



First Bancshares, Inc.

Annual Report
December 31, 2014

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Letter to Shareholders

Dear Fellow Shareholder:

It is my pleasure to forward our Annual Report for 2014. This report is somewhat unique in that it is our second annual report for 2014 as the result of the change in First Bancshares, Inc. fiscal year from June 30 to December 31. This change was made to align our financial reporting periods with our regulatory reporting periods. Next year our annual report will be for the full year ended December 31, 2015.

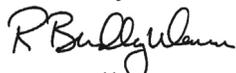
Our financial results continue to reflect our improved operations with continued earnings and stronger loan demand that has been reflected in our increasing loan growth. For the six months ended December 31, 2014, the Company had net income of \$142,000 or \$0.09 per diluted share. As a result, our book value per share increased from \$9.38 at June 30, 2014 to \$9.85 at December 31, 2014.

The recovery in our market area has been slow but we are encouraged by the increases we are seeing in loan demand. Our net loans receivable increased from \$109.93 million at June 30, 2014 to \$116.00 million at December 31, 2014. This included increases in commercial real estate and commercial business loans of \$3.22 million (7.6%) and \$1.37 million (16.1%), respectively, during the six months ended December 31, 2014.

During the six months ended December 31, 2014, we also continued to make good progress on the reduction of our non-performing assets. At December 31, 2014 we had \$1.25 million of non-performing loans compared \$1.28 million at June 30, 2014, and no other real estate owned at December 31, 2014 compared to \$80,000 in other real estate owned at June 30, 2014.

We continue to remain optimistic about the future. We believe that the positive results for the second half of 2014 coupled with our results for the first half of 2014 have positioned us well for the future. Thank you for your continued interest and support of First Bancshares, Inc. and First Home Bank. We look forward to seeing you at our Annual Stockholders Meeting on April 17, 2015 at 1:00 p.m.

Sincerely,



R. Bradley Weaver

President and Chief Executive Officer

Business of the Company

First Bancshares, Inc. (“Company”), a Missouri corporation, was incorporated on September 30, 1993 for the purpose of becoming the savings and loan holding company for First Home Savings Bank (“Bank”) upon the conversion of First Home from a Missouri mutual to a Missouri stock savings and loan association. The mutual to stock conversion was completed on December 22, 1993.

Effective January 22, 2014, the Bank changed its charter from a Missouri chartered stock savings and loan association to a Missouri chartered, non-member commercial bank. As part of the charter change, the Bank changed its corporate title to “First Home Bank.” In connection with the Bank’s charter change, the Company became a bank holding company, as approved by the Federal Reserve Bank of St. Louis.

Effective November 26, 2014, the Company and the Bank changed their fiscal year ends from June 30 to December 31. This change in fiscal year end was completed to align the financial reporting periods for the Company and the Bank with regulatory reporting periods now effective with the Company’s reorganization to a bank holding company and the Bank’s charter conversion to a commercial bank that occurred on January 22, 2014.

The Company is not engaged in any significant business activity other than holding the stock of the Bank. Accordingly, the information set forth in the report, including the consolidated financial statements and related data, applies primarily to the Bank.

First Home Bank is a Missouri-chartered, non-member commercial bank organized in 1911. The Bank is regulated by the Missouri Division of Finance and the Federal Deposit Insurance Corporation (“FDIC”). The Bank’s deposits are insured up to applicable limits by the FDIC.

The Bank is also a member of the Federal Home Loan Bank (“FHLB”) System. The Bank conducts its business from its home office in Mountain Grove and seven full service branch facilities in Marshfield, Ava, Kissee Mills, Gainesville, Sparta, Crane and Springfield, Missouri. The Bank provides its customers with a full array of community banking services and is primarily engaged in the business of attracting deposits from, and making loans to, the general public, including individuals and businesses. The Bank originates real estate loans, including one-to-four family residential mortgage loans, multi-family residential loans, commercial real estate loans and home equity loans, as well as, non-real estate loans, including commercial business and consumer loans. The Bank also invests in mortgage-back securities, United States Government and agency securities and other assets.

At December 31, 2014, the Company had total consolidated assets of \$196.4 million and consolidated stockholders’ equity of \$15.3 million.

SELECTED CONSOLIDATED FINANCIAL INFORMATION

The following tables set forth certain information concerning the consolidated financial position and operating results of the Company as of and for the dates indicated. The Company is primarily in the business of directing, planning and coordinating the business activities of First Home. The consolidated data is derived in part from, and should be read in conjunction with, the Consolidated Financial Statements of the Company and its subsidiaries presented herein.

	At Dec. 31,	2014	At June 30,			
	<u>2014</u>		<u>2013</u>	<u>2012</u>	<u>2011</u>	
			(In thousands)			
FINANCIAL CONDITION DATA:						
Total assets	\$	196,355	\$ 192,476	\$ 191,680	\$ 193,417	\$ 209,344
Loans receivable, net		116,003	109,934	95,554	95,521	95,817
Cash, interest-bearing deposits and securities		70,006	73,724	87,610	86,891	100,394
Deposits		168,746	166,386	163,834	165,858	180,661
Retail repurchase agreements		229	224	6,391	6,446	6,416
Borrowed funds		11,500	10,500	6,400	3,400	3,000
Stockholders' equity		15,267	14,541	14,250	16,335	18,065

	Six Months Ended Dec. 31	2014	Years Ended June 30,			
	<u>2014</u>		<u>2013</u>	<u>2012</u>	<u>2011</u>	
			(In thousands, except per share information)			
OPERATING DATA:						
Interest income	\$	3,188	\$ 6,132	\$ 6,074	\$ 6,747	\$ 8,253
Interest expense		534	1,068	1,261	1,491	2,104
Net interest income		2,654	5,064	4,813	5,256	6,149
Provision for loan losses		28	-	-	282	1,182
Net interest income after provision for loan losses		2,626	5,064	4,813	4,974	4,967
Gains (losses) on securities		(7)	79	309	712	315
Non-interest income, excluding gains (losses) on securities		479	1,073	820	978	(1,051)
Non-interest expense		2,956	5,621	6,035	8,013	7,751
Income (loss) before taxes		142	595	(93)	(1,349)	(3,520)
Income tax expense		-	-	-	85	581
Net income (loss)	\$	142	\$ 595	\$ (93)	\$ (1,434)	\$ (4,101)
Basic earnings (loss) per share	\$	0.09	\$ 0.38	\$ (0.06)	\$ (0.92)	\$ (2.66)
Diluted earnings (loss) per share	\$	0.09	\$ 0.38	\$ (0.06)	\$ (0.92)	\$ (2.66)
Dividends per share	\$	0.00	\$ 0.00	\$ 0.00	\$ 0.00	\$ 0.00

	Six Months Ended Dec. 31		At or For the Years June 30,			
	<u>2014</u>	<u>2014</u>	<u>2013</u>	<u>2012</u>	<u>2011</u>	
KEY OPERATING RATIOS:						
Return on average assets	0.15 %	0.31 %	N/A %	N/A %	N/A %	
Return on average equity	1.93	4.26	N/A	N/A	N/A	
Average equity to average assets	7.65	7.31	8.22	8.81	10.32	
Interest rate spread for period	2.85	2.79	2.64	2.79	3.10	
Net interest margin for period	2.86	2.81	2.67	2.88	3.22	
Non-interest expense to average assets	3.06	2.92	3.15	4.08	3.73	
Average interest-earning assets to interest-bearing liabilities	111.12	110.32	111.38	111.04	110.80	
Allowance for loan losses to total loans at end of period	1.41	1.42	1.65	1.86	2.03	
Net charge-offs (recoveries) to average loans outstanding during the period	(0.01)	0.02	0.08	0.48	1.70	
Dividend payout ratio	N/A	N/A	N/A	N/A	N/A	

	At Dec. 31		June 30,		
	<u>2014</u>	<u>2014</u>	<u>2013</u>	<u>2012</u>	<u>2011</u>
OTHER DATA:					
Number of:					
Loans outstanding	1,726	1,710	1,774	1,937	2,132
Deposit accounts	15,564	15,870	16,912	17,995	19,103
Full service offices	8	8	8	9	11



Independent Auditor's Report

To the Board of Directors
First Bancshares, Inc. and Subsidiaries
Mountain Grove, Missouri

Report on the Financial Statements

We have audited the accompanying consolidated financial statements of First Bancshares, Inc. and Subsidiaries which comprise the consolidated balance sheets as of December 31, 2014 and June 30, 2014, and the related consolidated statements of operations, comprehensive income, stockholders' equity and cash flows for the six month period ended December 31, 2014 and the related notes to the consolidated financial statements.

Management's Responsibility for the Financial Statements

Management is responsible for the preparation and fair presentation of these consolidated financial statements in accordance with accounting principles generally accepted in the United States of America; this includes the design, implementation, and maintenance of internal control relevant to the preparation and fair presentation of consolidated financial statements that are free from material misstatement, whether due to fraud or error.

Auditor's Responsibility

Our responsibility is to express an opinion on these consolidated financial statements based on our audits. We conducted our audits in accordance with auditing standards generally accepted in the United States of America. 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.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the consolidated financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the consolidated financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the consolidated financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the consolidated financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

Opinion

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of First Bancshares, Inc. and Subsidiaries as of December 31, 2014, and the results of its operations and its cash flows for the six month period ended December 31, 2014 in accordance with accounting principles generally accepted in the United States of America.

McGladrey LLP

Kansas City, Missouri
March 5, 2015

First Bancshares, Inc. and Subsidiaries

Consolidated Balance Sheets

December 31, 2014, and June 30, 2014

Assets	December 31, 2014	June 30, 2014
Cash and cash equivalents	\$ 4,239,541	\$ 11,261,514
Interest-bearing deposits at other financial institutions	3,182,022	-
Securities available for sale	62,584,659	62,461,515
Federal Home Loan Bank stock, at cost	685,700	645,700
Loans receivable, net	116,002,607	109,934,301
Premises and equipment, net	5,547,452	4,132,966
Real estate owned and other repossessed assets, net	-	80,129
Cash surrender value of bank owned life insurance	3,332,575	3,280,567
Other assets	779,963	679,018
Total assets	\$ 196,354,519	\$ 192,475,710
Liabilities and Stockholders' Equity		
Liabilities:		
Deposits	\$ 168,746,060	\$ 166,386,059
Repurchase agreements	229,009	224,026
Federal Home Loan Bank borrowings	11,500,000	10,500,000
Other liabilities	611,998	824,822
Total liabilities	181,087,067	177,934,907
Commitments and Contingencies (Notes 4 and 11)		
Stockholders' Equity:		
Preferred stock, \$.01 par value; 2,000,000 shares authorized, none issued	-	-
Common stock, \$.01 par value; 8,000,000 shares authorized, issued 2,895,036; outstanding 1,549,515 at December 31, 2014 and June 30, 2014	28,950	28,950
Additional paid-in-capital	18,062,566	18,062,566
Retained earnings	17,648,247	17,505,838
Accumulated other comprehensive loss	(1,348,952)	(1,933,192)
	34,390,811	33,664,162
Treasury stock, at cost, 1,345,521 at December 31, 2014 and June 30, 2014	(19,123,359)	(19,123,359)
Total stockholders' equity	15,267,452	14,540,803
Total liabilities and stockholders' equity	\$ 196,354,519	\$ 192,475,710

See Notes to Consolidated Financial Statements.

