

March 13, 2020

To the Shareholders:

Your HomeTown Bank Board of Directors is pleased to announce a \$1.35 per share cash dividend. The payout represents another record-breaking earnings performance in 2019 and a great start to 2020.

Last year's growth was a pleasant surprise. New loan growth had a record start but slowed in the third and fourth quarters. Deposits declined the first half of 2019 but finished strong in the third and fourth quarters. The large loan growth in the first two quarters provided strong interest income for the remainder of the year. Net interest margins improved slightly, providing solid net income numbers. The result was a record net income after tax of \$8.671 million compared to \$8.647 million in 2018, and \$6.166 million in 2017.

HomeTown Bank loan officers produced \$101 million in gross loans last year. Although those numbers were short of the record \$125 million in 2018, it was another banner year. The net growth for loans far exceeded budget expectations at \$35.5 million. The net growth in 2018 was \$8 million. Steady growth should continue in 2020 as a large number of unfunded construction loans will continue to progress.

Deposit growth for 2019 was \$21.88 million compared to \$2.5 million in 2018. Competition for deposits remains fierce as interest rates have declined. Our steady net interest margins have allowed us to pay very competitive CD rates but future interest rate cuts by the Federal Reserve will likely create an industry-wide lowering of deposit rates.

Thanks to our record earnings performance, capital grew to a record \$79.06 million compared to \$67.592 million in 2018 and \$62.278 million in 2017. The book value of our common stock is now at \$206 per share after posting earnings per share of \$22.66. As a result, we paid a record cash dividend of \$4.30 per share in 2019 compared to \$4.00 in 2018 and \$3.60 in 2017. All capital ratios exceed regulatory minimums as we continue to achieve the status of a highly capitalized community bank. Loan losses were slightly lower than previous years and remain at a very manageable level. The loan loss reserve is strong at \$4.9 million compared to \$4.6 million in 2018 and \$4.27 million in 2017. The reserve to total loans ratio stands at 1.15% compared to 1.17% in 2018 and 1.11% in 2017.

Last year's surprises included our very strong loan growth, volatile but solid deposit growth, and our steady net interest margins. The financial institutions market in our area is hyper-competitive. We face competition from the megabanks, regional banks, not-for-profit and tax-exempt credit unions, and what we refer to as other non-bank competition. The latter category includes finance companies, insurance companies and mortgage companies, to name a few. Many of our new competitors are internet-only with no physical locations. I find it impossible to try to follow what products each financial entity is offering, and what rates they are paying on loans and deposits.

2020 should be a very interesting year as the Fed is likely to lower rates. Many economies around the world are heading toward recession and are paying negative interest rates. In addition, the coronavirus is wreaking havoc on world stock markets. At home we have a congress that has not been able to agree on anything, and this year will be no different as they spend all their time campaigning for the November election.

At HomeTown Bank, our strategy has not changed. We have no exit strategy. As bank acquisitions increased in 2019 and expect to continue this year, our decision-making process is focused on long-term strategies. We will strive to meet the financial needs of our customers by getting to know them and to be good listeners.

On a personal note, I want to thank my HomeTown Bank directors and staff for their support this past seven months during the illness of my beautiful wife Diana. We were married for forty-seven years and she was the love of my life. The strength provided by my bank family was truly amazing. She now has a new home in Heaven.

Thank you for your investment in HomeTown Bank.

