	70
Total impaired loans					
Commercial	2,237	2,575	50	2,324	97
Real estate:					
Commercial	3,121	3,622	403	4,498	46
Residential	4,071	4,986	666	3,778	44
Consumer	212	220	60	156	
Total	$ 9,641	$ 11,403	$ 1,179	$ 10,756	$ 187

There were no amounts of interest income recognized using the cash-basis method on impaired loans for the years ended December 31, 2020, 2019 and 2018.

Included in the commercial loan, commercial real estate and residential real estate categories are troubled debt restructurings that were classified as impaired. Trouble debt restructurings totaled $2,818 and $2,193 at December 31, 2020 and 2019 respectively.

There were four loans modified in 2020, one loan modified in 2019 and one loan modified in 2018 that resulted in troubled debt restructurings. The four loans modified in 2020 were adversely impacted by COVID-19 and the economic slowdown and did not qualify for the CARES Act exclusion due to current and prior delinquencies. Two of the loans were to one restaurant and two of the loans were to retail related small businesses. The following tables summarize the loans whose terms have been modified resulting in troubled debt restructurings during the year ended December 31, 2020 and 2019 and 2018.

December 31, 2020	Number of Contracts	Pre-Modification Outstanding Recorded Investment	Post-Modification Outstanding Recorded Investment	Recorded Investment
Commercial	1	$ 12	$ 12	$ 5
Commercial real estate	3	1,073	1,073	1,046
Total	4	$ 1,085	$ 1,085	$ 1,051

December 31, 2019	Number of Contracts	Pre-Modification Outstanding Recorded Investment	Post-Modification Outstanding Recorded Investment	Recorded Investment
Commercial real estate	1	$ 346	$ 346	$ 241

December 31, 2018	Number of Contracts	Pre-Modification Outstanding Recorded Investment	Post-Modification Outstanding Recorded Investment	Recorded Investment
Commercial real estate	1	$ 340	$ 340	$ 340

There were no payment defaults within 12 months of its modification on loans considered troubled debt restructurings for the years ended December 31, 2020, December 31, 2019 and December 31, 2018.

The amount of residential loans in the formal process of foreclosure totaled $135 at December 31, 2020 and $665 at December 31, 2019.

The Company received a significant number of requests to modify loan terms and/or defer principal and/or interest payments from borrowers affected by COVID-19, and has agreed to many such deferrals. The federal banking regulators issued guidance and encouraged banks to work prudently with, and provide short-term payment accommodations to borrowers affected by COVID-19. Section 4013 of the CARES Act includes a provision for the Company to opt out of applying the troubled debt restructuring (“TDR”) guidance for certain loan modifications and specified that such modifications made on loans that were current as of December 31, 2019 do not need to be classified as TDRs. Peoples has applied this guidance. The payment modifications granted included principal only payments and principal and interest deferrals and generally ranged from 90 to 180 days. The modified loans were not considered past due unless the modified payment was delinquent. Similarly, FASB has confirmed that short-term modifications made on a good-faith basis in response to COVID-19 to loan customers who were current prior to any relief are not TDRs.

Beginning in March 2020, the Company began receiving requests for temporary modifications to the repayment structure for borrower loans. During 2020, the Company made a total of 479 commercial loan and 512 consumer loan temporary modifications with principal balances totaling $330,119. At December 31, 2020, 18 commercial loans and 26 consumer loans remain on deferral with principal balances of $6,084.

The following tables provide information as of December 31, 2020 and the total during 2020 with respect to the Company's payment deferrals granted in accordance with the CARES Act on commercial loans by North American Industry Classification System ("NAICS") categories:

December 31, 2020 NAICS category	Number of Loans	Balance	Percentage of Total Loan Portfolio	Percentage of Tier 1 Capital (Bank)
Lessors of Residential Buildings and Dwellings	3	$ 143		0.1 %
Full-Service Restaurants	3	1,961	0.1 %	0.8
General Automotive Repair	1	1,459	0.1	0.6
School and Employee Bus Transportation	1	725		0.3
All Others	10	1,508	0.1	0.6
	18	$ 5,796	0.3 %	2.3 %

2020 NAICS category	Number of Loans	Balance	Percentage of Total Loan Portfolio	Percentage of Tier 1 Capital (Bank)
Lessors of Nonresidential Buildings	65	$ 71,899	3.3 %	26.9 %
Lessors of Residential Buildings and Dwellings	64	53,564	2.5	19.9
Hotels and Motels	27	39,261	1.8	14.5
Full-Service Restaurants	33	27,783	1.3	10.3
Limited-Service Restaurants	8	11,829	0.5	4.4
Gasoline Stations with Convenience Stores	18	12,422	0.6	4.6
Construction and Mining	13	9,718	0.4	3.6
Assisted Living Facilities for the Elderly	2	6,319	0.3	2.3
Colleges, Universities, and Professional Schools	1	6,301	0.3	2.3
All Others	248	67,674	3.1	24.9
	479	$ 306,770	14.1 %	113.7 %

5. Off-balance sheet financial instruments:

The Company is a party to financial instruments with off-balance sheet risk in the normal course of business to meet the financing needs of its customers. These financial instruments include commitments to extend credit, unused portions of lines of credit and standby letters of credit. Those instruments involve, to varying degrees, elements of credit risk in excess of the amount recognized in the consolidated balance sheets.

The Company's exposure to credit loss in the event of nonperformance by the other party to the financial instrument for commitments to extend credit, unused portions of lines of credit and standby letters of credit is represented by the contractual amounts of those instruments. The Company follows the same credit policies in making commitments and conditional obligations as it does for on-balance sheet instruments. The Company records a valuation allowance for off-balance sheet credit losses, if deemed necessary, separately as a liability. The allowance is not significant.

The contractual amounts of off-balance sheet commitments at December 31, 2020 and 2019 are summarized as follows:

December 31	2020	2019
Commitments to extend credit	$ 336,667	$ 290,517
Unused portions of lines of credit	55,391	52,168
Standby letters of credit	34,428	45,018
	$ 426,486	$ 387,703

Commitments to extend credit are agreements to lend to a customer as long as there is no violation of any condition established in the contract. Since many of the commitments are expected to expire without being drawn upon, the total commitment amounts do not necessarily represent future cash requirements. Commitments generally have fixed expiration dates or other termination clauses and may require payment of a fee. The Company evaluates each customer's credit worthiness on a case-by-case basis. The amount of collateral obtained, if deemed necessary by the Company upon extension of credit, is based on management's credit evaluation. Collateral held varies but may include personal or commercial real estate, accounts receivable, inventory and equipment.

Unused portions of lines of credit, including home equity and overdraft protection agreements, are commitments for possible future extensions of credit to existing customers. Unused portions of home equity lines are collateralized and generally have fixed expiration dates. Overdraft protection agreements are uncollateralized and usually do not carry specific maturity dates. Unused portions of lines of credit ultimately may not be drawn upon to the total extent to which the Company is committed.

Standby letters of credit are conditional commitments issued by the Company to guarantee the performance of a customer to a third party. Generally, all standby letters of credit expire within twelve months. The credit risk involved in issuing standby letters of credit is essentially the same as that involved in extending other loan commitments. The Company requires collateral supporting these standby letters of credit as deemed necessary. Collateral supporting standby letters of credit amounted to $4,902 at December 31, 2020 and $31,893 at December 31, 2019. The carrying value of the liability for the Company's obligations under guarantees for standby letters of credit was not material at December 31, 2020 and 2019.

6. Premises and equipment, net:

Premises and equipment at December 31, 2020 and 2019 are summarized as follows:

December 31	2020	2019
Land	$ 5,217	$ 5,535
Premises and leasehold improvements	48,596	47,705
Right-of-use assets	6,282	6,125
Furniture, fixtures and equipment	18,395	17,422
	78,490	76,787
Less: accumulated depreciation	31,445	28,855
	$ 47,045	$ 47,932

7. Operating lease commitments and contingencies:

The Company is obligated under non-cancelable operating leases for certain branch locations. We determine if an arrangement is a lease at inception by assessing whether a contract contains a right to control an identified asset for a period of time in exchange for consideration. For all leases, we recognize a right-of-use asset and lease liability at the effective date of the lease. Operating leases right-of-use assets are included in premises and equipment, and lease liabilities are included in other liabilities in the consolidated balance sheet commencing at January 1, 2019. We have no finance leases. Leases with an initial term of 12 months or less are not recorded on the balance sheet and the related lease expense is recognized on a straight-line basis over the lease term.

Certain leases include options to renew, with renewal terms generally containing one or more five-year renewal options. At December 31, 2020, the Company's leases have remaining renewal terms that can extend the lease term from three years to twenty-one years that are reasonably certain of being exercised. The weighted average remaining lease term at December 31, 2020 is thirteen years. At December 31, 2019, the weighted average remaining lease term was sixteen years. The discount rate used in determining the lease liability for each individual lease was the FHLB fixed advance rate which corresponded with the remaining lease term as of January 1, 2019 for leases that existed at adoption and as of the lease commencement date for leases subsequently entered into after January 1, 2019. At December 31, 2020, discount rates ranged from 1.95% to 3.85% with an-average discount rate of 3.19%. At December 31, 2019, discount rates ranged from 2.89% to 3.85% with an average discount rate of 3.46%.

At December 31, 2020, right-of-use assets of $6,282 were included in premises and equipment, and the related lease liability totaled $6,425 and was included in other liabilities in the consolidated balance sheet. Right-of-use assets and the related lease liability were $6,125 and $6,194, respectively, at December 31, 2019. The lease liability decreased due to payments of $660 offset by $326 of lease expense and the termination of two leases. One additional lease was entered into and added $899 to the liability. Rent expense for the years ended December 31, 2020, 2019 and 2018 amounted to $727, $670, and $492, respectively, and is included in occupancy expenses.