First Bancshares, Inc. and Subsidiaries

**Consolidated Statement of Operations
Six-Month Period Ended December 31, 2014**

	Six month period ended December 31, 2014
Interest income:	
Loans	\$ 2,607,356
Securities	567,161
Other interest-earning assets	13,743
	<u>3,188,260</u>
Interest expense:	
Deposits	496,612
Repurchase agreements	612
Federal Home Loan Bank borrowings	37,246
	<u>534,470</u>
Net interest income	<u>2,653,790</u>
Provision for loan losses	28,000
Net interest income after provision for loan losses	<u>2,625,790</u>
Non-interest income:	
Service charges and other fee income	403,896
Loss on sale of securities	(6,650)
Gain on sale of real estate owned and other repossessed assets	1,680
Other	73,353
	<u>472,279</u>
Non-interest expense:	
Compensation and employee benefits	1,406,708
Occupancy and equipment	652,631
Professional fees	211,095
Deposit insurance premiums	64,411
Impairment losses on real estate owned	10,000
Other	610,815
	<u>2,955,660</u>
Net income	<u>142,409</u>
Basic and diluted income per share	<u>\$ 0.09</u>

See Notes to Consolidated Financial Statements.

First Bancshares, Inc. and Subsidiaries

**Consolidated Statements of Comprehensive Income
Six-Month Period Ended December 31, 2014**

	Six month period ended December 31, 2014
Net income	<u>\$ 142,409</u>
Other comprehensive income:	
Unrealized holding gains arising during the year	590,890
Reclassification adjustment for (losses) included in net income before income taxes	<u>(6,650)</u>
Comprehensive income	<u><u>\$ 726,649</u></u>

See Notes to Consolidated Financial Statements.

First Bancshares, Inc. and Subsidiaries

**Consolidated Statement of Stockholders' Equity
Six-Month Period Ended December 31, 2014**

	Common Stock	Additional Paid-in Capital	Retained Earnings	Treasury Stock	Accumulated Other Comprehensive Loss	Total Stockholders' Equity
Balance, June 30, 2014	\$ 28,950	\$ 18,062,566	\$ 17,505,838	\$ (19,123,359)	\$ (1,933,192)	\$ 14,540,803
Net income	-	-	142,409	-	-	142,409
Other comprehensive income	-	-	-	-	584,240	584,240
Balance, December 31, 2014	\$ 28,950	\$ 18,062,566	\$ 17,648,247	\$ (19,123,359)	\$ (1,348,952)	\$ 15,267,452

See Notes to Consolidated Financial Statements.

First Bancshares, Inc. and Subsidiaries

**Consolidated Statement of Cash Flows
Six-Month Period Ended December 31, 2014**

	Six month period ended December 31, 2014
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Cash Flows From Operating Activities	
Net income	\$ 142,409
Adjustments to reconcile net income to net cash provided by operating activities:	
Depreciation	188,415
Net premium amortization on securities	85,475
Loss on sale of securities	6,650
Provision for loan losses	28,000
Impairment losses on real estate owned	10,000
Impairment of premises and equipment	9,897
Gain on sale of real estate owned and other repossessed assets	(1,680)
Net change in operating assets and liabilities:	
Increase in cash surrender value of bank owned life insurance	(52,008)
Other assets	(100,945)
Other liabilities	(212,824)
Net cash provided by operating activities	<u>103,389</u>
 Cash Flows From Investing Activities	
Net decrease (increase) in interest-bearing deposits in other financial institutions	(3,182,022)
Purchase of securities available for sale	(9,123,326)
Proceeds from sales, maturities and principal paydowns of securities available for sale	9,492,297
Purchase of Federal Home Loan Bank stock	(40,000)
Net increase in loans receivable	(6,296,806)
Purchase of premises and equipment	(1,612,798)
Proceeds from sale of real estate owned and other repossessed assets	272,309
Net cash used in investing activities	<u>(10,490,346)</u>

(Continued)

First Bancshares, Inc. and Subsidiaries

Consolidated Statement of Cash Flows (Continued)
Six-Month Period Ended December 31, 2014

	Six month period ended December 31, 2014
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Cash Flows From Financing Activities	
Net increase in deposits	\$ 2,360,001
Net increase in repurchase agreements	4,983
Proceeds from Federal Home Loan Bank advances	4,000,000
Repayment of Federal Home Loan Bank advances	<u>(3,000,000)</u>
Net cash provided by activities	3,364,984
Net decrease in cash and cash equivalents	(7,021,973)
Cash and Cash Equivalents	
Beginning of period	<u>11,261,514</u>
End of period	<u>\$ 4,239,541</u>
Supplemental Disclosure of Cash Flow Information	
Cash paid during the year for:	
Interest on deposits and other borrowings	<u>\$ 540,997</u>
Supplemental Schedule of Non-Cash Investing and Financing Activities	
Loans transferred to real estate owned	<u>\$ 200,500</u>

See Notes to Consolidated Financial Statements.

First Bancshares, Inc. and Subsidiaries

Notes to Consolidated Financial Statements

Note 1. Summary of Significant Accounting Policies

Nature of operations: First Bancshares, Inc., a Missouri corporation (Company), is the holding company for First Home Bank (Bank). The Bank is primarily engaged in providing a full range of banking and mortgage services to individual and corporate customers in southern Missouri. On January 22, 2014, the Bank completed a charter conversion to a Missouri chartered non-member commercial bank from a Missouri chartered stock non-member thrift and changed its title from First Home Savings Bank to First Home Bank. The Company and Bank are also subject to the regulation by certain federal and state agencies and undergo periodic examinations by those regulatory authorities.

On November 26, 2014, the Bank approved changing its fiscal year end from June 30 to December 31. Balance sheets presented in this report are comparative, as of December 31, 2014 and June 30, 2014 and the statements of operations, comprehensive income, stockholders' equity and cash flows are for the six-months ended December 31, 2014.

Principles of consolidation: The accompanying consolidated financial statements include the accounts of the Company, and its wholly-owned subsidiaries, the Bank and SCMG, Inc. (formerly South Central Missouri Title, Inc.) and the wholly-owned subsidiaries of the Bank, Fybar Service Corporation and First Home Investments. In consolidation, all significant intercompany balances and transactions have been eliminated.

Use of estimates: In preparing the consolidated financial statements in conformity with accounting principles generally accepted in the United States of America, management is required to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities as of the date of the balance sheet and reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates. Material estimates that are particularly susceptible to significant change in the near term relate to the determination of the fair value of financial instruments, the allowance for loan losses, and the valuation allowance on deferred income tax assets.

Concentrations of credit risk: Most of the Company's lending activity occurs within the State of Missouri, including eleven counties surrounding one of the largest metropolitan areas in the State of Missouri, Springfield, as well as other markets. The majority of the Company's loan portfolio consists of residential real estate, commercial and commercial real estate loans. As of December 31, 2014 and June 30, 2014, there were no concentrations of loans related to any single industry in excess of 10 percent of total loans.

Cash and cash equivalents: For purposes of the consolidated statements of cash flows, cash consists of cash on hand and deposits with other financial institutions. Cash equivalents include highly-liquid instruments with an original maturity of three months or less. Cash flows from interest-bearing deposits in other financial institutions, loans, deposits, and retail repurchase agreements are reported net.

Securities: All securities are designated as available-for-sale, a designation which provides the Company with certain flexibility in managing its investment portfolio. Such securities are reported at fair value with unrealized gains and losses excluded from income and reported net of applicable income taxes as a component of comprehensive income.

Interest income on securities is recognized on the interest method according to the terms of the security. Gains or losses on sales of securities are recognized in operations at the time of sale and are determined by the difference between the net sales proceeds and the cost of the securities using the specific identification method, adjusted for any unamortized premiums or discounts. Premiums or discounts are amortized or accreted to income using the interest method over the period to maturity.

First Bancshares, Inc. and Subsidiaries

Notes to Consolidated Financial Statements

Note 1. Summary of Significant Accounting Policies (Continued)

Declines in the fair value of equity securities below their amortized cost basis that are deemed to be other-than-temporary impairment losses are reflected as realized losses in the consolidated statement of operations. To determine if an other-than-temporary impairment exists on an equity security, the Company considers (a) the length of time and the extent to which the fair value has been less than cost, (b) the financial condition and near-term prospects of the issuer, (c) the intent and ability of the Company to retain its investment in the issuer for a period of time sufficient to allow for an anticipated recovery in fair value and (d) the current market conditions. To determine if an other-than-temporary-impairment exists on a debt security, the Company first determines if (a) it intends to sell the security or (b) it is more likely than not that it will be required to sell the security before its anticipated recovery. If either of the conditions is met, the Company will recognize an other-than-temporary-impairment in earnings equal to the difference between the fair value of the security and its adjusted cost basis. If neither of the conditions is met, the Company determines (a) the amount of the impairment related to credit loss and (b) the amount of the impairment due to all other factors. The difference between the present values of the cash flows expected to be collected and the amortized cost basis is the credit loss. The amount of the credit loss is included in the consolidated statements of operations as an other-than-temporary impairment on securities and is an adjustment to the cost basis of the security. The portion of the total impairment that is related to all other factors is included in other comprehensive income.

Federal Home Loan Bank stock: The Bank, as a member of the Federal Home Loan Bank (FHLB) system, is required to maintain an investment in capital stock of the FHLB of Des Moines. The stock does not have a readily determinable fair market value and, as such, is carried at cost and evaluated for impairment annually. There have been no other-than-temporary impairments recorded on this security.

Loans receivable: Loans receivable are stated at the amount of unpaid principal, reduced by an allowance for loan losses. Direct loan origination fees and costs are generally being deferred and the net amounts amortized as an adjustment of the related loan's yield. The Company generally amortizes these amounts over the contractual life. Direct loan origination fees and costs related to loans sold to unrelated third parties are recognized as income or expense in the current consolidated statement of operations. Commitment fees based upon a percentage of customers' unused lines of credit and fees related to standby letters of credit are not significant to the consolidated financial statements.

The Company's portfolio segments and classes are as follows:

Real estate:

- Residential
- Commercial

Land

Consumer

Commercial

Generally, for all classes of loans, loans are considered past due if the required principal and interest payments have not been received as of the date such payments were due. Loans are placed on non-accrual status when, in management's opinion, the borrower may be unable to meet payment obligations as they become due, as well as when required by regulatory provisions, which is generally when loans become 90 days past due. Loans may be placed on non-accrual status regardless of whether or not such loans are considered past due. When interest accrual is discontinued, all unpaid accrued interest is reversed. Interest income is subsequently recognized only to the extent cash payments are received in excess of principal due. Loans are returned to accrual status when all the principal and interest amounts contractually due are brought current and future payments are reasonably assured.