Sincerely,

Jimmy Rasmussen
President & CEO

2019 Appendix A

Statements of Condition

	December 31,	
	2019	2018
Assets		
Cash and balances due from depository institutions:		
Noninterest-bearing balances, currency and coin	\$ 11,507,887	\$ 13,390,297
Interest-bearing balances	7,031,711	10,518,910
Total cash and cash equivalents	18,539,598	23,909,207
Federal funds sold	18,000,000	-
Securities available for sale	150,032,609	164,484,812
Securities held to maturity	3,225,070	1,842,340
Loans, total	428,843,749	393,339,752
Less: Reserve for possible loan losses	(4,931,213)	(4,618,424)
Loans, net	423,912,536	388,721,328
Bank Premises, equipment, furniture, fixtures and autos (net of depreciation)	9,990,785	10,069,810
Letters of Credit	2,201,891	1,139,529
Other Assets	4,180,401	4,996,990
TOTAL ASSETS	\$ 630,082,890	\$ 595,164,016
Liabilities		
Demand deposits	351,604,739	354,079,269
Savings deposits	65,332,057	64,426,054
Time deposits	129,067,295	105,617,189
Federal funds purchased	-	-
Letters of Credit	2,201,891	1,139,529
Other Liabilities	2,815,871	2,309,687
TOTAL LIABILITIES	\$ 551,021,853	\$ 527,571,728
Equity Capital Accounts		
Common Stock	12/31/19	12/31/18
Number Shares authorized	382,657	382,657
Number Shares outstanding	382,657	382,657
Common Stock (Par Value) \$1.00	\$ 382,657	\$ 382,657
Surplus	415,455	415,455
Undivided Profits	78,262,925	66,794,176
TOTAL EQUITY CAPITAL	\$ 79,061,037	\$ 67,592,288
TOTAL LIABILITIES AND EQUITY CAPITAL	\$ 630,082,890	\$ 595,164,016

2019 Appendix B

Statements of Income

	December 31,		
	2019	2018	2017
Operating Income			
Interest and fees on loans	\$ 23,287,124	\$ 21,846,380	\$ 18,689,909
Income on Federal funds sold and securities purchased under agreements to resell	151,306	190,886	53,357
Interest on Mortgage-backed securities	2,044,196	1,974,087	2,056,478
Interest on obligations of other U.S. Government Agencies and Corporations	136,829	138,703	155,135
Interest on obligations of States and political subdivisions	1,460,555	1,647,668	1,720,275
Dividends on stock	18,949	168,022	73,028
Interest on other investments	327,177	126,212	54,993
Service charges on deposit accounts	211,278	201,608	203,579
Other charges, collection and exchange charges, commissions and fees	671,590	688,588	657,205
Other operating income	1,280,742	1,343,392	1,686,797
TOTAL OPERATING INCOME	\$ 29,589,746	\$ 28,325,546	\$ 25,350,756
Operating Expenses			
Salaries, wages and other employee benefits	\$ 7,747,443	\$ 7,443,921	\$ 6,938,578
Interest on Time Certificates of Deposit of \$100,000 or more	1,506,129	970,023	776,004
Interest on other deposits	2,379,226	1,400,639	1,098,140
Occupancy expense of bank premises	897,374	920,363	1,001,757
Furniture and equipment expense (including depreciation of \$344,647, \$388,426, \$474,493)	607,497	608,207	682,791
Provision for possible loan losses	776,178	907,000	292,500
Other expenses	5,017,991	5,435,209	5,379,289
TOTAL OPERATING EXPENSES	\$ 18,931,838	\$ 17,685,362	\$ 16,169,059
Income before income taxes	10,657,908	10,640,184	9,181,697
Income taxes			
Current	2,069,090	2,064,043	3,229,819
Deferred (benefit) expense	(82,323)	(71,305)	(214,247)
Income taxes, net	<u>1,986,767</u>	<u>1,992,738</u>	<u>3,015,572</u>
Net Income	<u>\$ 8,671,141</u>	<u>\$ 8,647,446</u>	<u>\$ 6,166,125</u>
Earnings per common share			
Net Income	<u>\$ 22.66</u>	<u>\$ 22.60</u>	<u>\$ 16.11</u>

2019 Appendix C

Statements of Comprehensive Income

	December 31,		
	2019	2018	2017
Net income	\$ 8,671,141	\$ 8,647,446	\$ 6,166,125
Other comprehensive income, net of tax			
Unrealized gains (losses) on securities:			
Change in unrealized gain (loss) on securities available-for-sale, net of deferred income tax expense (benefit) of \$1,195,585, (\$475,911), and \$495,095	4,497,676	(1,790,330)	961,043
Reclassification adjustment for realized gains on investment securities available for sale included in net income, net of income tax expense of (\$39,899), (\$25,265), and (\$119,342)	(150,098)	(94,981)	(231,642)
Reclassification adjustment for realized losses on investment securities available for sale included in net income, net of income tax benefit \$25,375, \$21,759, and \$82,776	<u>95,457</u>	<u>81,853</u>	<u>160,682</u>
Total other comprehensive income	<u>4,443,035</u>	<u>(1,803,458)</u>	<u>890,083</u>
Comprehensive income	<u>\$13,114,176</u>	<u>\$ 6,843,988</u>	<u>\$ 7,056,208</u>