Future minimum lease payments under operating leases are summarized as follows:

2021	$ 611
2022	618
2023	560
2024	488
2025	504
Thereafter	5,500
Total future minimum lease payments	8,281
Less amount representing interest	(1,856)
Present value of future minimum lease payments	$ 6,425

8. Intangible assets, net:

The gross carrying amount of core deposit intangible assets totaled $8,146 at December 31, 2020 and 2019. The gross carrying amount of trade name intangible assets totaled $203 at December 31, 2020 and 2019. The gross carrying amount of the intangible asset related to the acquisition of an asset management and retirement plan services company acquired in 2015 totaled $1,091 at December 31, 2020 and 2019. The accumulated amortization on core deposit intangible assets was $7,507 and $7,071 at December 31, 2020 and 2019, respectively. The accumulated amortization trade name intangible assets was $182 and $168 at December 31, 2020 and 2019, respectively. The accumulated amortization on the asset management and retirement plan services intangible asset was $792 and $636 at December 31, 2020 and 2019, respectively.

The estimated amortization expense on intangible assets in years subsequent to December 31, 2020, is as follows:

2021	$ 491
2022	363
2023	106
Total	$ 960

9. Other assets:

The major components of other assets at December 31, 2020 and 2019 are summarized as follows:

	December 31, 2020	December 31, 2019
Other real estate owned	$ 864	$ 450
Investment in low income housing partnership	6,332	6,901
Mortgage servicing rights	838	738
Restricted equity securities (FHLB and other)	5,397	10,201
Net deferred tax asset	3,768	3,362
Interest rate floor	1,678	944
Interest rate swaps	13,693	4,728
Other assets	6,345	6,855
Total	$ 38,915	$ 34,179

The Company originates one-to-four family residential mortgage loans for sale in the secondary market with servicing rights retained. Mortgage loans serviced for others are not included in the accompanying Consolidated Balance Sheets. The unpaid principal balances of mortgage loans serviced for others were $166,472 at December 31, 2020 and $159,587 at December 31, 2019.

10. Deposits:

The major components of interest-bearing and noninterest-bearing deposits at December 31, 2020 and 2019 are summarized as follows:

At the period end	December 31, 2020	December 31, 2019
Interest-bearing deposits:		
Money market accounts	$ 496,634	$ 365,463
Now accounts	567,087	402,999
Savings accounts	431,224	370,270
Time deposits less than $250	221,446	231,450
Time deposits $250 or more	98,247	138,069
Total interest-bearing deposits	1,814,638	1,508,251
Noninterest-bearing deposits	622,475	463,238
Total deposits	$ 2,437,113	$ 1,971,489

The growth in deposits occurred in non-maturity deposits as demand for liquid accounts elevated due to low interest rates and economic uncertainty. Strong organic growth of core deposits from new and existing relationships, inflows of public fund deposits, and proceeds of PPP loans retained on deposit by our commercial borrowers, primarily in the second quarter, contributed to the increase. Time deposits $250 thousand or more decreased due to the maturity of a few large public fund certificates of deposit.

The aggregate amounts of maturities for all time deposits at December 31, 2020, are summarized as follows:

2021	$ 223,247
2022	40,093
2023	22,905
2024	15,099
2025	7,316
Thereafter	11,033
	$ 319,693

The aggregate amount of deposits reclassified as loans was $245 at December 31, 2020, and $343 at December 31, 2019. Management evaluates transaction accounts that are overdrawn for collectability as part of its evaluation for credit losses.

11. Short-term borrowings:

Short-term borrowings consisted of FHLB advances representing overnight borrowings or borrowings with original terms of less than twelve months at December 31, 2020, 2019 and 2018:

	At and for the year ended December 31, 2020				
	Ending Balance	Average Balance	Maximum Month-End Balance	Weighted Average Rate	Weighted Average Rate at December 31,2020
FHLB advances	$ 50,000	$ 83,716	$ 179,199	1.01 %	0.40 %

	At and for the year ended December 31, 2019				
	Ending Balance	Average Balance	Maximum Month-End Balance	Weighted Average Rate for the Year	Weighted Average Rate at End of the Year
FHLB advances	$ 152,150	$ 62,941	$ 152,150	2.61 %	1.84 %

	At and for the year ended December 31, 2018				
	Ending Balance	Average Balance	Maximum Month-End Balance	Weighted Average Rate for the Year	Weighted Average Rate at End of the Year
FHLB advances	$ 86,500	$ 133,834	$ 189,275	2.05 %	2.62 %

The Company has an agreement with the FHLB which allows for borrowings up to its maximum borrowing capacity based on a percentage of qualifying collateral assets. At December 31, 2020, the maximum borrowing capacity was $807,042 of which $64,769 was outstanding in borrowings and $218,350 was used to issue standby letters of credit to collateralize public fund deposits. Advances with the FHLB are secured under terms of a blanket collateral agreement by a pledge of FHLB stock and certain other qualifying collateral, such as investments and mortgage-backed securities and mortgage loans. Interest accrues daily on the FHLB advances based on rates of the FHLB discount notes. This rate resets each day.

The Company also has unsecured line of credit agreements with two correspondent banks, where the total line amount was $18,000 at December 31, 2020 and 2019. There were no amounts outstanding on either line of credit at December 31, 2020 or 2019. Interest on these borrowings accrues daily based on the daily federal funds rate.

12. Long-term debt:

Long-term debt consisting of advances from the FHLB at December 31, 2020 and 2019 are as follows:

Due	Interest Rate Fixed	December 31, 2020	December 31, 2019
June 2020	1.74 %		$ 5,000
June 2020	2.22		6,000
December 2020	1.84	$	5,000
June 2021	1.99	10,000	10,000
March 2023	4.69	4,769	6,733
		$ 14,769	$ 32,733

Maturities of long-term debt, by contractual maturity, in years subsequent to December 31, 2020 are as follows:

2021	$ 12,058
2022	2,156
2023	555
	$ 14,769

None of the advances from the FHLB are convertible. At December 31, 2020, long-term debt are all at fixed rates. There were no new long-term advances entered into with the FHLB during 2020. Two new long term advances were entered into with the FHLB during 2019 totaling $16,000 with terms of one and two years.

During 2020, the company participated in the Federal Reserve Banks PPPLF by pledging PPP loans as collateral. Borrowings from this facility are categorized as long-term based on the twenty four or sixty month term of the loans pledged. At December 31, 2020, no advances were outstanding under this facility.

13. Subordinated debt:

On June 1, 2020, the Company sold $33,000 aggregate principal amount of Subordinated Notes due 2030 (the "2020 Notes") to accredited investors. The 2020 Notes qualify as Tier 2 capital for regulatory capital purposes.

The 2020 Notes bear interest at a rate of 5.375% per year for the first five years and then float based on a benchmark rate (as defined), provided that the interest rate applicable to the outstanding principal balance during the period the 2020 Notes are floating will at no time be less the 4.75%. Interest will be payable semi-annually in arrears on June 1 and December 1 of each year, beginning on June 1, 2020, for the first five years after issuance and will be payable quarterly in arrears thereafter on March 1, June 1, September 1, and December 1. The 2020 Notes will mature on June 1, 2030 and are redeemable in whole or in part, without premium or penalty, at any time on or after June 1, 2025 and prior to June 1, 2030. Additionally, if all or any portion of the 2020 Notes cease to be deemed Tier 2 Capital, the Company may redeem, in whole and not in part, at any time upon giving not less than ten days' notice, an amount equal to one hundred percent (100%) of the principal amount outstanding plus accrued but unpaid interest to but excluding the date fixed for redemption.

Holders of the 2020 Notes may not accelerate the maturity of the 2020 Notes, except upon the bankruptcy, insolvency, liquidation, receivership or similar proceeding by or against the Company.

14. Fair value of financial instruments:

Assets and liabilities measured at fair value on a recurring basis at December 31, 2020 and 2019 are summarized as follows:

		Fair Value Measurement Using		
December 31, 2020	**Amount**	**Quoted Prices in Active Markets for Identical Assets (Level 1)**	**Significant Other Observable Inputs (Level 2)**	**Significant Unobservable Inputs (Level 3)**
U.S. Treasury securities	$ 18,905	$ 18,905		$
U.S. government-sponsored enterprises	65,188		$ 65,188	
State and municipals:				
Taxable	55,366		55,366	
Tax-exempt	56,994		56,994	
Mortgage-backed securities:				
U.S. government agencies	3,707		3,707	
U.S. government-sponsored enterprises	94,751		94,751	
Corporate debt securities	1,000		1,000	
Common equity securities	138	138		
Loan held for sale	837		837	
Interest rate floor-other assets	1,678		1,678	
Interest rate swap-other assets	13,693		13,693	
Interest rate swap-other liabilities	(14,099)		(14,099)	
Total	$ 298,158	$ 19,043	$ 279,115	$

		Fair Value Measurement Using		
December 31, 2019	**Amount**	**Quoted Prices in Active Markets for Identical Assets (Level 1)**	**Significant Other Observable Inputs (Level 2)**	**Significant Unobservable Inputs (Level 3)**
U.S. Treasury securities	$ 24,128	$ 24,128		$
U.S. government-sponsored enterprises	87,110		$ 87,110	
State and municipals:				
Taxable	34,898		34,898	
Tax-exempt	60,163		60,163	
Mortgage-backed securities:				
U.S. government agencies	8,470		8,470	
U.S. government-sponsored enterprises	115,709		115,709	
Common equity securities	423	423		
Loan held for sale	986		986	
Interest rate floor-other assets	944		944	
Interest rate swap-other assets	4,728		4,728	
Interest rate swap-other liabilities	(4,680)		(4,680)	
Total	$ 332,879	$ 24,551	$ 308,328	$

Assets and liabilities measured at fair value on a nonrecurring basis at December 31, 2020 and 2019 are summarized as follows:

December 31, 2020	Amount	Fair Value Measurement Using Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
Impaired loans	$ 2,884			$ 2,884
Other real estate owned	$ 527			$ 527

December 31, 2019	Amount	Fair Value Measurement Using Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
Impaired loans	$ 1,808			$ 1,808
Other real estate owned	$ 283			$ 283

The following table presents additional quantitative information about assets measured at fair value on a nonrecurring basis and for which the Company has utilized Level 3 inputs to determine fair value:

	Quantitative Information about Level 3 Fair Value Measurements			
December 31, 2020	Fair Value Estimate	Valuation Techniques	Unobservable Input	Range (Weighted Average)
Impaired loans	$ 2,884	Appraisal of collateral	Appraisal adjustments	9.0% to 97.0% (28.2)%
			Liquidation expenses	3.0% to 6.0% (5.5)%
Other real estate owned	$ 527	Appraisal of collateral	Appraisal adjustments	3.1% to 58.1% (29.9)%
			Liquidation expenses	3.0% to 6.0% (5.0)%

	Quantitative Information about Level 3 Fair Value Measurements			
December 31, 2019	Fair Value Estimate	Valuation Techniques	Unobservable Input	Range (Weighted Average)
Impaired loans	$ 1,808	Appraisal of collateral	Appraisal adjustments	8.6% to 97.0% (54.4)%
			Liquidation expenses	3.0% to 6.0% (5.2)%
Other real estate owned	$ 283	Appraisal of collateral	Appraisal adjustments	20.0% to 63.6% (43.7)%
			Liquidation expenses	3.0% to 6.0% (5.0)%

Fair value is generally determined through independent appraisals of the underlying collateral, which generally include various Level 3 inputs which are not identifiable.