First Bancshares, Inc. and Subsidiaries

Notes to Consolidated Financial Statements

Note 1. Summary of Significant Accounting Policies (Continued)

Troubled debt restructures: A troubled debt restructuring exists when the Company, for economic or legal reasons related to the borrower's financial difficulties, grants a concession (either imposed by court order, law, or agreement between the borrower and the Company) to the borrower that it would not otherwise consider. These concessions could include forgiveness of principal, extension of maturity dates, and reduction of stated interest rates or accrued interest. The Company is attempting to maximize its recovery of the balances of the loans through these various concessionary restructurings. See Note 3 for disclosure of the Company's troubled debt restructurings.

Allowance for loan losses: For all classes of loans, the allowance for loan losses is maintained at the level considered adequate by management of the Company to provide for losses that are probable. The allowance is increased by provisions charged to operating expense and reduced by net charge-offs. In determining the adequacy of the allowance balance, the Company makes continuous evaluations of the loan portfolio and related off-balance sheet commitments, considers current economic conditions, historical loan loss experience, review of specific problem loans and other factors.

A discussion of the risk characteristics and the allowance for loan losses by each loan class follows:

For real estate and land loans, the Company focuses on real estate developers, investors, and owner occupants in its recognized trade area. The Company provides term loans to finance the acquisition of real estate and lines of credit to finance land acquisition and development and construction of 1-4 family residential and commercial properties. The Company finances various types of real estate, including non-residential and residential owner occupied, land acquisition and development, and non-residential, non-owner occupied properties. It is the Company's policy that prudently underwritten real estate loans should reflect all relevant credit factors and approval is based on the following:

- The capacity of the borrower, or income from the underlying property, to adequately service the debt.
- The value of the mortgaged property.
- The overall credit worthiness of the borrower, and borrower's liquidity.
- The level of equity invested in the property.
- Historic and projected cash flow data, including interest and vacancy rates and sensitivity analysis, if investment property related.
- Any secondary sources of repayment.

Commercial and commercial real estate loans are underwritten after evaluating and understanding the borrower's ability to operate profitably and prudently expand its business. Underwriting standards are designed to promote relationship banking rather than transactional banking. Once it is determined that the borrower's management possesses sound ethics and solid business acumen, the Company's management examines current and projected cash flows to determine the ability of the borrower to repay their obligations as agreed. Commercial loans are primarily made based on the identified cash flows of the borrower and secondarily on the underlying collateral provided by the borrower. The cash flows of borrowers, however, may not be as expected and the collateral securing these loans may fluctuate in value. Most commercial loans are secured by the assets being financed, including business equipment loans, farm equipment loans and cattle loans and may incorporate a personal guarantee; however, some short-term loans may be made on an unsecured basis. In the case of loans secured by accounts receivable, the availability of funds for the repayment of these loans may be substantially dependent on the ability of the borrower to collect amounts due from its customers.

First Bancshares, Inc. and Subsidiaries

Notes to Consolidated Financial Statements

Note 1. Summary of Significant Accounting Policies (Continued)

The Company originates consumer loans utilizing a computer-based credit scoring analysis to supplement the underwriting process. To monitor and manage consumer loan risk, policies and procedures are developed and modified, as needed. This activity, coupled with relatively small loan amounts that are spread across many individual borrowers, minimizes risk. Additionally, trend and outlook reports are reviewed by management on a regular basis. Underwriting standards for home equity loans are heavily influenced by statutory requirements, which include, but are not limited to, a maximum loan-to-value, collection remedies, the total aggregate balance to one borrower and documentation requirements.

In some instances for all loans, it may be appropriate to originate or purchase loans that are exceptions to the guidelines and limits established within the lending policy described above and below. In general, exceptions to the lending policy do not significantly deviate from the guidelines and limits established within the lending policy and, if there are exceptions, they are clearly noted as such and specifically identified in loan approval documents.

The allowance for estimated losses on loans consists of specific and general components.

The specific component relates to loans that are classified as impaired, as defined below. For those loans that are classified as impaired, an allowance is established when the discounted cash flows (or collateral value or observable market price) of the impaired loan is lower than the carrying value of that loan.

A loan is considered impaired when, based on current information and events, it is probable that the Company will be unable to collect the scheduled payments of principal or interest when due according to the contractual terms of the loan agreement. Factors considered by management in determining impairment include payment status, collateral value, and the probability of collecting scheduled principal and interest payments when due. 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. Impairment is measured on a case-by-case basis by either the present value of expected future cash flows discounted at the loan's effective interest rate, the loan's observable market price, or the fair value of the collateral if the loan is collateral dependent.

The general component consists of quantitative and qualitative factors and covers non-impaired loans. The quantitative factors are based on historical charge-off experience and expected loss given default derived from the Company's internal risk rating process. See below for a detailed description of the Company's internal risk rating scale. The qualitative factors are determined based on an assessment of internal and/or external influences on credit quality that are not fully reflected in the historical loss or risk rating data.

For all loans, the Company utilizes the following internal risk rating scale:

Grade 1: This risk grading is generally reserved for credits fully secured by deposits at the Bank.

Grade 2: These are well established borrowers operating in a reasonably stable industry that may be only moderately affected by the business cycle. Management, owners, and guarantors have unquestioned character, as demonstrated by repeated performance. Elements of strength are present in such areas as liquidity, stability of margins and cash flows, diversity of assets, and lack of dependence on one type of business. The total credit relationship is less than \$500,000.

First Bancshares, Inc. and Subsidiaries

Notes to Consolidated Financial Statements

Note 1. Summary of Significant Accounting Policies (Continued)

Grade 3: This grade includes loans that are “pass grade” loans to borrowers of acceptable credit quality and risk. These borrowers have satisfactory asset quality and liquidity, adequate debt capacity and coverage, and good management in critical positions.

Grade 4: This grade includes loans that require “increased management attention.” These borrowers generally have limited additional debt capacity and modest coverage and average or below average asset quality, margins, and market share.

Grade 5: A special mention asset has potential weaknesses that deserve management’s close attention. If left uncorrected, these potential weaknesses may result in deterioration of the repayment prospects for the asset or in the institution’s credit position at some future date. Assets that could be included in the Special Mention category include those that have developed minor credit weaknesses since origination as well as those that were originated with such weaknesses. This includes loans the institution is unable to properly supervise because of an inadequate loan agreement, inadequate control over collateral (when such control is necessary to effect full repayment of the loan), or when a loan is made with significant deviations from prudent lending practices.

Grade 6: A “substandard” asset is inadequately protected by the current net worth and/or paying capacity of the obligor or by the collateral pledged, if any. Assets 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 institution will sustain some loss if the deficiencies are not corrected.

Assets classified substandard may be characterized by one or a combination of the following weaknesses:

- The primary source of repayment is gone or severely impaired and the institution may have to rely upon the secondary source.
- The asset is (or was) a loan or an investment that is nonperforming or nonearning.
- A loss may not seem likely, but sufficient problems have arisen to cause the Bank to go to extraordinary lengths to protect its position in order to maintain a high probability of repayment.
- The obligors are unable to generate enough cash flow to reduce their debts.
- There is a material deterioration in collateral value (if the collateral is expected to be a primary source of repayment).
- Flaws in security agreement or lien documentation leave the Bank in a subordinated or unsecured position when the collateral is likely to be needed for the repayment of the loan.

Grade 7: An asset classified “Doubtful” has all the weaknesses inherent in one classified substandard with the added characteristic that the weaknesses make collection or liquidation in full, on the basis of currently known facts, conditions, and values, highly questionable and improbable. The likelihood of a loss on an asset or portion of an asset classified Doubtful is high. Its classification as Loss is not appropriate, however, because pending events are expected to materially reduce the amount of loss.

Grade 8: An asset or portion thereof, classified “Loss” is considered uncollectible and of such little value that its continuance on the institution’s books as an asset, without establishment of a specific valuation allowance or charge-off, is not warranted. This classification does not necessarily mean that an asset has no recovery or salvage value; but rather, there is much doubt about whether, how much, or when the recovery would occur. As such, it is not practical or desirable to defer the write-off.

First Bancshares, Inc. and Subsidiaries

Notes to Consolidated Financial Statements

Note 1. Summary of Significant Accounting Policies (Continued)

The Company employs independent, outside consultants who review and validate the credit risk program on a periodic basis. The review consists of a sample of commercial and real estate loans, and includes a selection of borrowing relationships over \$500,000 and selected criticized loans. Results of these reviews are presented to management and the Board of Directors. The loan review process complements and reinforces the risk identification and assessment decisions made by lenders and credit personnel, as well as the Company's policies and procedures.

The Company provides many types of consumer and other loans including motor vehicle, home improvement, home equity, and small personal loans. The lending policy addresses specific credit guidelines by consumer loan type.

For residential real estate loans, consumer and other loans, these large groups of smaller balance homogenous loans are collectively evaluated for impairment, unless the loan has been restructured as a troubled debt restructuring, in which case the loan would be specifically evaluated for impairment. The Company applies a quantitative factor based on historical charge-off experience in total for each of these segments.

Troubled debt restructures are considered impaired loans and are subject to the same allowance methodology as described above for impaired loans by portfolio segment.

Credit related financial instruments: Financial instruments include off-balance-sheet credit instruments, such as commitments to make loans and commercial letters of credit, issued to meet customer financing needs. The face amount for these items represents the exposure to loss, before considering customer collateral or ability to repay. Such financial instruments are recorded when they are funded.

Cash surrender value of bank owned life insurance: The Company has purchased life insurance policies on certain key executives. Bank owned life insurance is recorded at its cash surrender value, or the amount that can be realized upon surrender of the policy.

Premises and equipment, net: Premises and equipment are stated at cost less accumulated depreciation. Land is carried at cost. Depreciation is computed principally on a straight line basis over the estimated useful lives of the related assets. Additions, major replacements and improvements are added to the respective asset balance at cost. Maintenance, repairs and minor replacements are charged directly to expense as incurred. Buildings and investment real estate have estimated useful lives ranging from 15 to 40 years. All other assets have estimated useful lives ranging from three to 10 years with improvements being depreciated over the remaining estimated life of the related asset.

Real estate owned and repossessed assets: Real estate acquired through foreclosure is initially recorded at fair value, less estimated costs to sell, establishing a new cost basis. If the fair value less costs to sell is less than the respective loan balance, a charge against the allowance for loan losses is recorded upon property acquisition. Declines in property value subsequent to acquisition are charged to operations. Holding costs are expensed as incurred.