2019 Appendix D

Statements of Changes in Stockholders' Equity

	<u>Common Stock</u>	<u>Additional Paid-in Capital</u>	<u>Retained Earnings</u>	<u>Accumulated Other Comprehensive Income</u>	<u>Total Stockholders' Equity</u>
Balances - December 31, 2017	\$ 382,657	\$ 415,455	\$ 62,989,581	\$ (1,508,702)	\$ 62,278,991
Net Income	-	-	8,647,446	-	8,647,446
Other comprehensive income	-	-	-	(1,803,520)	(1,803,520)
Cash dividends (\$4.00 per share)	-	-	(1,530,629)	-	(1,530,629)
Balances - December 31, 2018	382,657	415,455	70,106,398	(3,312,222)	67,592,288
Net Income	-	-	8,671,141	-	8,671,141
Other comprehensive income	-	-	-	4,443,035	4,443,035
Cash dividends (\$4.30 per share)	-	-	(1,645,426)	-	(1,645,426)
Balances - December 31, 2019	<u>\$ 382,657</u>	<u>\$ 415,455</u>	<u>\$ 77,132,113</u>	<u>\$ 1,130,813</u>	<u>\$ 79,061,038</u>

2019 Appendix E

Statements of Cash Flows Years Ended December 31, 2019, 2018, and 2017 Increase (Decrease) in Cash and Cash Equivalents

	2019	December 31, 2018	2017
<i>Cash flows from operating activities:</i>			
Net income	\$ 8,671,141	\$ 8,647,446	\$ 6,166,125
Adjustments to reconcile net income to net cash provided by operating activities:			
Depreciation	646,618	618,654	669,631
Provisions for possible loan losses	776,178	907,000	292,500
Provisions for ORE write-down	-	227,200	10,000
Gain on sale of investments	(69,165)	(16,697)	(107,526)
Change in deferred tax assets and liabilities	(82,321)	(71,307)	310,191
Accretion of discounts	(206,953)	(70,460)	(35,675)
Amortization of investment premium	1,660,315	1,987,867	2,728,299
Stock dividends - Federal Home Loan Bank	(4,480)	(4,200)	(2,000)
Gain on sale of foreclosed assets	(30,072)	53,169	(19,037)
Gain on disposal of assets	(97,388)	-	(144,739)
(Increase) decrease in other assets	(105,258)	323,089	(307,813)
(Increase) decrease in accrued interest receivable	78,386	467,356	(445,307)
Increase (decrease) in accrued interest payable and other liabilities	<u>185,907</u>	<u>(858,082)</u>	<u>1,139,188</u>
Total adjustments	<u>2,751,767</u>	<u>3,563,589</u>	<u>4,087,712</u>
Net cash provided by operating activities	\$ 11,422,908	\$ 12,211,035	\$ 10,253,837
<i>Cash flows from investing activities:</i>			
Purchases of securities - available for sale	(56,954,650)	(85,000,659)	(51,441,808)
Proceeds from sales, maturities, or calls and principal payments - available for sale	75,640,803	88,028,011	77,211,075
Purchases of securities - held to maturity	(1,634,954)	-	-
Proceeds from principal payments - securities held to maturity	262,651	-	-
Net increase in loans to customers	(36,087,776)	(8,977,988)	(35,808,160)
Recoveries on loans	122,009	80,857	-
Federal funds sold	(18,000,000)	-	-
Proceeds from sales of premise and equipment	142,000	-	504,271
Additions to premises and equipment	(612,205)	(307,932)	(758,158)
Proceeds from sales of foreclosed assets	93,453	285,085	155,147
Net cash used by investing activities	\$ (37,028,669)	\$ (5,892,626)	\$ (10,137,633)

2019 Appendix E

Statements of Cash Flows Years Ended December 31, 2019, 2018, and 2017 Increase (Decrease) in Cash and Cash Equivalents (Continued)