Appraisals may be adjusted by management for qualitative factors such as economic conditions and estimated liquidation expenses. The range and weighted average of liquidation expenses and other appraisal adjustments are presented as a percent of the appraisal.

The carrying and fair values of the Company's financial instruments at December 31, 2020 and 2019 and their placement within the fair value hierarchy are as follows:

			Fair Value Hierarchy		
December 31, 2020	**Carrying Value**	**Fair Value**	**Quoted Prices in Active Markets for Identical Assets (level 1)**	**Significant Other Observable Inputs (level 2)**	**Significant Unobservable Inputs (Level 3)**
Financial assets:					
Cash and due from banks	$ 228,192	$ 228,192	$ 228,192		
Investment securities:					
Available-for-sale	295,911	295,911	18,905	$ 277,006	
Common equity securities	138	138	138		
Held-to-maturity	7,225	7,513		7,513	
Loans held for sale	837	837		837	
Net loans	2,150,638	2,145,752			$ 2,145,752
Accrued interest receivable	8,255	8,255		8,255	
Mortgage servicing rights	838	1,269		1,269	
Restricted equity securities (FHLB and other)	5,397	5,397		5,397	
Interest rate floor	1,678	1,678		1,678	
Interest rate swaps	13,693	13,693		13,693	
Total	$ 2,712,802	$ 2,708,635			
Financial liabilities:					
Deposits	$ 2,437,113	$ 2,441,014		$ 2,441,014	
Long-term debt	14,769	15,073		15,073	
Subordinated debentures	33,000	33,096		33,096	
Accrued interest payable	736	736		736	
Interest rate swaps	14,099	14,099		14,099	
Total	$ 2,499,717	$ 2,504,018			

December 31, 2019	Carrying Value	Fair Value	Fair Value Hierarchy: Quoted Prices in Active Markets for Identical Assets (level 1)	Significant Other Observable Inputs (level 2)	Significant Unobservable Inputs (Level 3)
Financial assets:					
Cash and due from banks	$ 31,153	$ 31,153	$ 31,153		
Investment securities:					
Available-for-sale	330,478	330,478	24,128	$ 306,350	
Common equity securities	423	423	423		
Held-to-maturity	7,656	7,889		7,889	
Loans held for sale	986	986		986	
Net loans	1,915,563	1,881,658			$ 1,881,658
Accrued interest receivable	6,981	6,981		6,981	
Mortgage servicing rights	738	1,444		1,444	
Restricted equity securities (FHLB and other)	10,201	10,201		10,201	
Interest rate floor	944	944		944	
Interest rate swaps	4,728	4,728		4,728	
Total	$ 2,309,851	$ 2,276,885			
Financial liabilities:					
Deposits	$ 1,971,489	$ 1,972,084		$ 1,972,084	
Long-term debt	32,733	33,075		33,075	
Accrued interest payable	1,277	1,277		1,277	
Interest rate swaps	4,680	4,680		4,680	
Total	$ 2,010,179	$ 2,011,116			

15. Derivatives and hedging activities:

Risk Management Objective of Using Derivatives

The Company is exposed to certain risk arising from both its business operations and economic conditions. The Company principally manages its exposures to a wide variety of business and operational risks through management of its core business activities. The Company manages economic risks, including interest rate, liquidity, and credit risk primarily by managing the amount, sources, and duration of its assets and liabilities and the use of derivative financial instruments. Specifically, the Company enters into derivative financial instruments to manage exposures that arise from business activities that result in the receipt or payment of future known and uncertain cash amounts, the value of which are determined by interest rates. The Company's derivative financial instruments are used to manage differences in the amount, timing, and duration of the Company's known or expected cash receipts principally related to the Company's assets and borrowings.

Cash Flow Hedges of Interest Rate Risk

The Company's objectives in using interest rate derivatives are to add stability to interest income/expense and to manage its exposure to interest rate movements. To accomplish this objective, the Company primarily uses interest rate swaps and floors as part of its interest rate risk management strategy. Interest rate swaps designated as cash flow hedges involve the receipt of variable amounts from a counterparty in exchange for the Company making fixed-rate payments over the life of the agreements without exchange of the underlying notional amount. Interest rate floors designated as cash flow hedges involve the receipt of variable-rate amounts from a counterparty if interest rates fall below the strike rate on the contract in exchange for an up-front premium. During 2020, such derivatives were used to hedge the variable cash flows associated with existing variable-rate assets and issuances of debt.

The Company executed an interest rate swap to reduce its exposure to variability in the interest rate associated with floating-rate borrowings. For derivatives designated and that qualify as cash flow hedges of interest rate risk, the gain or loss on the derivative is recorded in Accumulated Other Comprehensive Income and subsequently reclassified into interest expense/income in the same period(s) during which the hedged transaction affects earnings. Amounts reported in accumulated other comprehensive income related to derivatives will be reclassified to interest expense/income as interest payments are made/received on the Company's variable-rate debt/assets. During 2021 the Company estimates that an additional $50 will be reclassified as a decrease to interest income.

Non-designated Hedges

Derivatives not designated as hedges are not speculative and result from a service the Company provides to certain customers. The Company executes interest rate swaps with commercial banking customers to facilitate their respective risk management strategies. Those interest rate swaps are simultaneously hedged by offsetting interest rate swaps that the Company executes with a third party, such that the Company minimizes its net risk exposure resulting from such transactions. As the interest rate swaps associated with this program do not meet the strict hedge accounting requirements, changes in the fair value of both the customer swaps and the offsetting swaps are recognized directly in earnings. As of December 31, 2020, the Company had 73 interest rate swaps with an aggregate notional amount of $375,341 related to this program.

Fair Values of Derivative Instruments on the Balance Sheet

The table below presents the fair value of the Company's derivative financial instruments as well as their classification on the Consolidated Balance Sheets as of December 31, 2020 and December 31, 2019.

		Asset Derivatives As of December 31, 2020		Asset Derivatives As of December 31, 2019 (1)		Liability Derivatives As of December 31, 2020		Liability Derivatives As of December 31, 2019 (2)	
	Notional Amount	Balance Sheet Location	Fair Value	Balance Sheet Location	Fair Value	Balance Sheet Location	Fair Value	Balance Sheet Location	Fair Value
Derivatives designated as hedging instruments									
Interest Rate Floor	$ 25,000	Other Assets	$ 1,678	Other Assets	$ 944				
Cash Flow Swap	$ 50,000					Other Liabilities	$ 485		
Total derivatives designated as hedging instruments			$ 1,678		$ 944		$ 485		
Derivatives **not** designated as hedging instruments									
Interest Rate Swaps (3)	$ 375,341	Other Assets	$ 13,693	Other Assets	$ 4,728	Other Liabilities	$ 13,614	Other Liabilities	$ 4,680
Total derivatives **not** designated as hedging instruments			$ 13,693		$ 4,728		$ 13,614		$ 4,680

(1) Assets amount does not include accrued interest receivable of $235
(2) Liabilities amount does not include accrued interest payable of $235
(3) Notional amount of interest rate swaps at December 31, 2019 $172,096

Effect of Fair Value and Cash Flow Hedge Accounting on Accumulated Other Comprehensive Income (Loss)

The table below presents the effect of fair value and cash flow hedge accounting on accumulated other comprehensive income (loss) as of December 31, 2020 and December 31, 2019.

Derivatives in Hedging Relationships	Amount of Gain (Loss) Recognized in OCI on Derivative	Amount of Gain (Loss) Recognized in OCI Included Component December 31, 2020	Amount of Loss Recognized in OCI Excluded Component	Location of Gain or (Loss) Recognized from Accumulated Other Comprehensive Income into Income	Amount of Gain (Loss) Reclassified from Accumulated OCI into Income	Amount of Gain (Loss) Reclassified from Accumulated OCI into Income Included Component December 31, 2020	Amount of Gain (Loss) Reclassified from Accumulated OCI into Income Excluded Component
Derivatives in Cash Flow Hedging Relationships							
Cash Flow Swap	$ 71	$ 71		Interest Expense	$ (40)	$ (40)	
Interest Rate Floor (*)	$ (18)	$ (17)	$ (1)	Interest Income	$ 134	$ 150	$ (16)
Total	$ 53	$ 54	$ (1)		$ 94	$ 110	$ (16)

Derivatives in Hedging Relationships	Amount of Gain Recognized in OCI on Derivative	Amount of Gain Recognized in OCI Included Component December 31, 2019	Amount of Gain Recognized in OCI Excluded Component	Location of Gain or (Loss) Recognized from Accumulated Other Comprehensive Income into Income	Amount of Loss Reclassified from Accumulated OCI into Income	Amount of Gain Reclassified from Accumulated OCI into Income Included Component December 31, 2019	Amount of Loss Reclassified from Accumulated OCI into Income Excluded Component
Derivatives in Cash Flow Hedging Relationships							
Interest Rate Floor (*)	$ 192	$ 196	$ (4)	Interest Income	$ 26	$ 42	$ (16)

* Amounts disclosed are gross and not net of taxes.