First Bancshares, Inc. and Subsidiaries

Notes to Consolidated Financial Statements

Note 1. Summary of Significant Accounting Policies (Continued)

Transfers of financial assets: Transfers of financial assets are accounted for as sales only 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 to pledge or exchange the assets it received, and no condition both constrains the transferee from taking advantage of its right to pledge or exchange and provides more than a modest benefit to the transferor, and (3) the Company does not maintain effective control over the transferred assets through an agreement to repurchase them before their maturity or the ability to unilaterally cause the holder to return specific assets.

Impairment of long-lived assets: Long-lived assets, including property and equipment, are reviewed for impairment whenever events or changes in circumstances indicate the carrying amount of an asset may not be recoverable. If such assets are considered to be impaired, the impairment to be recognized is measured by the amount by which the carrying amount of the assets exceeds the fair value of the assets.

Repurchase agreements: The Company has entered into sales of securities under agreements to repurchase. The amounts deposited under these agreements represent short-term borrowings and are reflected as a liability in the consolidated balance sheet. Securities held in safekeeping are pledged to the depositors under a written custodial agreement that explicitly recognizes the depositors' interest in the securities. Securities sold under agreements to repurchase generally mature within one day to twelve months from the transaction date.

Income taxes: The Company files its tax return on a consolidated basis with its subsidiaries. The entities follow the direct reimbursement method of accounting for income taxes under which income taxes or credits which result from the subsidiaries' inclusion on the consolidated tax return are paid to or received from the parent company.

Deferred taxes are determined using the liability (or balance sheet) method whereby deferred tax assets are recognized for deductible temporary differences and operating loss and tax credit carry-forwards 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 bases. Deferred tax assets are reduced by a valuation allowance when, in the opinion of management, it is more likely than not that some portion or all 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 date of enactment.

The Company accounts for uncertainty in income taxes, which addresses the determination of whether tax benefits claimed or expected to be claimed on a tax return should be recorded in the financial statements. Under this guidance, the Company may recognize the tax benefit from an uncertain tax position only if it is more-likely-than-not that the tax position will be sustained on examination by taxing authorities, based on the technical merits of the position. The tax benefits recognized in the financial statements from such a position are measured based on the largest benefit that has a greater than 50 percent likelihood of being realized upon ultimate settlement. The guidance on accounting for uncertainty in income taxes also addresses de-recognition, classification, interest and penalties on income taxes, and accounting in interim periods. The Company recognizes interest and penalties on income taxes as a component of income tax expense. The Company has not accrued any additional income taxes due to uncertain tax positions.

The Company is generally no longer subject to U.S. federal or state and local income tax examinations by tax authorities for years before 2011.

First Bancshares, Inc. and Subsidiaries

Notes to Consolidated Financial Statements

Note 1. Summary of Significant Accounting Policies (Continued)

Revenue recognition: Deposit account transaction fees and other ancillary non-interest income related to the Bank's deposit and lending activities are recognized as services are performed.

Stock-based compensation: The Company records any stock-based employee compensation cost using the fair value method. No stock options have been granted since 2007.

Comprehensive income: Comprehensive income consists of net income and other comprehensive income. For the Company, other comprehensive income consists entirely of unrealized gains (losses) on securities available for sale, net of deferred taxes and realized gains and losses in sales of securities.

Subsequent events: The Company has evaluated all subsequent events through March 5, 2015, the date that the financial statements were available to be issued.

Note 2. Securities

The amortized cost and estimated fair value of securities available for sale are as follows:

	Amortized Cost	Gross Unrealized		Fair Value
		Gains	(Losses)	
December 31, 2014:				
United States Government and federal agency obligations	\$ 9,981,226	\$ 1,318	\$ (144,135)	\$ 9,838,409
Municipal securities	365,277	-	(2,280)	362,997
Federal agency residential mortgage-backed securities	10,665,504	108,206	(9,553)	10,764,157
Federal agency collateralized mortgage obligations	42,703,604	33,153	(1,335,661)	41,401,096
Common and preferred stocks	218,000	-	-	218,000
	<u>\$ 63,933,611</u>	<u>\$ 142,677</u>	<u>\$ (1,491,629)</u>	<u>\$ 62,584,659</u>
June 30, 2014:				
United States Government and federal agency obligations	\$ 7,010,931	\$ -	\$ (207,961)	\$ 6,802,970
Municipal securities	8,880	-	(5,756)	3,124
Federal agency residential mortgage-backed securities	8,560,271	66,711	-	8,626,982
Federal agency collateralized mortgage obligations	48,596,625	10,709	(1,796,895)	46,810,439
Common and preferred stocks	218,000	-	-	218,000
	<u>\$ 64,394,707</u>	<u>\$ 77,420</u>	<u>\$ (2,010,612)</u>	<u>\$ 62,461,515</u>

First Bancshares, Inc. and Subsidiaries

Notes to Consolidated Financial Statements

Note 2. Securities (Continued)

The amortized cost and estimated market value of securities at December 31, 2014 by contractual maturity are shown below. Expected maturities will differ from contractual maturities because borrowers may have the right to call or prepay obligations with or without call or prepayment penalties. Securities not due at a single maturity date, such as residential mortgage-backed securities and collateralized mortgage obligations, are shown separately.

	Available for Sale	
	Amortized Cost	Fair Value
Due after one year through five years	\$ 2,071,620	\$ 2,071,510
Due after five years through ten years	8,010,003	7,866,990
Due after ten years	264,880	262,906
Subtotal	10,346,503	10,201,406
Federal agency residential mortgage-backed securities and collateralized mortgage obligations	53,369,108	52,165,253
Common and preferred stocks	218,000	218,000
Total	<u>\$ 63,933,611</u>	<u>\$ 62,584,659</u>

During the six-month period ended December 31, 2014, gross realized gain or loss on the sale of securities was \$(6,650).

The carrying value of securities pledged on repurchase agreements at December 31, 2014 and June 30, 2014, was \$4,911,960 and \$4,883,180, respectively.

The following tables present the fair value and gross unrealized losses of the Company's securities with unrealized losses aggregated by category and length of time that individual securities have been in a continuous unrealized loss position, at December 31, 2014, and June 30, 2014.

	Available for Sale as of December 31, 2014					
	Less than 12 Months		12 Months or More		Total	
	Fair Value	Gross Unrealized (Losses)	Fair Value	Gross Unrealized (Losses)	Fair Value	Gross Unrealized (Losses)
United States government and federal agency obligations	\$ 2,020,520	\$ (2,871)	\$ 6,868,740	\$ (141,264)	\$ 8,889,260	\$ (144,135)
Municipal securities	362,997	(2,280)	-	-	362,997	(2,280)
Federal agency residential mortgage backed securities	4,753,172	(9,553)	-	-	4,753,172	(9,553)
Federal agency collateralized mortgage obligations	-	-	34,756,446	(1,335,661)	34,756,446	(1,335,661)
Total temporarily impaired securities	<u>\$ 7,136,689</u>	<u>\$ (14,704)</u>	<u>\$ 41,625,186</u>	<u>\$ (1,476,925)</u>	<u>\$ 48,761,875</u>	<u>\$ (1,491,629)</u>

First Bancshares, Inc. and Subsidiaries

Notes to Consolidated Financial Statements

Note 2. Securities (Continued)

	Available for Sale as of June 30, 2014					
	Less than 12 Months		12 Months or More		Total	
	Fair Value	Gross Unrealized (Losses)	Fair Value	Gross Unrealized (Losses)	Fair Value	Gross Unrealized (Losses)
United States government and federal agency obligations	\$ -	\$ -	\$ 6,802,970	\$ (207,961)	\$ 6,802,970	\$ (207,961)
Municipal securities	-	-	3,124	(5,756)	3,124	(5,756)
Federal agency residential mortgage backed securities						
Federal agency collateralized mortgage obligations	779,529	(8,237)	43,212,101	(1,788,567)	43,991,631	(1,796,895)
Total temporarily impaired securities	\$ 779,529	\$ (8,237)	\$ 50,018,195	\$ (2,002,284)	\$ 50,797,725	\$ (2,010,612)

As of December 31, 2014, the investment portfolio included 75 securities. Of this number, 47 securities have current unrealized losses, 40 of which have existed for longer than one year. All of the debt securities with unrealized losses are considered to be acceptable credit risks. Based upon an evaluation of the available evidence, including recent changes in market rates and credit rating information, management believes the decline in fair values for these debt securities are temporary. In addition, the Company does not have the intent to sell these debt securities prior to their anticipated recovery and will more than likely not be required to sell these securities prior to maturity.

The Company did not recognize any other-than-temporary impairment on securities available for sale during the six-month period ended December 31, 2014.

Note 3. Loans Receivable

At December 31, 2014 and June 30, 2014, loans consisted of the following:

Type of Loan	December 31, 2014	June 30, 2014
Real estate:		
Residential	\$ 56,830,266	\$ 55,286,913
Commercial	45,464,299	42,248,282
Land	2,916,228	2,928,931
Commercial	9,910,163	8,535,785
Consumer	2,322,228	2,339,865
Total loans	117,443,184	111,339,776
Add: Unamortized deferred loan costs, net of origination fees	183,388	181,230
Less: Allowance for loan losses	(1,623,965)	(1,586,705)
Total loans receivable, net	\$ 116,002,607	\$ 109,934,301

First Bancshares, Inc. and Subsidiaries

Notes to Consolidated Financial Statements

Note 3. Loans Receivable (Continued)

The aging of the loan portfolio, by classes of loans, as of December 31, 2014 and June 30, 2014, are summarized below:

Type of Loan	Accruing Loans		Non-Accrual Loans	Current Loans	Total Loans
	30–89 Days Past Due	90+ Days Past Due			
December 31, 2014:					
Real estate:					
Residential	\$ 162,353	\$ -	\$ 399,204	\$ 56,268,709	\$ 56,830,266
Commercial	-	1,339	221,659	45,241,301	45,464,299
Land	-	-	-	2,916,228	2,916,228
Commercial	-	-	-	9,910,163	9,910,163
Consumer	-	-	-	2,322,228	2,322,228
Total loans	<u>\$ 162,353</u>	<u>\$ 1,339</u>	<u>\$ 620,863</u>	<u>\$ 116,658,629</u>	<u>\$ 117,443,184</u>

Type of Loan	Accruing Loans		Non-Accrual Loans	Current Loans	Total Loans
	30–89 Days Past Due	90+ Days Past Due			
June 30, 2014:					
Real estate:					
Residential	\$ 190,812	\$ -	\$ 412,107	\$ 54,683,994	\$ 55,286,913
Commercial	-	-	235,904	42,012,378	42,248,282
Land	-	-	-	2,928,931	2,928,931
Commercial	-	-	-	8,535,785	8,535,785
Consumer	-	-	-	2,339,865	2,339,865
Total loans	<u>\$ 190,812</u>	<u>\$ -</u>	<u>\$ 648,011</u>	<u>\$ 110,500,953</u>	<u>\$ 111,339,776</u>

Nonperforming loans, by classes of loans, as of December 31, 2014 and June 30, 2014, are summarized as follows:

Type of Loan	Accruing Past Due 90 Days Or More	Nonaccrual Loans*	Troubled Debt Restructurings—Accruing	Total Nonperforming Loans	Percentage of Total Nonperforming Loans
	December 31, 2014:				
Real estate:					
Residential	\$ -	\$ 399,204	\$ 180,930	\$ 580,134	46.49%
Commercial	1,339	221,659	444,765	667,763	53.51%
	<u>\$ 1,339</u>	<u>\$ 620,863</u>	<u>\$ 625,695</u>	<u>\$ 1,247,897</u>	<u>100.00%</u>

*Nonaccrual loans as of December 31, 2014 include \$221,659 of troubled debt restructurings, all of which are included in commercial.