	2019	December 31, 2018	2017
<i>Cash flows from financing activities:</i>			
Net increase in demand and savings account deposits	1,471,078	772,675	21,497,167
Net increase in time deposit accounts	20,410,500	1,816,617	(2,122,210)
Federal funds purchased	-	-	(12,000,000)
Cash dividends paid on common stock	(1,645,426)	(1,530,629)	(1,377,565)
Net cash provided by financing activities	\$ 20,236,152	\$ 1,058,663	\$ 5,997,392
Net increase in cash and cash equivalents	(5,369,609)	7,377,072	6,113,596
Cash and cash equivalents beginning of year	<u>23,909,207</u>	<u>16,532,135</u>	<u>10,418,539</u>
Cash and cash equivalents end of year	<u>\$ 18,539,598</u>	<u>\$ 23,909,207</u>	<u>\$ 16,532,135</u>

2019 Appendix F

Reconciliations of Reserve for Possible Loan Losses

	2019	December 31, 2018	2017
Balance at beginning of year	\$ 4,618,424	\$ 4,272,957	\$ 4,071,266
Recoveries credited to reserve	122,009	80,857	1,857
Provision for possible loan losses	776,178	907,000	292,500
TOTAL	\$ 5,516,611	\$ 5,260,814	\$ 4,365,623
Losses charged to Reserve	<u>(585,398)</u>	<u>(642,390)</u>	<u>(92,666)</u>
Balance at the end of year	<u>\$ 4,931,213</u>	<u>\$ 4,618,424</u>	<u>\$ 4,272,957</u>

2019 Appendix G

Notes to Financial Statements Valuation of Securities

	DECEMBER 31, 2019		DECEMBER 31, 2018	
	Book Value	Market Value	Book Value	Market Value
Mortgage-Backed Securities	\$ 92,298,839	\$ 92,408,751	\$ 102,504,923	\$ 99,299,207
Obligations of other U.S. Government Agencies and Corporations	5,492,832	5,406,915	7,229,803	6,961,980
Obligations of State and Political Subdivisions	50,809,532	52,216,943	58,942,775	58,223,624
Other Investments (Restricted)				
Senior Housing Crime Prevention Foundation	2,698,519	2,698,519	1,320,269	1,320,269
Lift Fund, Inc.	250,000	250,000	250,000	250,000
Federal Home Loan Bank Stock	252,601	252,601	248,121	248,121
Federal Reserve Bank Stock	23,950	23,950	23,950	23,950
TOTAL	\$ 151,826,273	\$ 153,257,679	\$ 170,519,841	\$ 166,327,151
Deposits and Profit 2018 and 2017				
TOTAL DEPOSITS	\$ 546,004,091		\$ 524,122,513	
TOTAL PROFIT	\$ 8,671,141		\$ 8,647,446	

2019 Appendix H

Selected Financial Data Summary of Operations

The Bank's operations for the past five fiscal years are summarized as follows:

	DECEMBER 31				
	2019	2018	2017	2016	2015
Net Interest Income	23,540,780	23,721,296	\$20,929,030	\$19,631,887	\$18,883,505
Other Operating Income	2,291,072	2,242,263	2,237,719	1,909,828	1,890,315
Total Operating Income - Net	\$25,831,852	\$25,963,559	\$23,166,749	\$21,541,715	\$20,773,820
Provisions for possible loan losses	776,178	907,000	292,500	101,400	50,000
Operating Expenses-including interest	14,466,931	14,433,009	13,800,078	13,227,703	12,548,751
Income before income taxes and securities gains	10,588,743	10,623,550	9,074,171	8,212,612	8,175,069
Applicable income taxes	1,986,767	1,992,738	3,015,572	2,305,557	2,184,930
Income before securities gains	8,601,976	8,630,812	6,058,599	5,907,055	5,990,139
Net Securities gains	69,165	16,634	107,526	323,215	35,413
Net Income	\$ 8,671,141	\$ 8,647,446	\$ 6,166,125	\$ 6,230,270	\$ 6,025,552
Net Income per share	\$ 22.66	\$ 22.60	\$ 16.11	\$ 16.28	\$ 15.75
Dividends per share	\$ 4.30 cash dividend	\$ 4.00 cash dividend	\$ 3.60 cash dividend	\$ 3.50 cash dividend	\$ 3.40 cash dividend

MANAGEMENT SUMMARY

HomeTown Bank, National Association, engages in the business of general banking in the cities of Galveston, Friendswood, League City, Alvin and Pearland, Texas. The bank's business is oriented toward serving the financial needs of its customers, both business and personal.