Effect of Fair Value and Cash Flow Hedge Accounting on the Consolidated Statements of Income and Comprehensive Income

The table below presents the effect of the Company's derivative financial instruments on the consolidated statements of income and comprehensive income as of December 31, 2020 and December 31, 2019.

	Location and Amount of Gain or (Loss) Recognized in Income on Fair Value and Cash Flow Hedging Relationships			
	2020 Interest Income	2020 Interest Expense	2019 Interest Income	2019 Interest Expense
Total amounts of income and expense line items presented in the statements of income and comprehensive income in which the effects of fair value or cash flow hedges are recorded	$ 134	$ (40)	$ 26	
The effects of fair value and cash flow hedging:				
Gain or (loss) on cash flow hedging relationships				
Interest contracts				
Amount of gain or (loss) reclassified from accumulated other comprehensive income into income	$ 134	$ (40)	$ 26	
Amount of gain or (loss) reclassified from accumulated other comprehensive income into income - included component	$ 150		$ 42	
Amount of gain or (loss) reclassified from accumulated other comprehensive income into income - excluded component	$ (16)		$ (16)	

Effect of Derivative Instruments on the Consolidated Statements of Income and Comprehensive Income

The tables below present the effect of the Company's other derivative financial instruments on the consolidated statements of income and comprehensive income for the years ended December 31, 2020 and 2019.

Derivatives Not Designated as Hedging Instruments	Location of Gain or (Loss) Recognized in Income on Derivative	Amount of Gain Recognized in Income Twelve Months Ended December 31, 2020	Amount of Loss Recognized in Income Twelve Months Ended December 31, 2019
Interest Rate Swaps	Interest rate swap revenue	$ 31	$ 77
Fee Income	Interest rate swap revenue	$ 2,290	$ 1,713

Offsetting Derivatives

The table below presents a gross presentation, the effects of offsetting, and a net presentation of the Company's derivatives as of December 31, 2020 and December 31, 2019. The net amounts of derivative assets or liabilities can be reconciled to the tabular disclosure of fair value. The tabular disclosure of fair value provides the location that derivative assets and liabilities are presented on the consolidated balance sheets.

Offsetting of Derivative Assets
as of December 31, 2020

	Gross Amounts of Recognized Assets	Gross Amounts Offset in the Balance Sheet	Net Amounts of Assets presented in the Balance Sheet	Gross Amounts Not Offset in the Balance Sheet		Net Amount
				Financial Instruments	Cash Collateral Received	
Derivatives	$ 15,371	$	$ 15,371	$		$ 15,371

Offsetting of Derivative Liabilities
as of December 31, 2020

	Gross Amounts of Recognized Assets	Gross Amounts Offset in the Balance Sheet	Net Amounts of Assets presented in the Balance Sheet	Gross Amounts Not Offset in the Balance Sheet		Net Amount
				Financial Instruments	Cash Collateral Received	
Derivatives	$ 14,099	$	$ 14,099	$		$ 14,099

Offsetting of Derivative Assets
as of December 31, 2019

	Gross Amounts of Recognized Assets	Gross Amounts Offset in the Balance Sheet	Net Amounts of Assets presented in the Balance Sheet	Gross Amounts Not Offset in the Balance Sheet		Net Amount
				Financial Instruments	Cash Collateral Received	
Derivatives	$ 5,672	$	$ 5,672	$		$ 5,672

Offsetting of Derivative Liabilities
as of December 31, 2019

	Gross Amounts of Recognized Assets	Gross Amounts Offset in the Balance Sheet	Net Amounts of Assets presented in the Balance Sheet	Gross Amounts Not Offset in the Balance Sheet		Net Amount
				Financial Instruments	Cash Collateral Received	
Derivatives	$ 4,680	$	$ 4,680	$		$ 4,680

Credit-risk-related Contingent Features

The Company has agreements with certain of its derivative counterparties that contain a provision where if the Company defaults on any of its indebtedness, including default where repayment of the indebtedness has not been accelerated by the lender, then the Company could also be declared in default on its derivative obligations.

The Company also has agreements with certain of its derivative counterparties that contain a provision where if the Company fails to maintain its status as a well capitalized institution, then the counterparty could terminate the derivative positions and the Company would be required to settle its obligations under the agreements.

As of December 31, 2020, the termination value of derivatives in a net asset position, which includes accrued interest but excludes any adjustment for nonperformance risk, related to these agreements was $79. As of December 31, 2019, the termination value of derivatives in a net asset position, which includes accrued interest but excludes any adjustment for nonperformance risk, related to these agreements was $48. The Company has minimum collateral posting thresholds with certain of its derivative counterparties, and has posted collateral of $15,360 against its obligations under these agreements as of December 30, 2020, compared to having posted collateral of $4,140 with counterparties at December 31, 2019. If the Company had breached any of these provisions it could have been required to settle its obligations under the agreements at the termination value.

16. Stock plans:

The 2008 long-term incentive plan ("2008 Plan") allowed for eligible participants to be granted equity awards. No awards may be made under the 2008 Plan after January 15, 2018.

In May 2017, the Company's stockholders approved the 2017 equity incentive plan ("2017 Plan"). The 2017 Plan allows for eligible participants to be granted equity awards. Under the 2017 Plan the Compensation Committee of the Board of Directors has the authority to, among other things:

- Select the persons to be granted awards under the 2017 Plan.
- Determine the type, size and term of awards.
- Determine whether such performance objectives and conditions have been met.
- Accelerate the vesting or excercisability of an award.

Persons eligible to receive awards under the 2008 Plan and 2017 Plan include directors, officers, employees, consultants and other service providers of the Company and its subsidiaries.

As of December 31, 2020, 56,966 shares of the Company's common stock were available for grant as awards pursuant to the 2017 Plan. The 2008 Plan expired in January 2018 but remained in effect in accordance with its terms to govern outstanding awards under that plan. As of December 31, 2020, no awards are outstanding under the 2008 Plan. If any outstanding awards under the 2017 Plan are forfeited by the holder or canceled by the Company, the underlying shares would be available for regrant to others.

The 2017 Plan authorizes grants of stock options, stock appreciation rights, cash awards, performance awards, restricted stock and restricted stock units. In 2020, the Company awarded 3,615 shares of non-performance-based restricted stock and 12,654 performance-based restricted stock units under the 2017 Plan. In 2019, the Company awarded 3,855 shares of non-performance-based restricted stock and 13,490 performance-based restricted stock units under the 2017 Plan. In 2020, 1,920 shares of non-performance-based and 6,535 shares of performance based restricted stock granted under the 2017 Plan vested along with 673 shares of non-performance-based restricted stock granted under the 2008 Plan and there were 1,875 shares forfeited under the provisions of the 2017 Plan. In 2019, 1,614 shares of non-performance-based restricted stock and 928 shares of performance-based shares granted under the 2017 Plan vested along with 674 shares of non-performance-based restricted stock and 5,743 of performance-based shares granted under the 2008 Plan. There were 1,711 shares forfeited under the provisions of the 2017 Plan and 1,327 shares forfeited under the provisions of the 2008 plan.

The non-performance restricted stock grants made in 2020, 2019, 2018 and 2017 vest equally over three years from the grant date. The performance-based restricted stock units vest three years after the grant date and include conditions based on the Company's three year cumulative diluted earnings per share and three-year average return on equity or tangible equity that determines the number of restricted stock units that may vest.

The activity related to the 2017 Plan for each of the years ended December 31, 2020, 2019 and 2018 was as follows:

Year Ended December 31	**2020**	**2019**	**2018**
Nonvested, January 1	25,984	12,892	1,538
Granted shares	16,269	17,345	11,468
Vested shares	8,455	2,542	114
Forfeited shares	1,875	1,711	
Nonvested, December 31	31,923	25,984	12,892

The Company expenses the fair value of all-share based compensation over the requisite service period commencing at grant date. The fair value of restricted stock is expensed on a straight-line basis. Compensation is recognized over the vesting period and adjusted based on the performance criteria. The Company classifies share-based compensation for employees within "salaries and employee benefits expense" on the Consolidated Statements of Income and Comprehensive Income.

In 2020, the Company recognized $570 for awards granted under the 2017 Plan. In 2019, the Company recognized $432 for awards granted under the 2017 Plan and $122 for awards granted under the 2008 plan. In 2018, the Company recognized $149 for awards granted under the 2017 Plan and $123 for awards granted under the 2008 plan. As of December 31, 2020, the Company had $586 of unrecognized compensation expense associated with restricted stock awards. The remaining cost is expected to be recognized over a weighted average vesting period of 1.9 years.

17. Employee benefit plans:

The Company sponsors a separate ESOP and Retirement Profit Sharing 401(k) Plan. The Company also maintains SERPs and an employees' pension plan, which is currently frozen.

Under the ESOP, amounts voted by the Company's board of directors are paid into the ESOP and each eligible participant is credited with an amount in proportion to their annual compensation or a fixed dollar amount. All contributions to the ESOP are invested in or will be invested primarily in Company stock. Distribution of a participant's ESOP account occurs upon retirement, death or termination in accordance with the plan provisions.

Under the Retirement Profit Sharing Plan, amounts approved by the board of directors have been paid into a fund and each participant was credited with an amount in proportion to their annual compensation. Upon retirement, death or termination, each participant is paid the total amount of their credits in the fund in one of a number of optional ways in accordance with the plan provisions. Eligible participants may elect deferrals of up to the maximum amounts permitted by law.

The Company contributed $371, $357 and $197 to the ESOP in 2020, 2019 and 2018. In addition, the Company contribution of $1,207, $1,139 and $1,047 to the Retirement Profit Sharing Plan in 2020, 2019 and 2018, was comprised of a safe harbor contribution of $655, $627 and $578 and a discretionary match of $552, $512 and $469.