First Bancshares, Inc. and Subsidiaries

Notes to Consolidated Financial Statements

Note 3. Loans Receivable (Continued)

	Accruing Past Due 90 Days Or More	Nonaccrual Loans*	Troubled Debt Restructurings— Accruing	Total Nonperforming Loans	Percentage of Total Nonperforming Loans
June 30, 2014:					
Real estate:					
Residential	\$ -	\$ 412,107	\$ 186,343	\$ 598,450	46.61%
Commercial	-	235,904	449,716	685,620	53.39%
	<u>\$ -</u>	<u>\$ 648,011</u>	<u>\$ 636,059</u>	<u>\$ 1,284,070</u>	<u>100.00%</u>

*Nonaccrual loans as of June 30, 2014 include \$235,904 of troubled debt restructurings, all of which are included in commercial.

The following tables detail activity in the allowance for loan losses by class of loan for the six-month period ended December 31, 2014, and the year ended June 30, 2014.

	Real Estate Residential	Real Estate Commercial	Land	Commercial	Consumer	Total
December 31, 2014:						
Balance, beginning	\$ 357,400	\$ 776,970	\$ 26,277	\$ 410,105	\$ 15,953	\$ 1,586,705
Provision charged to expense	28,000	-	-	-	-	28,000
Recoveries	24,691	5,604	-	1,836	450	32,581
	<u>410,091</u>	<u>782,574</u>	<u>26,277</u>	<u>411,941</u>	<u>16,403</u>	<u>1,647,286</u>
Loans charged off	(15,311)	-	-	-	(8,010)	(23,321)
Balance, ending	<u>\$ 394,780</u>	<u>\$ 782,574</u>	<u>\$ 26,277</u>	<u>\$ 411,941</u>	<u>\$ 8,393</u>	<u>\$ 1,623,965</u>

	Real Estate Residential	Real Estate Commercial	Land	Commercial	Consumer	Total
June 30, 2014:						
Balance, beginning	\$ 393,498	\$ 776,970	\$ 26,277	\$ 394,106	\$ 11,602	\$ 1,602,453
Provision charged to expense	-	-	-	-	-	-
Recoveries	10,979	-	-	15,999	4,351	31,329
	<u>404,477</u>	<u>776,970</u>	<u>26,277</u>	<u>410,105</u>	<u>15,953</u>	<u>1,633,782</u>
Loans charged off	(47,077)	-	-	-	-	(47,077)
Balance, ending	<u>\$ 357,400</u>	<u>\$ 776,970</u>	<u>\$ 26,277</u>	<u>\$ 410,105</u>	<u>\$ 15,953</u>	<u>\$ 1,586,705</u>

First Bancshares, Inc. and Subsidiaries

Notes to Consolidated Financial Statements

Note 3. Loans Receivable (Continued)

The allowance for loan losses by impairment evaluation and by portfolio class, as of December 31, 2014 and June 30, 2014, are summarized as follows:

	Real Estate Residential	Real Estate Commercial	Land	Commercial	Consumer	Total
December 31, 2014:						
Allowance for loans individually evaluated for impairment	\$ 32,872	\$ 72,638	\$ -	\$ 276	\$ -	\$ 105,786
Allowance for loans collectively evaluated for impairment	361,908	709,936	26,277	411,665	8,393	1,518,179
	<u>\$ 394,780</u>	<u>\$ 782,574</u>	<u>\$ 26,277</u>	<u>\$ 411,941</u>	<u>\$ 8,393</u>	<u>\$ 1,623,965</u>
Loans individually evaluated for impairment	\$ 656,644	\$ 1,465,274	\$ 53,928	\$ 276	\$ -	\$ 2,176,122
Loans collectively evaluated for impairment	56,173,622	43,999,025	2,862,300	9,909,887	2,322,228	115,267,062
	<u>\$ 56,830,266</u>	<u>\$ 45,464,299</u>	<u>\$ 2,916,228</u>	<u>\$ 9,910,163</u>	<u>\$ 2,322,228</u>	<u>\$ 117,443,184</u>
June 30, 2014:						
Allowance for loans individually evaluated for impairment	\$ 34,304	\$ 72,638	\$ -	\$ 1,156	\$ -	\$ 108,098
Allowance for loans collectively evaluated for impairment	323,096	704,332	26,277	408,949	15,953	1,478,607
	<u>\$ 357,400</u>	<u>\$ 776,970</u>	<u>\$ 26,277</u>	<u>\$ 410,105</u>	<u>\$ 15,953</u>	<u>\$ 1,586,705</u>
Loans individually evaluated for impairment	\$ 785,655	\$ 1,532,789	\$ 56,001	\$ 1,156	\$ -	\$ 2,375,601
Loans collectively evaluated for impairment	54,501,258	40,715,493	2,872,930	8,534,629	2,339,865	108,964,175
	<u>\$ 55,286,913</u>	<u>\$ 42,248,282</u>	<u>\$ 2,928,931</u>	<u>\$ 8,535,785</u>	<u>\$ 2,339,865</u>	<u>\$ 111,339,776</u>

First Bancshares, Inc. and Subsidiaries

Notes to Consolidated Financial Statements

Note 3. Loans Receivable (Continued)

Loans, by classes of loans, considered to be impaired as of December 31, 2014 and June 30, 2014, are summarized as follows:

	Recorded Investment	Unpaid Principal Balance	Related Allowance	Average Recorded Investment	Interest Income Recognized for Cash Payments Received
December 31, 2014:					
Classes of loans:					
Impaired loans with no specific allowance recorded:					
Real estate:					
Residential	\$ 364,151	\$ 364,151	\$ -	\$ 421,903	\$ 13,309
Commercial	994,597	994,597	-	1,024,974	57,823
Land	53,928	53,928	-	54,965	3,144
	<u>1,412,676</u>	<u>1,412,676</u>	<u>-</u>	<u>1,501,842</u>	<u>74,276</u>
Impaired loans with specific allowance recorded:					
Real estate:					
Residential	292,493	292,493	32,872	299,247	13,403
Commercial	470,677	470,677	72,638	474,058	28,595
Commercial	276	276	276	716	408
	<u>763,446</u>	<u>763,446</u>	<u>105,786</u>	<u>774,021</u>	<u>42,406</u>
Total impaired loans:					
Real Estate:					
Residential	656,644	656,644	32,872	721,150	26,712
Commercial	1,465,274	1,465,274	72,638	1,499,032	86,418
Land	53,928	53,928	-	54,965	3,144
Commercial	276	276	276	716	408
	<u>\$ 2,176,122</u>	<u>\$ 2,176,122</u>	<u>\$ 105,786</u>	<u>\$ 2,275,863</u>	<u>\$ 116,682</u>

First Bancshares, Inc. and Subsidiaries

Notes to Consolidated Financial Statements

Note 3. Loans Receivable (Continued)

	Recorded Investment	Unpaid Principal Balance	Related Allowance	Average Recorded Investment	Interest Income Recognized for Cash Payments Received
June 30, 2014:					
Classes of loans:					
Impaired loans with no specific allowance recorded:					
Real estate:					
Residential	\$ 479,655	\$ 479,655	\$ -	\$ 262,720	\$ 5,768
Commercial	1,055,351	1,055,351	-	1,001,680	23,039
Land	56,001	56,001	-	58,167	1,856
	<u>1,591,007</u>	<u>1,591,007</u>	<u>-</u>	<u>1,322,567</u>	<u>30,663</u>
Impaired loans with specific allowance recorded:					
Real estate:					
Residential	306,000	306,000	34,304	427,789	6,526
Commercial	477,438	477,438	72,638	469,004	13,872
Commercial	1,156	1,156	1,156	1,930	275
	<u>784,594</u>	<u>784,594</u>	<u>108,098</u>	<u>898,723</u>	<u>20,673</u>
Total impaired loans:					
Real Estate:					
Residential	785,655	785,655	34,304	690,509	12,294
Commercial	1,532,789	1,532,789	72,638	1,470,684	36,911
Land	56,001	56,001	-	58,167	1,856
Consumer	-	-	-	869	-
Commercial	1,156	1,156	1,156	1,930	275
	<u>\$ 2,375,601</u>	<u>\$ 2,375,601</u>	<u>\$ 108,098</u>	<u>\$ 2,222,159</u>	<u>\$ 51,336</u>

Impaired loans, for which no allowance has been provided as of December 31, 2014 and June 30, 2014, have adequate collateral, based on management's current estimates.

First Bancshares, Inc. and Subsidiaries

Notes to Consolidated Financial Statements

Note 3. Loans Receivable (Continued)

The following tables show the outstanding balance of loans by credit quality indicator and loan class as of December 31, 2014, and June 30, 2014:

Type of Loan	Pass (Grades 1-4)	(Grade 5)	Substandard (Grade 6)	Doubtful (Grade 7)	Total
December 31, 2014:					
Real estate:					
Residential	\$ 55,997,544	\$ 176,078	\$ 656,212	\$ 432	\$ 56,830,266
Commercial	43,999,025	-	1,465,274	-	45,464,299
Land	2,862,300	-	53,928	-	2,916,228
Commercial	9,909,887	-	276	-	9,910,163
Consumer	2,322,228	-	-	-	2,322,228
Total gross loans	<u>\$ 115,090,984</u>	<u>\$ 176,078</u>	<u>\$ 2,175,690</u>	<u>\$ 432</u>	<u>\$ 117,443,184</u>

Type of Loan	Pass (Grades 1-4)	(Grade 5)	Substandard (Grade 6)	Doubtful (Grade 7)	Total
June 30, 2014:					
Real estate:					
Residential	\$ 54,322,261	\$ 178,698	\$ 784,089	\$ 1,865	\$ 55,286,913
Commercial	40,715,493	-	1,532,789	-	42,248,282
Land	2,872,930	-	56,001	-	2,928,931
Commercial	8,534,629	-	1,156	-	8,535,785
Consumer	2,339,865	-	-	-	2,339,865
Total gross loans	<u>\$ 108,785,178</u>	<u>\$ 178,698</u>	<u>\$ 2,374,035</u>	<u>\$ 1,865</u>	<u>\$ 111,339,776</u>

The Company's credit quality indicator is internally assigned risk ratings. Each loan is assigned a risk rating upon origination. This risk rating is reviewed on commercial and commercial real estate loans greater than \$250,000 on an annual basis or on an as needed basis depending on circumstances. All other loans are reviewed on an as needed basis depending on the specific circumstances of the loan. See Note 1 for further discussion on the Bank's risk ratings.