The headquarters for HomeTown Bank remains in Galveston. There are twelve competing banks and credit unions with offices on Galveston Island. Only three of the banks are locally owned. The competitive conditions in Galveston are not unusual for a city with a population of approximately 50,180.

The League City, Alvin, Pearland and two Friendswood locations compete for business in northern Galveston, southern Harris, and eastern Brazoria Counties where both large and small banks and credit unions create intense competition. HomeTown Bank has attracted many residential and commercial real estate loans and retail installment loans for the purchase of automobiles and other consumer items. For the fiscal year ending December 31, 2019, HomeTown Bank had approximately \$46 million in outstanding loan commitments compared to \$59.8 million in 2018 and \$51.7 million in 2017. All the loan commitments outstanding as of December 31, 2019 are expected to be exercised during the year 2020.

No material portion of the bank's deposits has been obtained from a single person or from a few persons. HomeTown Bank continues to be a strong real estate lender as 88.2 percent of the bank's loans are secured by some form of real property. The loans are spread across our market area and strict underwriting standards have produced losses well below peer levels. A large percentage of the commercial real estate portfolio is made up of loans to owner-occupied businesses. The bank's business is not seasonal to any significant extent. HomeTown Bank has no foreign source for deposits or loans, as all the bank's business is local in nature.

The bank employs approximately 107 full time equivalent persons. The bank is engaged in commercial and consumer activities. The bank does not participate in any international, trust or municipal trading services. To the best of our officers' knowledge, local compliance with federal, state, and local provisions, which have been enacted or adopted, regulating the discharge of materials into the environment or otherwise relating to the protection of the environment, have not had a material effect upon the capital expenditures, earnings or competitive position of the bank.

The bank's common stock is not registered on any stock exchange. There is no market maker and market quotations are not available. As of December 31, 2019, there were 382,657.18 outstanding shares of the common stock of HomeTown Bank, National Association. There were 564 holders of common stock at that date.

Whitley Penn, LLP serves as the bank's outside auditor. The bank's Internal Audit Committee is composed of four outside directors. In addition, the bank employs a full-time internal audit coordinator and auditing consultant who performs specific audits for the bank. HomeTown Bank, N.A. is a national bank and is examined by the Office of the Comptroller of the Currency. The bank is also a member of the Federal Deposit Insurance Corporation, the Federal Reserve System, and files reports quarterly with the Office of Comptroller of the Currency.

Deposits grew 4.17 percent in 2019 compared to .50 percent in 2018 and 3.86 percent in 2017. Deposits for 2020 are projected to increase 1.96 percent. The projected deposit increase will place no burden on capital requirements. Tier 1 Risk Based Capital at year-end 2019 was 17.11 percent compared to 17.09 percent in 2018 and 15.85 percent in 2017. The 2019 Leverage Ratio was 12.44 percent compared to 12.01 percent in 2018 and 10.88 percent in 2017. All capital ratios are substantially above regulatory minimums. A cash dividend of \$4.30 per share totaling \$1,645,426 was paid in 2019. The cash dividend was \$4.00 per share totaling \$1,530,629 in 2018.

As of December 31, 2019, The Baker Group- Oklahoma City, The Independent Bankers Bank- Dallas and Raymond James Fixed Income Capital Markets are the approved vendors for the bank's investment portfolio. The bank's investment portfolio as of December 31, 2019, represents 24.32 percent of total assets compared to 27.94 percent in 2018.

The bank follows the guidance in Accounting Standards Codification 320 Investments - Debt and Equity Securities. Securities that management has the ability and intent to hold to maturity are classified as "Held to Maturity" and carried at cost. Remaining securities are classified as "Available for Sale" and are carried at fair value. Unrealized gains and losses on "Available for Sale" securities are recognized as direct increases or decreases in stockholder's equity.

As of December 31, 2019, the "Available for Sale" portion of the portfolio showed an unrealized gain in fair value of \$1,431,405 with an after-tax adjustment to capital of \$1,130,813. This compares with an unrealized loss of (\$4,192,689) in 2018 with an after-tax adjustment to capital of (\$3,312,225).