The Company established a SERP Plan to replace certain 401(k) plan benefits lost due to compensation limits imposed on qualified plans by federal tax law. The annual benefit is a maximum of 6% of the executive compensation in excess of Federal limits. The total liability associated with this plan was $142 and $133 at December 31, 2020 and 2019, respectively. The expense associated with the plan was $9, $17 and $20 for 2020, 2019 and 2018 respectively.

The Company has SERPs for the benefit of certain officers. At December 31, 2020 and 2019, other liabilities include $2,351 and $2,077 accrued under the Plans. Compensation expense includes approximately $461, $360 and $335 relating to these SERPs for the years ended December 31, 2020, 2019 and 2018, respectively.

Under the Employees' Pension Plan, currently under curtailment, amounts computed on an actuarial basis were being paid by the Company into a trust fund. The plan provided for fixed benefits payable for life upon retirement at the age of 65, based on length of service and compensation levels as defined in the plan. As of June 22, 2008 no further benefits are being accrued in this plan. Plan assets of the trust fund are invested and administered by the Trust Department of the Company.

Information related to the Employees' Pension Plan is as follows:

	Pension Benefits	
December 31	**2020**	**2019**
Change in benefit obligation:		
Benefit obligation, beginning	$ 17,491	$ 16,338
Interest cost	544	639
Change in experience gain	(291)	96
Change in actuarial assumptions loss	2,159	1,221
Benefits paid	(790)	(803)
Benefit obligation, ending	19,113	17,491
Change in plan assets:		
Fair value of plan assets, beginning	16,930	14,919
Actual return on plan assets	1,488	2,814
Employer contributions		
Benefits paid	(790)	(803)
Fair value of plan assets, ending	17,628	16,930
Funded status at end of year	$ (1,485)	$ (561)

The Society of Actuaries updated the mortality scale within the mortality tables from MP 2019 to MP 2020 which the Company utilized in its pension plan remeasurements at December 31, 2020 and 2019. The change in the discount rate, coupled with changes in the mortality assumption, resulted in an increase to the benefit obligation of $2,159 in 2020 and $1,221 in 2019.

Amounts recognized in the consolidated balance sheets are as follows:

	Pension Benefits	
December 31	**2020**	**2019**
Liabilities	$ 1,485	$ 561
Amounts recognized in the accumulated other comprehensive loss consist of:		
Net actuarial gain	(7,977)	(6,579)
Deferred taxes	1,675	1,382
Net amount recognized	$ (6,302)	$ (5,197)

The accumulated benefit obligation for the defined benefit pension plan was $19,113 and $17,491 at December 31, 2020 and 2019, respectively.

Components of net periodic pension income and other amounts recognized in other comprehensive loss are as follows:

	Pension Benefits		
Years Ended December 31,	**2020**	**2019**	**2018**
Net periodic pension income:			
Interest cost	$ 544	$ 639	$ 623
Expected return on plan assets	(1,236)	(1,084)	(960)
Amortization of unrecognized net loss	218	227	194
Net periodic pension income:	(474)	(218)	(143)
Other changes in plan assets and benefit obligations recognized in other comprehensive income (loss):			
Net loss (gain)	544	639	(590)
Deferred tax	(114)	(134)	124
Total recognized in other comprehensive income (loss)	430	505	(466)
Total recognized in net period pension cost and other comprehensive income (loss)	$ (44)	$ 287	$ (609)

Weighted-average assumptions used to determine benefit obligations and related expenses were as follows:

	Pension Benefits		
December 31,	**2020**	**2019**	**2018**
Discount rate:			
Obligation	2.25 %	3.25 %	4.00 %
Expense	3.25	4.00	3.75
Expected long-term return on plan assets	7.50 %	7.50 %	7.50 %

The expected long-term return on plan assets was determined using average historical returns of the Company's plan assets.

The Company's pension plan weighted-average asset allocations at December 31, 2020 and 2019, by asset category are as follows:

December 31,	**2020**	**2019**
Asset Category:		
Cash and cash equivalents	6.8 %	6.2 %
Equity securities	63.3	61.9
Corporate bonds	20.7	20.6
U.S. government securities	9.2	11.3
	100.0 %	100.0 %

Fair value measurement of pension plan assets at December 31, 2020 and 2019 is as follows:

December 31, 2020	Total	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Observable Inputs (Level 2)	Significant Observable Inputs (Level 3)
Cash and cash equivalents	$ 1,203	$ 1,203		$
Equity securities:				
U.S. large cap	10,266	10,266		
International	888	888		
Fixed income securities:				
U.S. Treasuries	216		$ 216	
U.S. government agencies	1,400		1,400	
Corporate bonds	3,655		3,655	
Total	$ 17,628	$ 12,357	$ 5,271	$

December 31, 2019	Total	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Observable Inputs (Level 2)	Significant Observable Inputs (Level 3)
Cash and cash equivalents	$ 1,053	$ 1,053		$
Equity securities:				
U.S. large cap	9,663	9,663		
International	817	817		
Fixed income securities:				
U.S. Treasuries	202		$ 202	
U.S. government agencies	1,713		1,713	
Corporate bonds	3,482		3,482	
Total	$ 16,930	$ 11,533	$ 5,397	$

The Company investment policies and strategies with respect to the pension plan include: (i) the Trust and Investment Division's equity philosophy is large-cap core with a value bias. We invest in individual high-grade common stocks that are selected from our approved list; (ii) diversification is maintained by having no more than 20% in any industry sector and no individual equity representing more than 10% of the portfolio; and (iii) the fixed income style is conservative but also responsive to the various needs of our individual clients. Fixed income securities consist of U.S. government agencies or corporate bonds rated "A" or better. The Company targets the following allocation percentages: (i) cash equivalents 10%; (ii) fixed income 40% ; and (iii) equities 50%.

There is no Company stock included in equity securities at December 31, 2020 or 2019. The Company has not determined the amount of the expected contribution to the Employees' Pension Plan for 2021.

The following benefit payments are expected to be paid in the next five years and in the aggregate for the five years thereafter:

	Pension Benefits
2021	$ 840
2022	878
2023	896
2024	948
2025	970
Thereafter	5,019

18. Income taxes:

The current and deferred amounts of the provision for income taxes expense (benefit) for each of the years ended December 31, 2020, 2019 and 2018 are summarized as follows:

Year Ended December 31	2020	2019	2018
Current	$ 6,600	$ 2,761	$ 4,072
Deferred	(1,779)	394	(681)
Total	$ 4,821	$ 3,155	$ 3,391

The components of the net deferred tax asset at December 31, 2020 and 2019 are summarized as follows:

December 31	2020	2019
Deferred tax assets:		
Allowance for loan losses	$ 5,742	$ 4,762
Lease liability	1,349	1,301
Defined benefit plan	1,108	815
Deferred compensation	789	682
Deferred loan fees	1,368	525
Other	170	137
Total	10,526	8,222
Deferred tax liabilities:		
Lease right-of-use assets	1,319	1,286
Premises and equipment, net	1,455	1,350
Merger related accounting	694	850
Deferred loan costs	936	716
Investment securities available-for-sale	2,033	416
Other	321	242
Total	6,758	4,860
Net deferred tax asset	$ 3,768	$ 3,362

Management believes that future taxable income will be sufficient to utilize deferred tax assets. Core earnings of the Company have remained strong and will continue to support the recognition of the deferred tax asset based on future growth projections.

A reconciliation between the amount of the effective income tax expense and the income tax expense that would have been provided at the federal statutory rate of 21.0 percent for the years ended December 31, 2020, December 31, 2019 and December 31, 2018 is summarized as follows:

	2020		2019		2018	
Year Ended December 31	Amount	%	Amount	%	Amount	%
Federal income tax at statutory rate	$ 7,177	21.00 %	$ 6,067	21.00 %	$ 5,945	21.00 %
Effect of federal income tax rate changes (Note 1)						
Tax exempt interest	(1,032)	(3.02)	(1,299)	(4.50)	(1,320)	(4.66)
Bank owned life insurance income	(299)	(0.87)	(159)	(0.55)	(236)	(0.83)
Residential housing program tax credits	(1,094)	(3.20)	(1,094)	(3.79)	(1,094)	(3.87)
Other, net	69	0.19	(360)	(1.25)	96	0.34
Total	$ 4,821	14.10 %	$ 3,155	10.91 %	$ 3,391	11.98 %

19. Parent Company financial statements:

CONDENSED BALANCE SHEETS

December 31	2020	2019
Assets:		
Cash and cash equivalents	$ 1,069	$ 5,192
Equity securities	138	423
Investment in bank subsidiary	348,584	293,415
Other assets	273	19
Total assets	$ 350,064	$ 299,049
Liabilities and Stockholders' Equity:		
Subordinated debt	$ 33,000	
Accrued interest payable	148	
Other liabilities	39	$ 39
Stockholders' equity	316,877	299,010
Total liabilities and stockholders' equity	$ 350,064	$ 299,049

CONDENSED STATEMENTS OF INCOME

Year Ended December 31	2020	2019	2018
Income:			
Dividends from subsidiaries	$ 10,518	$ 10,131	$ 9,691
Other income	8	8	72
Net gain realized on sale of equity securities	29		
Unrealized holding gains (losses) on equity securities	(35)	132	13
Total income	10,520	10,271	9,776
Expense:			
Interest expense on subordinated debt	1,035		
Other expenses	200	145	214
Total expenses	1,235	145	214
Income before taxes and undistributed income	9,285	10,126	9,562
Income tax benefit	(255)	(1)	(27)
Income before undistributed income of subsidiaries	9,540	10,127	9,589
Equity in undistributed net income of subsidiaries	19,814	15,609	15,331
Net income	$ 29,354	$ 25,736	$ 24,920