As of December 31, 2014 and June 30, 2014, troubled debt restructurings totaled \$847,354 and \$871,963, respectively.

There were no loans restructured during the six-month period ended December 31, 2014.

First Bancshares, Inc. and Subsidiaries

Notes to Consolidated Financial Statements

Note 4. Premises and Equipment

Premises and equipment at December 31, 2014 and June 30, 2014 consists of the following:

	December 31, 2014	June 30, 2014
Land	\$ 2,117,166	\$ 624,794
Buildings	5,832,742	5,832,742
Office furniture, fixtures and equipment	2,886,568	2,932,227
Automobiles	184,696	159,916
	<u>11,021,172</u>	<u>9,549,679</u>
Less accumulated depreciation	5,622,756	5,510,970
Construction in progress	149,036	94,257
Property and equipment, net	<u>\$ 5,547,452</u>	<u>\$ 4,132,966</u>

As of December 31, 2014, there are no significant remaining commitments on construction in progress.

The Bank's full-service branch office in Springfield, Missouri is leased. The lease on the branch was assumed and it has less than five years remaining on the initial term.

Rent expense for the six-month period ended December 31, 2014 was \$50,108.

Minimum future lease payments for the Springfield branch office for the period ended December 31, 2014, are as follows:

2015	\$ 100,217
2016	16,703
Total	<u>\$ 116,920</u>

First Bancshares, Inc. and Subsidiaries

Notes to Consolidated Financial Statements

Note 5. Deposits

A summary of deposit accounts at December 31, 2014 and June 30, 2014, is as follows:

	December 31, 2014	June 30, 2014
Non-interest-bearing checking	\$ 13,163,924	\$ 12,596,845
Interest-bearing checking	40,146,896	39,794,167
Super saver money market	12,677,865	13,077,883
Savings	9,996,620	8,745,122
Money market savings accounts	31,846,511	31,480,770
Certificates of deposit	60,914,244	60,691,272
Total	<u>\$ 168,746,060</u>	<u>\$ 166,386,059</u>

The aggregate amount of certificates of deposit, each with a minimum denomination of \$100,000, was \$32,934,251 and \$32,169,856 at December 31, 2014 and June 30, 2014, respectively.

The aggregate amount of deposits, each with a balance greater than the FDIC insurance coverage of \$250,000, was \$29,966,046 and \$26,077,956 at December 31, 2014 and June 30, 2014, respectively.

At December 31, 2014, scheduled maturities of certificates of deposit are as follows:

2015	\$ 34,966,610
2016	12,704,350
2017	5,966,617
2018	4,333,040
2019	2,943,627
	<u>\$ 60,914,244</u>

Note 6. Repurchase Agreements

The Bank offers repurchase agreements as an additional product offering to its customers. Repurchase agreements allow customers to have excess checking account balances “swept” from the checking accounts into a non-insured interest bearing account. The customers’ investment in these non-insured accounts is collateralized by securities of the Bank pledged at FHLB for that purpose. The agreements mature daily and carry a weighted-average interest rate of 0.30 percent at December 31, 2014 and June 30, 2014.

Note 7. Advances from Federal Home Loan Bank and Other Borrowed Money

Advances are obtained from the FHLB of Des Moines. The advances are secured by FHLB stock and a blanket pledge of qualifying one-to-four family mortgage loans. Advances from the FHLB at December 31, 2014 and June 30, 2014, are \$11,500,000 and \$10,500,000, respectively. The advances bear interest rates ranging from 0.43 percent to 1.39 percent and mature February 2015 to October 2018. The weighted average interest rate was 0.53 percent and 0.72 percent as of December 31, 2014 and June 30, 2014, respectively.

First Bancshares, Inc. and Subsidiaries

Notes to Consolidated Financial Statements

Note 7. Advances from Federal Home Loan Bank and Other Borrowed Money (Continued)

As of December 31, 2014, the fixed-rate term advances shown above are subject to a prepayment fee equal to 100 percent of the present value of the monthly lost cash flow to the FHLB based upon the difference between the contract rate on the advance and the rate on an alternative qualifying investment of the same remaining maturity. Advances may be prepaid without a prepayment fee if the rate on an advance being prepaid is equal to or below the current rate for an alternative qualifying investment of the same remaining maturity.

Maturities of FHLB advances are as follows:

Year Ended December 31	Aggregate Annual Maturities
2015	\$ 3,000,000
2016	3,000,000
2017	1,500,000
2018	1,500,000
Revolving loan	2,500,000
	\$ 11,500,000

At December 31, 2014, the Bank had irrevocable letters of credit issued on its behalf from the FHLB totaling \$1,385,000 as collateral for public entity deposits in excess of federal insurance limits. The letters of credit expire through February 2016. At December 31, 2014, the Bank had collateralized borrowing capacity with the FHLB of approximately \$21.3 million.

Note 8. Income Taxes

There was no provision for income taxes for the six-month period ended December 31, 2014.

The provision for income taxes (benefit) differs from that computed at the statutory corporate rate (34 percent), for the six months ended December 31, 2014 as follows:

	December 31, 2014	June 30, 2014
Tax at statutory rate	\$ 48,417	\$ 202,185
Increase (decrease) in taxes resulting from:		
State taxes, net of federal benefit	4,110	19,374
Tax-exempt income	(432)	(72)
Bank-owned life insurance	(17,683)	(34,423)
Dividends received deduction	-	(1,959)
Change in valuation allowance	(51,127)	(161,697)
Other, net	16,715	(23,408)
Provision for income taxes	\$ -	\$ -

The change in valuation allowance does not reflect that portion of the change related to the net unrealized loss on available-for-sale securities of \$458,644 for the six-month period ended December 31, 2014.

First Bancshares, Inc. and Subsidiaries

Notes to Consolidated Financial Statements

Note 8. Income Taxes (Continued)

The components of deferred tax assets and liabilities as of December 31, 2014 and June 30, 2014, consisted of:

	December 31, 2014	June 30, 2014
Deferred tax assets:		
Allowance for loan losses	\$ 620,789	\$ 587,081
Missouri low income housing and other credits	165,291	171,533
Net unrealized loss on available-for-sale securities	458,644	657,285
Real estate owned	151,709	146,003
Compensated employee absences	-	16,180
State net operating loss carry-forwards	185,687	186,694
Federal net operating loss carry-forwards	2,725,278	2,759,680
Charitable contributions	16,231	14,354
Total gross deferred tax assets	4,323,629	4,538,810
Valuation allowance	(4,044,632)	(4,294,400)
	278,997	244,410
Deferred tax liabilities:		
Premises and equipment	(77,305)	(90,679)
FHLB stock dividends	(63,318)	(60,936)
Prepaid expenses	(67,869)	(25,740)
Unamortized deferred loan costs, net of fees	(70,505)	(67,055)
Total gross deferred tax liabilities	(278,997)	(244,410)
Total net deferred tax liabilities	\$ -	\$ -

In accordance with FASB ASC Topics 740-10 and 740-30, a deferred tax liability has not been recognized for tax basis bad debt reserves of \$2.2 million of the former Savings Bank that arose in tax years that began prior to December 31, 1987. At December 31, 2014, the amount of the deferred tax liability that had not been recognized was approximately \$811,000. This deferred tax liability could be recognized if, in the future, there is a change in federal tax law, the former Savings Bank fails to meet the definition of a "qualified savings institution," as defined by the Internal Revenue Code, certain distributions are made with respect to the stock of the former Savings Bank, or the bad debt reserves are used for any purpose other than absorbing bad debts.

During the six months ended December 31, 2014, the Company recorded a valuation allowance of \$4.0 million. As of December 31, 2014, management has provided a full valuation allowance for net deferred tax assets resulting from the Company's cumulative net losses during the past several years. Realization of deferred tax assets is dependent upon sufficient future taxable income during the period that deductible temporary differences and carry forwards are expected to be available to reduce taxable income.

At December 31, 2014, the Company had net operating loss carry forwards of approximately \$8.0 million which are available to offset future taxable income and expire in varying amounts through 2034.

First Bancshares, Inc. and Subsidiaries

Notes to Consolidated Financial Statements

Note 9. Employee Benefit Plans

The Bank had participated in a multiple-employer defined benefit pension plan covering substantially all employees. In fiscal 2006, the Bank opted to freeze the plan. Participants in the plan became entitled to their vested benefits at the date it was frozen. The Bank limited its future obligations to the funding amount required by the annual actuarial evaluation of the plan and administrative costs. No participants will be added to the plan. Pension expense for the six-month period ended December 31, 2014 was approximately \$6,000. This plan is not subject to the requirements of FASB ASC Topics 715 and 958.

The First Home Bank Employee Stock Ownership and 401(k) Plan covers all employees that are age 21 and have completed six months of service. The Company makes contributions on a matching basis 100 percent on the first 3 percent of employee deferrals and 50 percent on the next 2 percent of employee deferrals. Expense for the ESOP and 401(k) plan for the six-month period ended December 31, 2014 was \$24,084.

Compensation expense for stock-based awards is recorded over the vesting period at the fair values of the award at the time of the grant. The recording of such compensation began on July 1, 2006 for shares not yet vested as of that date and for all new grants subsequent to that date. The exercise price of options granted under the Company's incentive plans is equal to the fair market value of the underlying stock at the grant date. The Company assumes no projected forfeiture rates on its stock-based compensation.

The Company's 2004 Stock Option and Incentive Plan has authorized the grant of options to certain officers, employees and directors for up to 100,000 shares of the Company's common stock. All options granted have 10 year terms and vest and become exercisable ratably over five years following the date of grant. The plan was approved by shareholders in October 2004. At December 31, 2014, there were 78,000 shares of stock available for grant under the plan.

The Company's 2004 Management Recognition Plan has authorized the award of shares to certain officers, employees and directors for up to 50,000 shares of the Company's common stock. All shares awarded will have a restricted period to be determined by the Corporation's Compensation Committee. The restricted period shall not be less than three years if the award is time based, or not less than one year if performance based. The plan was approved by shareholders in October 2004. No shares have been issued from this plan.

No options were granted during the six-month period ended December 31, 2014. The last options were granted in fiscal 2007.

First Bancshares, Inc. and Subsidiaries

Notes to Consolidated Financial Statements

Note 9. Employee Benefit Plans (Continued)

A summary of the Company's stock option activity, and related information for the years ended June 30 follows:

	December 31, 2014		June 30, 2014	
	Options	Weighted Average Exercise Price	Options	Weighted Average Exercise Price
Outstanding at beginning of year	7,000	\$ 17.14	17,000	\$ 16.93
Granted	-	-	-	-
Exercised	-	-	-	-
Forfeited	-	-	(10,000)	16.78
Outstanding at end of year	<u>7,000</u>	-	<u>7,000</u>	17.14
Exercisable at end of year	<u>7,000</u>	\$ 17.14	<u>7,000</u>	\$ 17.14

The following table summarizes information about stock options at December 31, 2014:

Exercise Price	Number Outstanding at December 31, 2014	Number Exercisable at December 31, 2014	Remaining Contractual Life (Months)
\$ 18	2,000	2,000	14
17	5,000	5,000	27

As of December 31, 2014, there was no unrecognized compensation cost related to non-vested share-based compensation agreements granted under the plan. There is no intrinsic value of vested options on Company stock as of December 31, 2014.

