

SHORE BANCSHARES INC  
Form 10-Q  
November 09, 2010

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

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FORM 10-Q

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

For the Quarterly Period Ended September 30, 2010

OR

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

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

Commission file number 0-22345

SHORE BANCSHARES, INC.  
(Exact name of registrant as specified in its charter)

Maryland  
(State or Other Jurisdiction of  
Incorporation or Organization)

52-1974638  
(I.R.S. Employer  
Identification No.)

18 East Dover Street, Easton, Maryland  
(Address of Principal Executive Offices)

21601  
(Zip Code)

(410) 822-1400  
Registrant's Telephone Number, Including Area Code

N/A

Former name, former address and former fiscal year, if changed since last report.

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

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes  No  (Not Applicable)

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

Large accelerated filer	<input type="checkbox"/>	Accelerated filer	<input checked="" type="checkbox"/>
Non-accelerated filer	<input type="checkbox"/>	Smaller reporting company	<input type="checkbox"/>

(Do not check if a smaller reporting company)

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

APPLICABLE ONLY TO CORPORATE ISSUERS

Indicate the number of shares outstanding of each of the issuer’s classes of common stock, as of the latest practicable date: 8,443,436 shares of common stock outstanding as of October 29, 2010.

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## PART I – FINANCIAL INFORMATION

## Item 1. Financial Statements.

SHORE BANCSHARES, INC.  
CONSOLIDATED BALANCE SHEETS  
(Dollars in thousands, except per share amounts)

	September 30, 2010 (Unaudited)	December 31, 2009
<b>ASSETS</b>		
Cash and due from banks	\$ 21,764	\$ 14,411
Interest-bearing deposits with other banks	18,014	598
Federal funds sold	35,161	60,637
Investment securities:		
Available for sale, at fair value	96,219	97,595
Held to maturity, at amortized cost – fair value of \$8,125 (2010) and \$9,012 (2009)	7,856	8,940
Loans	906,490	916,557
Less: allowance for credit losses	(13,153)	(10,876)
Loans, net	893,337	905,681
Premises and equipment, net	14,714	14,307
Goodwill	12,954	15,954
Other intangible assets, net	4,969	5,406
Other real estate and other assets owned, net	1,517	2,572
Other assets	27,998	30,415
<b>TOTAL ASSETS</b>	<b>\$ 1,134,503</b>	<b>\$ 1,156,516</b>
<b>LIABILITIES</b>		
Deposits:		
Noninterest-bearing demand	\$ 121,480	\$ 122,492
Interest-bearing demand	122,774	133,946
Money market and savings	261,500	249,793
Certificates of deposit \$100,000 or more	266,082	262,663
Other time	210,592	222,043
Total deposits	982,428	990,937
Short-term borrowings	17,782	20,404
Accrued expenses and other liabilities	10,509	15,936
Long-term debt	1,429	1,429
<b>TOTAL LIABILITIES</b>	<b>1,012,148</b>	<b>1,028,706</b>
<b>STOCKHOLDERS' EQUITY</b>		
Common stock, par value \$.01 per share; shares authorized – 35,000,000; shares issued and outstanding – 8,443,436 (2010) and 8,418,963 (2009)	84	84
Warrant	1,543	1,543
Additional paid in capital	30,173	29,872
Retained earnings	92,115	96,151
Accumulated other comprehensive (loss) income	(1,560)	160

TOTAL STOCKHOLDERS' EQUITY	122,355	127,810
TOTAL LIABILITIES AND STOCKHOLDERS' EQUITY	\$ 1,134,503	\$ 1,156,516

See accompanying notes to Consolidated Financial Statements.

SHORE BANCSHARES, INC.  
CONSOLIDATED STATEMENTS OF INCOME (LOSS) (Unaudited)  
(Dollars in thousands, except per share amounts)