CONDENSED STATEMENTS OF CASH FLOWS

Year Ended December 31	2020	2019	2018
Cash flows from operating activities:			
Net income	$ 29,354	$ 25,736	$ 24,920
Adjustments:			
Net losses (gains) on investment securities	6	(132)	(14)
Undistributed net income of subsidiaries	(19,814)	(15,609)	(15,331)
Decrease in other assets	(255)	(302)	(106)
Increase (decrease) in other liabilities	148		(10)
Stock based compensation	570	554	272
Increase in due from subsidiaries		1,974	
Net cash provided by operating activities	10,009	12,221	9,731
Cash flows from investing activities:			
Purchase of equity securities			(234)
Sale of equity securities	279		
Net cash provided by (used in) investing activities	279		(234)
Cash flows used in financing activities:			
Proceeds from subordinated debt	33,000		
Investment in subsidiary	(30,000)		
Retirement of stock	(6,893)	(634)	
Cash dividends paid	(10,518)	(10,131)	(9,693)
Net cash used in financing activities	(14,411)	(10,765)	(9,693)
Increase (decrease) in cash	(4,123)	1,456	(196)
Cash at beginning of year	5,192	3,736	3,932
Cash at end of year	$ 1,069	$ 5,192	$ 3,736

20. Regulatory matters:

Dividends are paid by the Parent Company from its assets, which are mainly provided by dividends from Peoples Bank. Under the Pennsylvania Business Corporation Law of 1988, as amended, the Company may not pay a dividend if, after payment, either the Company could not pay its debts as they become due in the usual course of business, or the Company's total assets would be less than its total liabilities. The determination of total assets and liabilities may be based upon: (i) financial statements prepared on the basis of GAAP; (ii) financial statements that are prepared on the basis of other accounting practices and principles that are reasonable under the circumstances; or (iii) a fair valuation or other method that is reasonable under the circumstances. In addition, the Federal Reserve Board has the power to prohibit dividends by bank holding companies if their actions constitute unsafe or unsound practices. The Federal Reserve Board has issued a policy statement on the payment of cash dividends by bank holding companies, which expresses the Federal Reserve Board's view that a bank holding company should pay cash dividends only to the extent that the company's net income for the past year is sufficient to cover both the cash dividends and a rate of earnings retention that is consistent with the company's capital needs, asset quality and overall financial condition. The Federal Reserve Board also indicated that it would be inappropriate for a bank holding company experiencing serious financial problems to borrow funds to pay dividends. Under the prompt corrective action regulations, the Federal Reserve Board may prohibit a bank holding company from paying any dividends if the holding company's bank subsidiary is classified as "undercapitalized."

In addition, under the Pennsylvania Banking Code of 1965, as amended, Peoples Bank may only declare and pay dividends out of accumulated net earnings, or accumulated net earnings acquired as a result of a merger within seven years. Further, Peoples Bank may not declare or pay any dividend unless Peoples Bank's surplus would not be reduced by the payment of the dividend below 100 percent of our capital stock. Pennsylvania law requires that each year Peoples Bank set aside as surplus, a sum equal to not less than 10 percent of its net earnings if surplus does not equal at least 100 percent of our capital stock. Under federal law and FDIC regulations, an insured bank may not pay dividends if doing so would make it undercapitalized within the meaning of the prompt corrective action law or if in default of its deposit insurance fund assessment.

Although subject to the aforementioned regulatory restrictions, the Company's consolidated retained earnings at December 31, 2020 and 2019 were not restricted under any borrowing agreement as to payment of dividends or reacquisition of common stock.

The Company has paid cash dividends since its formation as a bank holding company in 1986. It is the present intention of the Board of Directors to continue this dividend payment policy, however, further dividends must necessarily depend upon earnings, financial condition, appropriate legal restrictions and other factors relevant at the time the Board of Directors considers payment of dividends.

The amount of funds available for transfer from Peoples Bank to the Company in the form of loans and other extensions of credit is also limited. Under Federal regulation, transfers to any one affiliate are limited to 10.0 percent of capital and surplus. At December 31, 2020, the maximum amount available for transfer from Peoples Bank to the Company in the form of loans amounted to $31,002. At December 31, 2020 and 2019, there were no loans outstanding, nor were any advances made during 2020 and 2019.

The Company and Peoples Bank are subject to certain regulatory capital requirements administered by the federal banking agencies, which are defined in Section 38 of the Federal Deposit Insurance Corporation Improvement Act of 1991 ("FDICIA"). Failure to meet minimum capital requirements can initiate certain mandatory and possibly additional discretionary actions by regulators that, if undertaken, could have a direct material effect on the Company's and Peoples Bank's consolidated financial statements. In the event an institution is deemed to be undercapitalized by such standards, FDICIA prescribes an increasing amount of regulatory intervention, including the required institution of a capital restoration plan and restrictions on the growth of assets, branches or lines of business. Further restrictions are applied to the significantly or critically undercapitalized institutions including restrictions on interest payable on accounts, dismissal of management and appointment of a receiver. For well capitalized institutions, FDICIA provides authority for regulatory intervention when the institution is deemed to be engaging in unsafe and unsound practices or receives a less than satisfactory examination report rating. Under capital adequacy guidelines and the regulatory framework for prompt corrective action, the Company and Peoples Bank must meet specific capital guidelines that involve quantitative measures of their assets, liabilities and certain off-balance sheet items as calculated under regulatory accounting practices. The capital amounts and classifications are also subject to qualitative judgments by the regulators about components, risk weightings and other factors. Prompt corrective action provisions are not applicable to bank holding companies.

Risk-based capital rules require that banks and holding companies maintain a "capital conservation buffer" of 250 basis points in excess of the "minimum capital ratio." The minimum capital ratio is equal to the prompt corrective action adequately capitalized threshold ratio. Failure to maintain the required capital conservation buffer will result in limitations on capital distributions and on discretionary bonuses to executive officers.

Peoples Bank met the capital requirement for the "well capitalized" category under the regulatory framework for prompt corrective action at December 31, 2020. To be categorized as well capitalized, Peoples Bank must maintain certain minimum Tier I risk-based, total risk-based and Tier I Leverage ratios as set forth in the following tables. The Tier I Leverage ratio is defined as Tier I capital to total average assets less intangible assets. Regulators may assign Peoples Bank to a lower capitalization category based on factors other than capital.

The Company and Peoples Bank's actual capital ratios at December 31, 2020 and 2019, and the minimum ratios required for capital adequacy purposes and to be well capitalized under the prompt corrective action provisions are as follows:

December 31, 2020	Actual		Minimum For Capital Adequacy Purposes		Minimum to be Well Capitalized under Prompt Corrective Action Provisions	
	Amount	Ratio	Amount	Ratio	Amount	Ratio
Common equity Tier 1 capital to risk-weighted assets:						
Consolidated	$ 250,397	12.16 %	$ 92,631	4.50 %		
Peoples Bank	282,104	13.73	92,461	4.50	$ 133,554	6.50 %
Tier 1 capital to risk-weighted assets:						
Consolidated	250,397	12.16	123,508	6.00		
Peoples Bank	282,104	13.73	123,281	6.00	164,374	8.00
Total capital to risk-weighted assets:						
Consolidated	310,741	15.10	164,677	8.00		
Peoples Bank	307,807	14.98	164,374	8.00	205,468	10.00
Tier 1 capital to average assets:						
Consolidated	250,397	9.28	107,878	4.00		
Peoples Bank	282,104	10.08 %	111,891	4.00 %	139,864	5.00 %

December 31, 2019	Actual		Minimum For Capital Adequacy Purposes		Minimum to be Well Capitalized under Prompt Corrective Action Provisions	
	Amount	Ratio	Amount	Ratio	Amount	Ratio
Common equity Tier 1 capital to risk-weighted assets:						
Consolidated	$ 237,280	11.90 %	$ 89,717	4.50 %		
Peoples Bank	231,685	11.64	89,576	4.50	$ 129,387	6.50 %
Tier 1 capital to risk-weighted assets:						
Consolidated	237,280	11.90	119,623	6.00		
Peoples Bank	231,685	11.64	119,434	6.00	159,246	8.00
Total capital to risk-weighted assets:						
Consolidated	259,957	13.04	159,497	8.00		
Peoples Bank	254,362	12.78	159,246	8.00	199,057	10.00
Tier 1 capital to average assets:						
Consolidated	237,280	10.14	93,633	4.00		
Peoples Bank	231,685	9.91 %	93,508	4.00 %	116,884	5.00 %

21. Contingencies:

Neither the Company nor any of its property is subject to any material legal proceedings. Management, after consultation with legal counsel, does not anticipate that the ultimate liability, if any, arising out of pending and threatened lawsuits will have a material effect on the operating results or financial position of the Company.

22. Accumulated Other Comprehensive Income (Loss):

The components of accumulated other comprehensive income (loss) included in stockholders' equity at December 31, 2020 and 2019 are as follows:

	December 31, 2020	December 31, 2019
Net unrealized gain on investment securities available-for-sale	$ 9,696	$ 1,835
Income tax	2,036	385
Net of income taxes	7,660	1,450
Benefit plan adjustments	(7,977)	(6,579)
Income tax benefit	(1,675)	(1,382)
Net of income taxes	(6,302)	(5,197)
Derivative adjustments	1,002	687
Income tax	211	144
Net of income taxes	791	543
Accumulated other comprehensive income (loss)	$ 2,149	$ (3,205)

Other comprehensive income (loss) and related tax effects for the years ended December 31, 2020, 2019 and 2018 are as follows:

Year Ended December 31,	2020	2019	2018
Unrealized gain (loss) on investment securities available-for-sale	$ 8,779	$ 5,109	$ (2,014)
Net gain on the sale of investment securities available-for-sale	(918)	(23)	
Other comprehensive income on available-for-sale debt securities	7,861	5,086	(2,014)
Benefit plans:			
Amortization of actuarial loss (2)	218	227	194
Actuarial gain (loss)	(1,616)	412	(785)
Net change in benefit plan liabilities	(1,398)	639	(591)
Net change in derivatives	315	441	246
Other comprehensive loss before taxes	6,778	6,166	(2,359)
Income tax (benefit)	1,424	1,295	(496)
Other comprehensive income (loss)	$ 5,354	$ 4,871	$ (1,863)

(1) Represents amounts reclassified out of accumulated comprehensive income (loss) and included in gains on sale of investment securities on the consolidated statements of income and comprehensive income.