Note 10. Related Party Transactions

Certain employees, officers and directors are engaged in transactions with the Bank in the ordinary course of business. It is the Bank's policy that all related party transactions are conducted at "arm's length" and all loans and commitments included in such transactions are made on substantially the same terms, including interest rates and collateral, as those prevailing at the time for comparable transactions with other customers.

Loans to officers and directors as of December 31, 2014 and June 30, 2014, were \$9,669,942 and \$9,592,572, respectively.

First Bancshares, Inc. and Subsidiaries

Notes to Consolidated Financial Statements

Note 11. Commitments and Contingencies

In the ordinary course of business, the Bank has various outstanding commitments that are not reflected in the accompanying consolidated financial statements. The principal commitments of the Bank are as follows:

Letters of credit—Outstanding standby letters of credit were approximately \$29,000 and \$8,000 at December 31, 2014 and June 30, 2014, respectively.

Loan commitments—The Bank had outstanding firm commitments to originate loans of approximately \$3,880,000 and \$3,313,000 at December 31, 2014 and June 30, 2014, respectively.

Lines of credit—The unused portion of lines of credit was approximately \$5,532,000 and \$5,054,000 at December 31, 2014 and June 30, 2014, respectively.

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. Commitments generally have fixed expiration dates or other termination clauses and may require payment of a fee. Since many of the commitments are expected to expire without being drawn upon, the total commitment amounts do not necessarily represent future cash requirements. The Company evaluates each customer's creditworthiness on a case-by-case basis. The amount of collateral obtained, if deemed necessary by the Company upon extension of credit, is based on management's credit evaluation of the party. Collateral held varies, but may include accounts receivable, crops, livestock, inventory, property and equipment, residential and commercial real estate as well as income-producing commercial properties.

Standby letters of credit are conditional commitments issued by the Company to guarantee the performance of a customer to a third party. Those guarantees are primarily issued to support public and private borrowing arrangements, including commercial paper, bond financing and similar transactions.

None of the guarantees extend longer than one year. The credit risk involved in issuing letters of credit is essentially the same as that involved in extending loan facilities to customers. Collateral held varies as specified above and is required in instances which the Company deems necessary. All of the standby letters of credit outstanding at December 31, 2014 were collateralized. No amounts were recorded as liabilities for the six-month period ended December 31, 2014, or the year ended June 30, 2014, for the Company's potential obligations under these guarantees.

In the normal course of business, the Company is involved in various legal proceedings. In the opinion of management, any liability resulting from such proceedings would not have a material adverse effect on the Company's consolidated financial statements.

Note 12. Regulatory Matters

The Bank is subject to various regulatory capital requirements administered by its primary federal regulator, the FDIC. Failure to meet the minimum regulatory capital requirements can initiate certain mandatory and possible additional discretionary, actions by regulators that if undertaken, could have a direct material effect on the Bank and the consolidated financial statements. Under the regulatory capital adequacy guidelines and the regulatory framework for prompt corrective action, the Bank must meet specific capital guidelines involving quantitative measures of the Bank's assets, liabilities, and certain off-balance-sheet items as calculated under regulatory accounting practices. The Bank's capital amounts and classification under the prompt corrective action guidelines are also subject to qualitative judgments by the regulators about components, risk weightings, and other factors.

First Bancshares, Inc. and Subsidiaries

Notes to Consolidated Financial Statements

Note 12. Regulatory Matters (Continued)

Quantitative measures established by regulation to ensure capital adequacy require the Bank to maintain minimum amounts and ratios (set forth in the table below) of total risk-based capital and Tier 1 capital to risk-weighted assets (as defined in the regulations), Tier 1 capital to adjusted total assets (as defined), and tangible capital to adjusted total assets (as defined).

Management believes, as of December 31, 2014, that the Bank meets all capital adequacy requirements to which it is subject and was well capitalized.

The Bank's actual capital amounts and ratios are also presented in the table.

	Actual		Minimum for Capital Adequacy Purposes		Minimum to Be Well-Capitalized Under Prompt Corrective Action Provisions	
	Amount	Ratio	Amount	Ratio	Amount	Ratio
As of December 31, 2014:						
Total-risk-based capital (to risk-weighted assets)	\$ 17,702	15.89%	\$ 8,910	8.00%	\$ 11,138	10.00%
Core capital (to adjusted tangible assets)	16,307	8.23%	7,921	4.00%	9,901	5.00%
Tangible capital (to adjusted tangible assets)	16,307	8.23%	2,970	1.50%	N/A	0.00%
Tier 1 capital (to risk-weighted assets)	16,307	14.64%	4,455	4.00%	6,683	6.00%
As of June 30, 2014:						
Total-risk-based capital (to risk-weighted assets)	\$ 17,408	16.72%	\$ 8,327	8.00%	\$ 10,409	10.00%
Core capital (to adjusted tangible assets)	16,103	8.18%	7,877	4.00%	9,846	5.00%
Tangible capital (to adjusted tangible assets)	16,103	8.18%	2,954	1.50%	N/A	0.00%
Tier 1 capital (to risk-weighted assets)	16,103	15.47%	4,164	4.00%	6,245	6.00%

In July 2013, the federal banking agencies issued a final rule revising the regulatory capital rules applicable to most national banks and federal savings associations as well as their holding companies generally beginning on January 1, 2015. The rule implements the Basel Committee's December 2010 framework known as "Basel III" for strengthening international capital standards as well as certain provisions of the Dodd-Frank Act. The final rule implements a revised definition of regulatory capital, a new common equity Tier 1 minimum capital requirement of 4.50 percent, and a higher Tier 1 capital requirement of 6.00 percent (which is an increase from 4.00 percent). Under the final rule, the total capital ratio remains at 8.00 percent and the minimum leverage ratio (Tier 1 capital to total assets) for all banking organizations, regardless of supervisory rating is 4.00 percent.

Additionally, under the final rule, in order to avoid limitations on capital distributions, including dividend payments and certain discretionary bonus payments to executive officers, a banking organization must hold a capital conservation buffer composed of common equity Tier 1 capital above its minimum risk-based capital requirements. The buffer is measured relative to risk-weighted assets. The final rule also enhances risk sensitivity and addresses weaknesses identified by the regulators over recent years with the measure of risk-weighted assets, including through new measures of creditworthiness to replace references to credit ratings, consistent with the requirements of the Dodd-Frank Act.

First Bancshares, Inc. and Subsidiaries

Notes to Consolidated Financial Statements

Note 12. Regulatory Matters (Continued)

Except for the largest internationally active banking organizations (which are subject to the “advanced approaches” provisions of the final rule), the new minimum capital requirements generally become effective for all banking organizations on January 1, 2015, whereas the capital conservation buffer and the deductions from common equity Tier 1 capital phase in over time, beginning on January 1, 2016. Similarly, nonqualifying capital instruments phase out over time.

Note 13. Fair Value Measurements

Accounting guidance on fair value measurements defines fair value, establishes a framework for measuring fair value using a hierarchy system and requires disclosure of fair value measurements. The hierarchy is intended to maximize the use of observable inputs and minimize the use of unobservable inputs and includes three levels based on upon the valuation techniques used. The three levels are as follows:

- Level 1: Quoted prices (unadjusted) for identical assets or liabilities in active markets that the entity has the ability to access as of the measurement date.
- Level 2: Significant observable inputs other than the 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.

A description of the valuation methodologies used for assets measured at fair value, as well as the general classification of such instruments pursuant to the valuation hierarchy, is set forth below.

Assets recorded at fair value on a recurring basis: A description of the valuation methodologies used for assets measured at fair value on a recurring basis, as well as the general classification of such instruments pursuant to the valuation hierarchy, is set forth below.

Securities available for sale: Where quoted prices are available in an active market, securities are classified within level 1 of the valuation hierarchy. Level 1 securities would include highly liquid government bonds and exchange traded equities. If quoted market prices are not available, then fair values are estimated by using pricing models, quoted prices of securities with similar characteristics, or discounted cash flows. Level 2 securities would include U.S. agency securities, mortgage-backed agency securities, obligations of states and political subdivisions and certain corporate, asset backed and other securities. In certain cases where there is limited activity of less transparency around the input to the valuation, securities are classified within Level 3 of the valuation hierarchy.

First Bancshares, Inc. and Subsidiaries

Notes to Consolidated Financial Statements

Note 13. Fair Value Measurements (Continued)

The following tables summarize financial assets measured at fair value on a recurring basis as of December 31, 2014 and June 30, 2014, segregated by the level of the valuation inputs within the fair value hierarchy utilized to measure fair value:

December 31, 2014	Level 1 Inputs	Level 2 Inputs	Level 3 Inputs	Total Fair Value
Securities available-for-sale:				
United States Government and federal agency obligations	\$ -	\$ 9,838,409	\$ -	\$ 9,838,409
Municipal securities	-	362,997	-	362,997
Federal agency residential mortgage-backed securities	-	10,764,157	-	10,764,157
Federal agency collateralized mortgage obligations	-	41,401,096	-	41,401,096
Common and preferred stocks	-	-	218,000	218,000
Total	\$ -	\$ 62,366,659	\$ 218,000	\$ 62,584,659

June 30, 2014	Level 1 Inputs	Level 2 Inputs	Level 3 Inputs	Total Fair Value
Securities available-for-sale:				
United States Government and federal agency obligations	\$ -	\$ 6,802,970	\$ -	\$ 6,802,970
Municipal securities	-	3,124	-	3,124
Federal agency residential mortgage-backed securities	-	8,626,982	-	8,626,982
Federal agency collateralized mortgage obligations	-	46,810,439	-	46,810,439
Common and preferred stocks	-	-	218,000	218,000
Total	\$ -	\$ 62,243,515	\$ 218,000	\$ 62,461,515

Assets recorded at fair value on a nonrecurring basis: A description of the valuation methodologies used for assets measured at fair value on a nonrecurring basis, as well as the general classification of such instruments pursuant to the valuation hierarchy, is set forth below.

First Bancshares, Inc. and Subsidiaries

Notes to Consolidated Financial Statements

Note 13. Fair Value Measurements (Continued)

Impaired loans: The Company does not record loans at fair value on a recurring basis. From time to time, a loan is considered impaired and an allowance for loan losses is established. Once a loan has been identified as impaired, management measures impairment based upon the value of the underlying collateral. Collateral may be real estate and/or business assets including equipment, inventory and/or accounts receivable. Loan impairment is measured based upon the present value of expected future cash flows discounts at the loan's effective interest rate, except where more practical, at the observable market price of the loan based upon appraisals by qualified licensed appraisers hired by the Company, and are, generally, considered Level 2 measurements. In some cases, adjustments are made to the appraised values due to various factors including age of the appraisal, age of comparables included in the appraisal, and known changes in the market and in the collateral. When significant adjustments are based on unobservable inputs, the resulting fair market measurement is categorized as a Level 3 measurement.