	For the Three Months Ended September 30,		For the Nine Months Ended September 30,	
	2010	2009	2010	2009
<b>INTEREST INCOME</b>				
Interest and fees on loans	\$ 13,083	\$ 14,001	\$ 39,004	\$ 41,372
Interest and dividends on investment securities:				
Taxable	677	800	2,405	2,324
Tax-exempt	50	77	165	241
Interest on federal funds sold	21	31	47	61
Interest on deposits with other banks	6	4	11	11
Total interest income	13,837	14,913	41,632	44,009
<b>INTEREST EXPENSE</b>				
Interest on deposits	3,117	4,368	9,744	13,094
Interest on short-term borrowings	17	19	68	96
Interest on long-term debt	16	98	47	247
Total interest expense	3,150	4,485	9,859	13,437
NET INTEREST INCOME	10,687	10,428	31,773	30,572
Provision for credit losses	4,193	1,702	16,727	5,318
NET INTEREST INCOME AFTER PROVISION FOR CREDIT LOSSES	6,494	8,726	15,046	25,254
<b>NONINTEREST INCOME</b>				
Service charges on deposit accounts	841	861	2,458	2,558
Trust and investment fee income	357	274	1,145	750
Investment securities gains	-	-	-	49
Insurance agency commissions	2,513	2,744	7,997	8,972
Other noninterest income	932	840	2,493	3,087
Total noninterest income	4,643	4,719	14,093	15,416
<b>NONINTEREST EXPENSE</b>				
Salaries and wages	4,404	4,765	13,257	14,064
Employee benefits	897	1,211	2,936	3,791
Occupancy expense	547	616	1,766	1,752
Furniture and equipment expense	325	299	938	915
Data processing	696	675	1,987	1,865
Directors' fees	118	109	344	394
Goodwill and other intangible assets impairment	3,051	-	3,051	-
Amortization of other intangible assets	128	128	386	386
Insurance agency commissions expense	338	428	1,230	1,515
FDIC insurance premium expense	448	458	1,389	1,621
Other noninterest expenses	1,677	1,608	5,354	4,570

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Total noninterest expense	12,629	10,297	32,638	30,873
(LOSS) INCOME BEFORE INCOME TAXES	(1,492)	3,148	(3,499)	9,797
Income tax (benefit) expense	(92)	1,197	(982)	3,740
NET (LOSS) INCOME	(1,400)	1,951	(2,517)	6,057
Preferred stock dividends and discount accretion	-	-	-	1,876
Net (loss) income available to common shareholders	\$ (1,400)	\$ 1,951	\$ (2,517)	\$ 4,181
Basic net (loss) earnings per common share	\$ (0.17)	\$ 0.23	\$ (0.30)	\$ 0.50
Diluted net (loss) earnings per common share	\$ (0.17)	\$ 0.23	\$ (0.30)	\$ 0.50
Dividends paid per common share	\$ 0.06	\$ 0.16	\$ 0.18	\$ 0.48

See accompanying notes to Consolidated Financial Statements.

SHORE BANCSHARES, INC.  
CONSOLIDATED STATEMENTS OF CHANGES IN STOCKHOLDERS' EQUITY (Unaudited)  
For the Nine Months Ended September 30, 2010 and 2009  
(Dollars in thousands, except per share amounts)

	Preferred	Common		Additional	Retained	Accumulated	Total
	Stock	Stock	Warrant	Paid in	Earnings	Other	Stockholders'
				Capital		Comprehensive	Equity
						Income	
						(Loss)	
Balances, January 1, 2010	\$ -	\$ 84	\$ 1,543	\$ 29,872	\$ 96,151	\$ 160	\$ 127,810
Comprehensive income:							
Net loss	-	-	-	-	(2,517)	-	(2,517)
Unrealized gains on available-for-sale securities, net of taxes	-	-	-	-	-	989	989
Unrealized losses on cash flow hedging activities, net of taxes	-	-	-	-	-	(2,709)	(2,709)
Total comprehensive income							(4,237)
Stock-based compensation expense							
	-	-	-	301	-	-	301
Cash dividends paid (\$0.18 per share)							
	-	-	-	-	(1,519)	-	(1,519)
Balances, September 30, 2010	\$ -	\$ 84	\$ 1,543	\$ 30,173	\$ 92,115	\$ (1,560)	\$ 122,355
Balances, January 1, 2009	\$ -	\$ 84	\$ -	\$ 29,768	\$ 96,140	\$ 1,393	\$ 127,385
Comprehensive income:							
Net income	-	-	-	-	6,057	-	6,057
Unrealized losses on available-for-sale securities, net of taxes	-	-	-	-	-	(276)	(276)
Unrealized losses on cash flow hedging activities, net of taxes	-	-	-	-	-	(652)	(652)
Total comprehensive income							5,129
Warrant issued							
	-	-	1,543	-	-	-	1,543
Preferred shares issued pursuant to TARP							
	25,000	-	-	-	-	-	25,000
Discount from issuance of preferred stock							
	(1,543)	-	-	-	-	-	(1,543)
Discount accretion							
	68	-	-	-	(68)	-	-



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Repurchase of preferred stock	(23,525)	-	-	-	-	-	(23,525)
Common shares issued for employee stock-based awards	-	-	-	2	-	-	2
Stock-based compensation expense	-	-	-	74	-	-	74
Preferred stock dividends	-	-	-	-	(1,808)	-	(1,808)
Cash dividends paid (\$0.48 per share)	-	-	-	-	(4,038)	-	(4,038)
Balances, September 30, 2009	\$ -	\$ 84	\$ 1,543	\$ 29,844	\$ 96,283	\$ 465	\$ 128,219

See accompanying notes to Consolidated Financial Statements.