(2) Represents amounts reclassified out of accumulated comprehensive income (loss) and included in the computation of net periodic pension expense. Refer to Note 17 included in these consolidated financial statements.

23. Summary of quarterly financial information (unaudited):

	2020			
Quarter Ended	**March 31**	**June 30**	**Sept. 30**	**Dec. 31**
Interest income	$ 23,842	$ 23,852	$ 23,346	$ 23,085
Interest expense	4,281	3,345	3,422	3,276
Net interest income	19,561	20,507	19,924	19,809
Provision for loan losses	3,500	1,800	1,050	1,050
Net interest income after provision for loan losses	16,061	18,707	18,874	18,759
Noninterest income	3,550	3,422	4,935	4,735
Noninterest expense	13,651	13,242	13,974	14,001
Income before income taxes	5,960	8,887	9,835	9,493
Income tax expense	679	1,311	1,523	1,308
Net income	$ 5,281	$ 7,576	$ 8,312	$ 8,185
Per share data:				
Net income - basic	$ 0.72	$ 1.03	$ 1.14	$ 1.13
Net income - diluted	0.71	1.03	1.13	1.13
Cash dividends declared	$ 0.36	$ 0.36	$ 0.36	$ 0.36
Average common shares outstanding - basic	7,379,438	7,341,636	7,277,189	7,222,810
Average common shares outstanding - diluted	7,405,703	7,376,700	7,312,253	7,257,874

	2019			
Quarter Ended	**March 31**	**June 30**	**Sept. 30**	**Dec. 31**
Interest income	$ 22,801	$ 23,332	$ 23,632	$ 23,616
Interest expense	4,504	4,604	4,396	4,364
Net interest income	18,297	18,728	19,236	19,252
Provision for loan losses	1,050	350	700	4,000
Net interest income after provision for loan losses	17,247	18,378	18,536	15,252
Noninterest income	3,416	4,152	3,682	3,870
Noninterest expense	13,490	14,429	14,079	13,644
Income before income taxes	7,173	8,101	8,139	5,478
Income tax expense	761	957	991	446
Net income	$ 6,412	$ 7,144	$ 7,148	$ 5,032
Per share data:				
Net income - basic	$ 0.87	$ 0.96	$ 0.97	$ 0.68
Net income - diluted	0.87	0.96	0.96	0.68
Cash dividends declared	$ 0.34	$ 0.34	$ 0.34	$ 0.35
Average common shares outstanding - basic	7,379,438	7,399,302	7,394,992	7,388,488
Average common shares outstanding - diluted	7,408,536	7,413,114	7,417,403	7,410,899

Item 9. Changes in and Disagreements with Accountants on Accounting and Financial Disclosure.
None.

Item 9A. Controls and Procedures.

Evaluation of Disclosure Controls and Internal Controls

At December 31, 2020, the end of the period covered by this Annual Report on Form 10-K, the Chief Executive Officer ("CEO") and Chief Financial Officer ("CFO") evaluated the effectiveness of the Company's disclosure controls and procedures as defined in Rule 13a-15(e) under the Exchange Act. Based upon that evaluation, the CEO and CFO concluded that the disclosure controls and procedures, at December 31, 2020, were effective to provide reasonable assurance that information required to be disclosed in the Company's reports filed under the Exchange Act is recorded, processed, summarized and reported within the time periods specified in the SEC's rules and forms, and to provide reasonable assurance that information required to be disclosed in such reports is accumulated and communicated to the CEO and CFO to allow timely decisions regarding required disclosure.

MANAGEMENT'S REPORT ON INTERNAL CONTROL OVER FINANCIAL REPORTING

We are responsible for the preparation and fair presentation of the accompanying consolidated balance sheets of Peoples Financial Services Corp. and subsidiaries (the "Company") as of December 31, 2020 and 2019, and the related consolidated statements of income and comprehensive income, changes in stockholders' equity and cash flows for each of the years in the three-year period ended December 31, 2020, in accordance with accounting principles generally accepted in the United States. This responsibility includes: establishing, implementing and maintaining adequate internal controls relevant to the preparation and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error; selecting and applying appropriate accounting policies; and making accounting estimates that are reasonable under the circumstances. We are also responsible for compliance with the laws and regulations relating to safety and soundness that are designated by the Federal Deposit Insurance Corporation, Board of Governors of the Federal Reserve System and the Pennsylvania Department of Banking and Securities.

Our internal controls are designed to provide reasonable assurance that assets are safeguarded and transactions are initiated, executed, recorded and reported in accordance with our intentions and authorizations and to comply with applicable laws and regulations. The internal control system includes an organizational structure that provides appropriate delegation of authority and segregation of duties, established policies and procedures and comprehensive internal audit and loan review programs. To enhance the reliability of internal controls, we recruit and train highly qualified personnel and maintain sound risk management practices. The internal control system is maintained through a monitoring process that includes a program of internal audits.

Under Section 404 of the Sarbanes-Oxley Act of 2002, we are required to assess the effectiveness of our internal control over financial reporting at the end of each fiscal year and report, based on that assessment, whether the Company's internal control over financial reporting is effective. Our assessment includes controls over initiating, recording, processing and reconciling account balances, classes of transactions and disclosure and related assertions included in the financial statements. Our assessment also includes controls related to the initiation and processing of non-routine and non-systematic transactions, to the selection and application of appropriate accounting policies and to the prevention, identification and detection of fraud.

There are inherent limitations in any internal control system, including the possibility of human error and the circumvention or overriding of controls. Accordingly, even effective internal controls can provide only reasonable assurance with respect to financial statement preparation.

Furthermore, due to changes in conditions, the effectiveness of internal controls may vary over time. Our internal auditor reviews, evaluates and makes recommendations on policies and procedures, which serves as an integral, but independent, component of our internal control.

Our financial reporting and internal controls are under the general oversight of our board of directors, acting through its audit committee. The audit committee is composed entirely of independent directors. The independent registered public accounting firm and the internal auditor have direct and unrestricted access to the audit committee at all times. The audit committee meets periodically with us, the internal auditor and the independent registered public accounting firm to determine that each is fulfilling its responsibilities and to support actions to identify, measure and control risks and augment internal controls.

Our management, including our CEO and CFO, is responsible for establishing and maintaining adequate internal control over financial reporting for the Company. Our management, including our CEO and CFO, assessed the effectiveness of our internal controls over financial reporting as of December 31, 2020 using the criteria established in *Internal Control-Integrated Framework* (2013) issued by the Committee of Sponsoring Organizations of the Treadway Commission. These criteria are in the areas of control environment, risk assessment, control activities, information and communication, and monitoring. Our management's assessment included extensive documenting, evaluating and testing the design and operating effectiveness of our internal control over financial reporting.

Based on its assessment, management believes that our internal control over financial reporting was effective as of December 31, 2020.

Baker Tilly US, LLP, the Company's independent registered public accounting firm that audited our consolidated financial statements as of and for the year ended December 31, 2020 has issued an audit report on the Company's internal control over financial reporting as of December 31, 2020. That report is included in Item 8 of this Annual Report on Form 10-K.

/s/ Craig W. Best

Craig W. Best
Chief Executive Officer
(Principal Executive Officer)

/s/ John R. Anderson III

John R. Anderson III
Executive Vice President and Chief Financial Officer
(Principal Financial Officer and
Principal Accounting Officer)

March 16, 2021

Changes in Internal Control Over Financial Reporting
There were no changes in our internal control over financial reporting that occurred during the fiscal quarter ended December 31, 2020, that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

Item 9B. Other Information.

None.

PART III

Item 10. Directors, Executive Officers and Corporate Governance.
We incorporate the information required by this Item 10 by reference to the definitive proxy statement for our 2020 annual meeting of shareholders, to be filed with the Securities and Exchange Commission.

Item 11. Executive Compensation.
We incorporate the information required by this Item 11 by reference to the definitive proxy statement for our 2020 annual meeting of shareholders, to be filed with the Securities and Exchange Commission.

Item 12. Security Ownership of Certain Beneficial Owners and Management and Related Stockholder Matters.
We incorporate the information required by this Item 12 by reference to the definitive proxy statement for our 2020 annual meeting of shareholders, to be filed with the Securities and Exchange Commission.

Item 13. Certain Relationships and Related Transactions, and Director Independence.
We incorporate the information required by this Item 13 by reference to the definitive proxy statement for our 2020 annual meeting of shareholders, to be filed with the Securities and Exchange Commission.

Item 14. Principal Accounting Fees and Services.
We incorporate the information required by this Item 14 by reference to the definitive proxy statement for our 2020 annual meeting of shareholders, to be filed with the Securities and Exchange Commission.

PART IV

Item 15. Exhibits, Financial Statement Schedules.

All consolidated financial statements and financial statement schedules required to be filed by Form 10-K or by Regulation S-X that are applicable to us have been presented in the consolidated financial statements and notes thereto in Part II, Item 8, or elsewhere in this annual report, where appropriate. The listing of exhibits is set forth on the Exhibit Index beginning on page E-1 and is incorporated in this Item 15 by reference.

Item 16. Form 10-K Summary.

We have elected to omit the optional summary of information included in this Form 10-K.