Real estate owned: Real estate owned is carried at the estimated fair value of the property, less disposal costs. The fair value of the property is determined based upon appraisals. As with impaired loans, if significant adjustments are made to the appraised value, based upon unobservable inputs, the resulting fair value measurement is categorized as a Level 3 measurement.

The following tables summarize financial assets measured at fair value on a non-recurring basis as of December 31, 2014, and June 30, 2013, segregated by the level of the valuation inputs within the fair value hierarchy utilized to measure fair value:

December 31, 2014	Level 1 Inputs	Level 2 Inputs	Level 3 Inputs	Total Fair Value
Impaired loans	\$ -	\$ -	\$ 763,879	\$ 763,879
Total	\$ -	\$ -	\$ 763,879	\$ 763,879

June 30, 2014	Level 1 Inputs	Level 2 Inputs	Level 3 Inputs	Total Fair Value
Impaired loans	\$ -	\$ -	\$ 784,594	\$ 784,594
Real estate owned	-	-	88,142	88,142
Total	\$ -	\$ -	\$ 872,736	\$ 872,736

There have been no changes in valuation techniques used for any assets or liabilities measured at fair value during the six-month period ended December 31, 2014.

There were no transfers of assets or liabilities between Levels 1, 2 and 3 of the fair value hierarchy during the six-month period ended December 31, 2014.

Accounting guidance and fair value measurements require disclosure of fair value information about financial instruments, whether or not recognized in the balance sheet for which it is practicable to estimate that fair value. Certain financial instruments and all nonfinancial instruments are excluded from these disclosure requirements.

Cash and interest-bearing deposits at other financial institutions – For these short-term instruments, the carrying amount approximates fair value.

First Bancshares, Inc. and Subsidiaries

Notes to Consolidated Financial Statements

Note 13. Fair Value Measurements (Continued)

Loans receivable—For variable rate loans that reprice in accordance with indices, carrying amounts reported approximate those loans' fair values. The fair values for fixed rate loans were estimated using discounted cash flow analysis that applies interest rates currently offered for loans with similar terms.

Investment in FHLB stock—Fair value of the Bank's investment in FHLB stock approximates the carrying value as no ready market exists for this investment and the stock could only be sold back to the FHLB at par.

Accrued interest—The carrying amounts of accrued interest approximate their fair value.

Deposits—The fair value of demand deposits, savings accounts and interest-bearing demand deposits is the amount payable on demand at the reporting date (i.e., their carrying amount). The fair value of fixed-maturity time deposits is estimated using a discounted cash flow calculation that applies the market rates currently offered for deposits of similar remaining maturities.

Retail repurchase agreements—The carrying amount of retail repurchase agreements approximates fair value.

FHLB advances—The fair value of the Bank's advances are estimated using discounted cash flows, based on the Bank's current incremental borrowing rates for similar types of borrowing arrangements.

Commitments to extend credit, letters of credit and lines of credit—The fair value of commitments is estimated using the fees currently charged to enter into similar agreements, taking into account the remaining terms of the agreements and the present credit worthiness of the counterparties. For fixed-rate loan commitments, fair value also considers the difference between current levels of interest rates and the committed rates. The fair value of letters of credit and lines of credit is based on fees currently charged for similar agreements or on the estimated cost to terminate or otherwise settle the obligations with the counterparties at the reporting date and are insignificant.

First Bancshares, Inc. and Subsidiaries

Notes to Consolidated Financial Statements

Note 13. Fair Value Measurements (Continued)

The following table presents estimated fair values of the Company's financial instruments. The fair values of certain instruments were calculated by discounting expected cash flows. This method involves significant judgments by management and uncertainties. Fair value is the estimated amount at which financial assets or liabilities could be exchanged in a current transaction between willing parties, other than in a forced or liquidation sale. Because no market exists for certain of these financial instruments, and because management does not intend to sell these financial instruments, the fair values shown below may not represent values at which the respective financial instruments could be sold, individually or in the aggregate.

	December 31, 2014		June 30, 2014	
	Carrying Amount	Approximate Fair Value	Carrying Amount	Approximate Fair Value
Financial assets:				
Cash and cash equivalents	\$ 4,239,541	\$ 4,240,000	\$ 11,261,514	\$ 11,262,000
Interest-bearing deposits at other financial institutions	3,182,022	3,182,000	-	-
Available-for-sale securities	62,584,659	62,585,000	62,461,515	62,462,000
Investment in FHLB stock	685,700	686,000	645,700	646,000
Loans, net of allowance for loan losses	116,002,607	116,926,000	109,934,301	111,868,000
Accrued interest receivable	494,658	492,000	450,902	451,000
Financial liabilities:				
Deposits	168,746,060	157,022,000	166,386,059	158,858,000
Retail repurchase agreements	229,009	229,000	224,026	224,000
FHLB advances	11,500,000	11,472,000	10,500,000	10,489,000
Accrued interest payable	83,453	83,000	76,926	77,000

FIRST BANCSHARES, INC. AND SUBSIDIARIES

ADDITIONAL INFORMATION

COMMON STOCK INFORMATION

The common stock of First Bancshares, Inc. is traded on the Over-the-Counter Bulletin Board under the symbol "FBSI". As of March 9, 2015, there were 326 registered stockholders and 1,549,515 shares of common stock outstanding. This does not reflect the number of persons or entities who hold stock in nominee or "street name."

In 2007, the Board of Directors decided to suspend dividend payments until the Company's earnings improved. As a result, there were no dividend payments made during fiscal 2008. In connection with the Company's improved operating results for fiscal 2008, the Board of Directors declared a special dividend of \$0.10 per share on July 31, 2008, which was payable on August 29, 2008 to stockholders of record on August 15, 2008. Subsequently, there have been no dividend payments by the Company, including the year ended June 30, 2014 and six months ended December 31, 2014.

Dividend payments by the Company are dependent on its cash flows, which include reimbursement from its subsidiaries for the income tax savings created by its stand alone operating loss, the operation of real estate owned by the Company and dividends received by the Company from the Bank. Under Federal regulations, the dollar amount of dividends a bank may pay is dependent upon the bank's capital position and recent net income. Generally, if the Bank satisfies its regulatory capital requirements, it may make dividend payments up to the limits prescribed by the FDIC regulations. However, institutions that have converted to stock form of ownership, like First Home Bank, may not declare or pay a dividend on, or repurchase any of, its common stock if the effect thereof would cause the regulatory capital of the institution to be reduced below the amount required for the liquidation account which was established in accordance with federal banking regulations and the Bank's Plan of Conversion. Under Missouri law, the Company is generally prohibited from declaring and paying dividends at a time when the Company's net assets are less than its stated capital or when the payment of dividends would reduce the Company's net assets below its stated capital.

The Company's Board of Directors authorized a stock repurchase plan in November 2013 to repurchase up to \$15,000 of the Company's shares. As of March 9, 2015, 1,300 authorized shares had been repurchased at an average price of \$8.26 per share.

The following table sets forth market price and dividend information for the Company's common stock.

Year Ended

June 30, 2014

	<u>High</u>	<u>Low</u>	<u>Dividend</u>
First Quarter	\$ 8.50	\$ 7.10	N/A
Second Quarter	\$ 8.25	\$ 8.00	N/A
Third Quarter	\$ 8.60	\$ 7.95	N/A
Fourth Quarter	\$ 8.65	\$ 8.00	N/A

Six Months Ended

December 31, 2014

	<u>High</u>	<u>Low</u>	<u>Dividend</u>
First Quarter	\$ 8.51	\$ 7.20	N/A
Second Quarter	\$ 7.90	\$ 6.50	N/A

DIRECTORS AND EXECUTIVE OFFICERS

FIRST BANCSHARES, INC.

DIRECTORS:

R. Bradley Weaver, Chairman and
Chief Executive Officer

Thomas M. Sutherland
One of the owners and operators of Sutherlands
Home Improvement Centers group of stores

D. Mitch Ashlock
Chairman, President and Chief Executive Officer
First Federal Savings and Loan Bank of Olathe

Billy E. Hixon
Retired partner from regional CPA firm of
BKD, LLP

Robert J. Breidenthal
Director
Security Bank of Kansas City

John G. Moody
Attorney at Law
Pointer Law Office

Mark E. Gardner
President
Gardner Capital

Bradley M. Segebarth
Chief Operating Officer
Lebanon Auto Transport

OFFICERS:

R. Bradley Weaver
President and Chief Executive Officer

Jeffrey C. Palmer
Senior Vice President
and Chief Financial Officer

Shannon Peterson
Corporate Secretary

FIRST HOME BANK

DIRECTORS:

R. Bradley Weaver, Chairman and
Chief Executive Officer

Thomas M. Sutherland
One of the owners and operators of Sutherlands
Home Improvement Centers group of stores

D. Mitch Ashlock
Chairman, President and Chief Executive Officer
First Federal Savings and Loan Bank of Olathe

Billy E. Hixon
Retired partner from regional CPA firm of
BKD, LLP

Robert J. Breidenthal
Director
Security Bank of Kansas City

John G. Moody
Attorney at Law
Pointer Law Office

Mark E. Gardner
President
Gardner Capital

Bradley M. Segebarth
Chief Operating Officer
Lebanon Auto Transport

OFFICERS:

R. Bradley Weaver
President and Chief Executive Officer

Joseph E. James
Executive Vice President
and Senior Lending Officer

Jeffrey C. Palmer
Senior Vice President
And Chief Financial Officer

Shannon Peterson
Corporate Secretary

CORPORATE INFORMATION

CORPORATE HEADQUARTERS:

142 East First Street
P.O. Box 777
Mountain Grove, Missouri 65711

INDEPENDENT AUDITORS:

McGladrey LLP
Kansas City, Missouri

GENERAL COUNSEL:

Harold F. Glass
Springfield, Missouri

SPECIAL COUNSEL:

Breyer & Associates PC
McLean, Virginia

TRANSFER AGENT:

Computershare
P.O. Box 43078
Providence, RI 02940
(800) 942-5909

COMMON STOCK:

Traded on the Over-the-Counter Bulletin
OTCQB Symbol: FstBksh: **FBSI**

ANNUAL MEETING

The Annual Meeting of Stockholders will be held Friday, April 17, 2015, at 1:00 p.m., Central Time, at the Hilton Garden Inn located at 4155 S. Nature Center Way, Springfield, Missouri.

First Home Bank
is a wholly owned subsidiary of
First Bancshares, Inc.
With 10 convenient locations to
serve the area residents of
south central Missouri.



First Bancshares, Inc.
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