SHORE BANCSHARES, INC.  
CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME (LOSS) (Unaudited)  
(Dollars in thousands)

	For the Three Months Ended		For the Nine Months Ended	
	September 30,		September 30,	
	2010	2009	2010	2009
Net (loss) income	\$ (1,400)	\$ 1,951	\$ (2,517)	\$ 6,057
Other comprehensive (loss) income:				
Securities available for sale:				
Unrealized holding gains (losses) on available-for-sale securities	242	604	1,654	(410)
Tax effect	(97)	(241)	(665)	163
Reclassification of gains recognized in net income	-	-	-	(49)
Tax effect	-	-	-	20
Net of tax amount	145	363	989	(276)
Cash flow hedging activities:				
Unrealized holding losses on cash flow hedging activities	(1,077)	(1,093)	(4,543)	(1,093)
Tax effect	435	441	1,834	441
Net of tax amount	(642)	(652)	(2,709)	(652)
Total other comprehensive loss	(497)	(289)	(1,720)	(928)
Comprehensive (loss) income	\$ (1,897)	\$ 1,662	\$ (4,237)	\$ 5,129

See accompanying notes to Consolidated Financial Statements.

SHORE BANCSHARES, INC.  
CONSOLIDATED STATEMENTS OF CASH FLOWS (Unaudited)  
(Dollars in thousands)

	For the Nine Months Ended September 30,	
	2010	2009
<b>CASH FLOWS FROM OPERATING ACTIVITIES:</b>		
Net (loss) income	\$ (2,517)	\$ 6,057
Adjustments to reconcile net income to net cash provided by operating activities:		
Provision for credit losses	16,727	5,318
Goodwill and other intangible assets impairment	3,051	-
Depreciation and amortization	1,835	1,370
Discount accretion on debt securities	(91)	(191)
Stock-based compensation expense	301	74
Gains on sales of securities	-	(49)
Losses on sales of other real estate owned	56	-
Write-downs of other real estate owned	657	159
Gains on interest rate swaps	-	(420)
Net changes in:		
Insurance premiums receivable	565	155
Accrued interest receivable	90	(163)
Other assets	(1,589)	(1,704)
Accrued interest payable	(855)	(132)
Other liabilities	(4,572)	285
Net cash provided by operating activities	13,658	10,759
<b>CASH FLOWS FROM INVESTING ACTIVITIES:</b>		
Proceeds from maturities and principal payments of securities available for sale	44,113	36,686
Proceeds from sales of securities available for sale	-	2,048
Purchases of securities available for sale	(41,580)	(54,851)
Proceeds from maturities and principal payments of securities held to maturity	1,070	2,815
Purchases of securities held to maturity	-	(1,563)
Net increase in loans	(5,030)	(36,059)
Purchases of premises and equipment	(1,253)	(982)
Proceeds from sales of other real estate owned	990	-
Purchases of interest rate caps	-	(6,475)
Investment in unconsolidated subsidiary	(25)	-
Net cash used in investing activities	(1,715)	(58,381)
<b>CASH FLOWS FROM FINANCING ACTIVITIES:</b>		
Net (decrease) increase in demand, money market and savings deposits	(477)	102,839
Net (decrease) increase in certificates of deposit	(8,032)	43,987
Net decrease in short-term borrowings	(2,622)	(35,296)
Repayment of long-term debt	-	(6,000)
Net receipt of counterparty collateral – interest rate caps	-	6,528
Proceeds from issuance of preferred stock and warrant	-	25,000
Repurchase of preferred stock	-	(23,525)
Proceeds from issuance of common stock	-	2

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Preferred stock dividends paid	-	(1,808)
Common stock dividends paid	(1,519)	(4,038)
Net cash (used in) provided by financing activities	(12,650)	107,689
Net (decrease) increase in cash and cash equivalents	(707)	60,067
Cash and cash equivalents at beginning of period	75,646	27,294
Cash and cash equivalents at end of period	\$ 74,939	\$ 87,361
Supplemental cash flows information:		
Interest paid	\$ 10,715	\$ 13,569
Income taxes paid	\$ 988	\$ 3,678
Transfers from loans to other real estate owned	\$ 668	\$ 2,072

See accompanying notes to Consolidated Financial Statements.