EXHIBIT INDEX

Exhibit No.	Description of Exhibit
3.1	Peoples Financial Services Corp. Articles of Incorporation, as amended (incorporated by reference to Exhibit 3.1 to the registrant's Form 10-K filed with the Commission on March 17, 2014).
3.2	Articles of Amendment to the Articles of Incorporation of Peoples Financial Services Corp., effective as of May 19, 2020 (Incorporated by reference to Exhibit 3.2 to registrant's quarterly report on Form 10-Q filed with the Commission on August 10, 2020)
3.3	Amended and Restated Bylaws of Peoples Financial Services Corp. (incorporated by reference to Exhibit 3.1 to the registrant's Form 8-K filed with the Commission on December 2, 2013)
4.1	The Registrant agrees to furnish to the Commission upon request copies of all instruments defining the rights of holders of long-term debt of the registrant and its consolidated subsidiaries.
10.1	Peoples Financial Services Corp. Long-Term Incentive Plan, formerly known as the Penseco Financial Services Corporation 2008 Long Term Incentive Plan (incorporated by reference to Exhibit 10.1 of registrant's registration statement on Form S-8 (File No. 333-216321) filed with the SEC on February 28, 2017)*
10.2	Form of Restricted Stock or Restricted Stock Unit Award Agreement (incorporated by reference to Exhibit 10.2 to Penseco's registration statement on Form S-8 (File No. 333-166886) filed with the SEC on May 17, 2010)*
10.3	Form of Stock Option and/or Appreciation Right Award Agreement (incorporated by reference to Exhibit 10.3 to Penseco's registration statement on Form S-8 (File No. 333-166886) filed with the SEC on May 17, 2010)*
10.4	Form of Performance Award Agreement (incorporated by reference to Exhibit 10.4 to Penseco's registration statement on Form S-8 (File No. 333-166886) filed with the SEC on May 17, 2010)*
10.5	Peoples Security Bank and Trust Company Employee Stock Ownership Plan, amended and restated as of January 1, 2015 (incorporated by reference to Exhibit 10.1 to registrant's quarterly report on Form 10-Q filed with the SEC on May 5, 2017)*
10.6	2016 Compliance Amendment to the Peoples Security Bank and Trust Company Employee Stock Ownership Plan.
10.7	Amendment #2 to the Peoples Security Bank and Trust Company Employee Stock Ownership Plan.
10.8	Peoples Security Bank and Trust Company Executive Cash Bonus Plan, amended and restated as of May 8, 2020 (Incorporated by reference to Exhibit 10.1 attached to the registrant's current report on Form 8-K filed with the Commission on May 12, 2020)
10.9	Penn Security Bank & Trust Company Executive Deferred Compensation Plan (incorporated by reference to Exhibit 10.6 to the annual report of Penseco Financial Services Corp. on Form 10-K filed with the SEC on March 14, 2011)*
10.10	Employment Agreement, dated January 3, 2011, among Penseco Financial Services Corporation, Penn Security Bank & Trust, and Craig W. Best (incorporated by reference to Exhibit 10.1 of the current report of Penseco Financial Services Corp. on Form 8-K filed with the SEC on January 7, 2011)*
10.11	First Amendment to Employment Agreement dated December 31, 2015, by and among Peoples Financial Services Corp., Peoples Security Bank and Trust Company and Craig W. Best (incorporated by reference to Exhibit 10.1 of the current report of Penseco Financial Services Corp. on Form 8-K filed with the SEC on January 6, 2016)*
10.12	Amended and Restated Deferred Compensation Plan #2, dated April 22, 2014, by and between Peoples Security Bank and Trust Company and Craig W. Best (incorporated by reference to Exhibit 10.1 to the registrant's Form 8-K filed with the Commission on April 28, 2014)*
10.13	First Amendment to Amended and Restated Deferred Compensation Plan #2, dated August 29, 2015, by and between Peoples Security Bank and Trust Company and Craig Best (incorporated by reference to Exhibit 10.1 to the registrant's Form 8-K filed with the Commission on September 3, 2015)*
10.14	Second Amendment to Amended and Restated Deferred Compensation Plan #2, dated January 30, 2020, by and between Peoples Security Bank and Trust and Craig Best (incorporated by reference to Exhibit 10.01 to the registrant's Form 8-K filed with the Commission on January 31, 2020)*

Exhibit No.	Description of Exhibit
10.15	Penn Security Bank & Trust Company Excess Benefit Plan, amended and restated December 31, 2008 (incorporated by reference to Exhibit 10.9 to the annual report of Penseco Financial Services Corp. on Form 10-K filed with the SEC on March 14, 2011)*
10.16	Employment Agreement, dated May 30, 2012, among Penseco Financial Services Corporation, Penn Security Bank and Trust Company, and Thomas P. Tulaney (incorporated by reference to Exhibit 10.1 of the Registrant’s quarterly report on Form 10-Q filed with the SEC on August 9, 2012)*
10.17	Supplemental Executive Retirement Plan Agreement, dated May 31, 2012, by and among Penn Security Bank and Trust Company, Penseco Financial Services Corporation, and Thomas P. Tulaney (incorporated by reference to Exhibit 10.2 to the Registrant’s quarterly report on Form 10-Q filed with the SEC on August 9, 2012)*
10.18	Employment Agreement, dated as of August 27, 2014, by and between Peoples Bank and Neal D. Koplin (incorporated by reference to Exhibit 10.32 to the registrant’s Form 10-K filed with the Commission on March 16, 2015)*
10.19	Supplemental Executive Retirement Plan Agreement, dated April 24, 2017, by and among Peoples Security Bank and Trust Company, Peoples Financial Services Corp. and Neal D. Koplin (incorporated by reference to Exhibit 10.1 to registrant’s current report on Form 8-K filed with the Commission on April 25, 2017.)*
10.20	Form of Supplemental Director Retirement Plan Agreement for Non-employee Directors (incorporated by reference to Exhibit 10.7 to the registrant’s Form 10-K filed with the Commission on March 15, 2005) *
10.21	Form of Amendment to Supplemental Director Retirement Plan Agreement for Non-employee Directors (incorporated by reference to Exhibit 10.10 to the registrant’s Form 10-K filed with the Commission on March 15, 2006)*
10.22	Life Insurance Plan for all Non-employee Directors (incorporated by reference to Exhibit 10.21 to the registrant’s Form 10-K filed with the Commission on March 15, 2012)*
10.23	Employment Agreement dated as of September 30, 2016 between Peoples Security Bank and Trust Company and Timothy H. Kirtley (incorporated by reference to Exhibit 10.1 to the registrant’s quarterly report on Form 10-Q filed with the Commission on November 7, 2016)*
10.24	First Amendment to Employment Agreement dated as of December 5, 2017, by and between Peoples Security Bank and Trust Company and Timothy H. Kirtley(incorporated by reference to Exhibit 10.28 to the registrant’s annual report on Form 10-K filed with the Commission on March 14, 2018*
10.25	Second Amendment to Employment Agreement among Peoples Security Bank and Trust Company, Peoples Financial Services Corp. and Timothy H. Kirtley (Incorporated by reference to Exhibit 10.1 to registrant’s quarterly report on Form 10-Q filed with the Commission on August 10, 2020)
10.26	Change in Control Severance Agreement, dated as of January 5, 2021, by and between Peoples Security Bank and Trust Company and John R. Anderson, III (Incorporated by reference to Exhibit 10.1 to the registrant’s current report on Form 8-K filed with the Commission on January 8, 2021)
21.1	List of Subsidiaries
23.1	Consent of Baker Tilly US, LLP
24.1	Power of Attorney (Included as part of signature page)
31.1	Rule 13a-14(a)/15d-14(a) Certification of the Principal Executive Officer of Registrant
31.2	Rule 13a-14(a)/15d-14(a) Certification of the Principal Financial Officer of Registrant
32.1	Section 1350 Certifications of the Principal Executive Officer and Principal Financial Officer of Registrant
101.INS	Inline XBRL Instance Document
101.SCH	Inline XBRL Taxonomy Extension Schema
101.CAL	Inline XBRL Taxonomy Extension Calculation Linkbase
101.DEF	Inline XBRL Taxonomy Extension Definition Linkbase
101.LAB	Inline XBRL Taxonomy Extension Label Linkbase
101.PRE	Inline XBRL Taxonomy Extension Presentation Linkbase
104	Cover Page Interactive Data File (formatted as Inline XBRL and contained in Exhibit 101)
*	- Management contract or compensatory plan or arrangement

SIGNATURES

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

Peoples Financial Services Corp.

By:/s/ Craig W. Best
Craig W. Best
Chief Executive Officer
(Principal Executive Officer)

By:/s/ John R. Anderson III
John R. Anderson III
Executive Vice President and Chief Financial Officer
(Principal Financial Officer and Principal Accounting Officer)

POWER OF ATTORNEY

KNOW ALL PERSONS BY THESE PRESENTS, that each person whose signature appears below constitutes and appoints each of Craig W. Best and John R. Anderson III as his attorney-in-fact, with the full power of substitution, for him in any and all capacities, to sign any amendments to this report, and to file the same, with exhibits thereto and other documents in connection therewith, with the Securities and Exchange Commission, hereby ratifying and confirming all that said attorney-in-fact, or his substitute or substitutes, may do or cause to be done by virtue hereof.

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

Name	*Title*	*Date*
/s/ William E. Aubrey II William E. Aubrey II	Director and Chairman of the Board	March 16, 2021
/s/ Craig W. Best Craig W. Best	Director and Chief Executive Officer (Principal Executive Officer)	March 16, 2021
/s/ John R. Anderson III John R. Anderson III	Executive Vice President and Chief Financial Officer (Principal Financial Officer and Principal Accounting Officer)	March 16, 2021
/s/ Sandra L. Bodnyk Sandra L. Bodnyk	Director	March 16, 2021

Name	*Title*	*Date*
/s/ Ronald G. Kukuchka Ronald G. Kukuchka	Director	March 16, 2021
/s/ Richard S. Lochen, Jr. Richard S. Lochen, Jr.	Director	March 16, 2021
/s/ James B. Nicholas James B. Nicholas	Director	March 16, 2021
/s/ Steven L. Weinberger Steven L. Weinberger	Director	March 16, 2021
/s/ Joseph T. Wright, Jr. Joseph T. Wright, Jr.	Director	March 16, 2021

Element	Value
dei:EntityCentralIndexKey#	0001056943
dei:CurrentFiscalYearEndDate	--12-31
dei:DocumentFiscalYearFocus	2020
dei:DocumentFiscalPeriodFocus	FY
dei:AmendmentFlag	false