Net income after federal income tax for 2019 was \$8,671,138 compared to \$8,647,445 in 2018 and \$6,166,125 in 2017. Net earnings were up .27% percent in 2019 as compared to 2018. New gross loan volume totaled \$101.3 million in 2019 compared to \$124.9 million in 2018 and \$105.5 million in 2017. Income on investment securities was \$4.20 million in 2019 compared to \$4.26 million in 2018.

The loan loss reserve at year-end 2019 totaled \$4,931,213 compared to \$4,618,424 in 2018. As of December 31, 2019, the reserve was 1.15 percent of total loans compared to 1.17 percent in 2018. The reserve is considered adequate by management based on the strong performance of the loan portfolio. The loan loss reserve is reviewed monthly and approved quarterly by the Board of Directors. The 2020 budget will keep the loan loss reserve to total loan ratio in a range from 1.15 to 1.20 percent. As of December 31, 2019, non-accrual loans totaled \$1,167,027 compared to \$255,980 in 2018 and \$4,637,525 in 2017. Non-accrual loans as a percentage of total loans on December 31, 2019 were 0.27 percent compared to 0.07 percent in 2018 and 1.20 percent in 2017. Management believes the amount of non-accrual loans is at a manageable level.

The 2020 budget projects a 7.58 percent increase in net income after tax, based on strong loan demand, an improvement in investment yield, and strong cost controls. Deterioration in economic conditions could have a material adverse impact on the quality of the bank's loan portfolio and the demand for its products and services. These forward-looking statements relate to, among other things, expectations of the business environment in which HomeTown Bank, N.A. operates, projections of future performance, perceived opportunities in the market and statements regarding the bank's mission and vision. The bank's actual results, performance, or achievements may differ significantly from the results, performance, or achievements expressed or implied in such forward-looking statements.

Thank you for your investment in HomeTown Bank.

Jimmy Rasmussen
President and CEO

OFFICERS

Jimmy Rasmussen
President & CEO
Allan Rasmussen, Jr.
Senior Executive Vice President
Kyle McFatrige
Executive Vice President/
Cashier
Scott Kusnerik
Executive Vice President
Candy Temple
Executive Vice President
Angela Brooks
Senior Vice President
Stephany Cantu
Senior Vice President
Gayle Culling
Senior Vice President
Rosie Garcia
Senior Vice President
Sharon Hansen
Senior Vice President
Cesar Hernandez
Senior Vice President
Marvin Langston
Senior Vice President
Jennifer Matthews
Senior Vice President
Sean P. Murphy
Senior Vice President
Steve Owens
Senior Vice President
Bill Provenzano
Senior Vice President
Ray Rusk
Senior Vice President
Martha Salinas
Senior Vice President
Jenny Calles
Vice President
Jenny Chatman
Vice President
Chad Dudley
Vice President
Jill Fredo
Vice President
Armando Garza
Vice President
Jim Goebel
Vice President
Lulu Higgins
Vice President
Jeanette Mack
Vice President
Chris Myers
Vice President

Susan O'Quinn
Vice President
Diana Ramos
Vice President
Donna Rizzo
Vice President
Brandon Rogers
Vice President
Traci Shugart-Garcia
Vice President
Denise Spruiell
Vice President
Elise Worthen
Vice President
Scott Asimakis
Assistant Vice President
Graylin Beals
Assistant Vice President
Elizabeth Birch
Assistant Vice President
Cynthia Gomez
Assistant Vice President
Tiffini Hughes
Assistant Vice President
Lynda Lee
Assistant Vice President
Crystal Martinez
Assistant Vice President
Ana Mireles-Dominguez
Assistant Vice President
Crystal Pena
Assistant Vice President
Anita Pohlemann
Assistant Vice President
Brittney Salinas
Assistant Vice President
Diana Torres
Assistant Vice President
Lauren Zahniser
Assistant Vice President

DIRECTORS

Dotsy Balentine
Kent Ballard
Stacy Dienst
Maurice Estlinbaum
Sidney C. Farmer III
M.J. Gaido, Jr.
Greg Garrison
E. Vince Matthews III
Robert L. Moody, Jr.
Jimmy Rasmussen
G. William Rider
T.A. Waterman, Jr.