Shore Bancshares, Inc.  
Notes to Consolidated Financial Statements  
For the Three and Nine Months Ended September 30, 2010 and 2009  
(Unaudited)

Note 1 - Basis of Presentation

The consolidated financial statements include the accounts of Shore Bancshares, Inc. and its subsidiaries with all significant intercompany transactions eliminated. The consolidated financial statements conform to accounting principles generally accepted in the United States of America (“GAAP”) and to prevailing practices within the banking industry. The accompanying interim financial statements are unaudited; however, in the opinion of management all adjustments necessary to present fairly the consolidated financial position at September 30, 2010, the consolidated results of operations and comprehensive income for the three and nine months ended September 30, 2010 and 2009, and changes in stockholders’ equity and cash flows for the nine months ended September 30, 2010 and 2009, have been included. All such adjustments are of a normal recurring nature. The amounts as of December 31, 2009 were derived from the 2009 audited financial statements. The results of operations for the three and nine months ended September 30, 2010 are not necessarily indicative of the results to be expected for any other interim period or for the full year. This Quarterly Report on Form 10-Q should be read in conjunction with the Annual Report of Shore Bancshares, Inc. on Form 10-K for the year ended December 31, 2009. For purposes of comparability, certain reclassifications have been made to amounts previously reported to conform with the current period presentation.

Shore Bancshares, Inc. has evaluated events and transactions occurring subsequent to the balance sheet date of September 30, 2010 for items that should potentially be recognized or disclosed in these financial statements as prescribed by Topic 855, “Subsequent Events”, of the Financial Accounting Standards Board’s Accounting Standards Codification (“ASC”).

When used in these notes, the term “the Company” refers to Shore Bancshares, Inc. and, unless the context requires otherwise, its consolidated subsidiaries.

Note 2 – Earnings Per Share

Basic earnings/(loss) per common share are calculated by dividing net income/(loss) available to common stockholders by the weighted average number of common shares outstanding during the period. Diluted earnings/(loss) per common share are calculated by dividing net income/(loss) available to common stockholders by the weighted average number of common shares outstanding during the period, adjusted for the dilutive effect of stock-based awards. There is no dilutive effect on the loss per share during loss periods. The following table provides information relating to the calculation of earnings/(loss) per common share:

(In thousands, except per share data)	For the Three Months Ended		For the Nine Months Ended	
	September 30,		September 30,	
	2010	2009	2010	2009
Net (loss) income available to common shareholders	\$ (1,400)	\$ 1,951	\$ (2,517)	\$ 4,181
Weighted average shares outstanding - Basic	8,443	8,419	8,441	8,412
Dilutive effect of stock-based awards	-	4	-	4
Weighted average shares outstanding - Diluted	8,443	8,423	8,441	8,416
(Loss) earnings per common share - Basic	\$ (0.17)	\$ 0.23	\$ (0.30)	\$ 0.50
(Loss) earnings per common share - Diluted	\$ (0.17)	\$ 0.23	\$ (0.30)	\$ 0.50

The calculations of diluted earnings/(loss) per share for the three and nine months ended September 30, 2010 each excluded eight thousand weighted average stock-based awards and that portion of a warrant to purchase 173 thousand weighted average shares of common stock because the effect would have been antidilutive. There were no weighted average stock-based awards excluded from the calculations of diluted earnings per share for the three and nine months ended September 30, 2009. The calculations of diluted earnings per share for the three and nine months ended September 30, 2009 excluded that portion of a warrant to purchase 173 thousand and 168 thousand weighted average shares of common stock, respectively, because the effect would have been antidilutive.

## Note 3 – Investment Securities

The amortized cost and estimated fair values of investment securities are as follows:

(Dollars in thousands)	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Estimated Fair Value
<b>Available-for-sale securities:</b>				
<b>September 30, 2010:</b>				
Obligations of U.S. Government agencies and corporations	\$ 55,902	\$ 1,648	\$ 32	\$ 57,518
Mortgage-backed securities	36,888	1,320	91	38,117
Other equity securities	561	23	-	584
<b>Total</b>	<b>\$ 93,351</b>	<b>\$ 2,991</b>	<b>\$ 123</b>	<b>\$ 96,219</b>
<b>December 31, 2009:</b>				
Obligations of U.S. Treasury	\$ 2,998	\$ -	\$ -	\$ 2,998
Obligations of U.S. Government agencies and corporations	57,258	879	397	57,740
Mortgage-backed securities				