

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

**FORM 10-Q**

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

For the quarterly period ended March 31, 2023

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

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

**NATIONAL BANKSHARES, INC.**

(Exact name of registrant as specified in its charter)

Commission File Number 0-15204

Virginia

(State or other jurisdiction of incorporation or organization)

54-1375874

(I.R.S. Employer Identification No.)

101 Hubbard Street

Blacksburg, Virginia 24062-9002

(Address of principal executive offices)

(540) 951-6300

(Registrant's telephone number, including area code)

(Not applicable)

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

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

Title of each class	Trading Symbol(s)	Name of each exchange on which registered
<b>Common Stock, par value \$1.25 per share</b>	<b>NKSH</b>	<b>Nasdaq Capital Market</b>

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

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

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, a smaller reporting company, or an emerging growth company. See the definitions of "large accelerated filer," "accelerated filer," "smaller reporting company," and "emerging growth company" in Rule 12b-2 of the Exchange Act.

Large accelerated filer  Accelerated filer  Non-accelerated filer  Smaller reporting company  Emerging growth company

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

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

Indicate the number of shares outstanding of each of the issuer's classes of common stock, as of the latest practicable date.

Outstanding shares of common stock at May 10, 2023

5,889,687

**NATIONAL BANKSHARES, INC.**  
Form 10-Q  
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**Item 1. Financial Statements**

**Part I**  
**Financial Information**  
National Bankshares, Inc.  
Consolidated Balance Sheets

<b>(in thousands, except share and per share data)</b>	<b>(Unaudited)</b> <b>March 31,</b> <b>2023</b>	<b>December 31,</b> <b>2022</b>
<b>Assets</b>		
Cash and due from banks	\$ 11,695	\$ 12,403
Interest-bearing deposits	42,966	59,026
Securities available for sale, at fair value	651,047	656,852
Restricted stock, at cost	929	941
Loans:		
Loans, net of unearned income and deferred fees and costs	856,965	852,744
Less allowance for credit losses	(10,650)	(8,225)
Loans, net	846,315	844,519
Premises and equipment, net	10,431	10,371
Accrued interest receivable	6,007	6,001
Other real estate owned, net	662	662
Goodwill	5,848	5,848
Bank-owned life insurance	43,551	43,312
Other assets	34,826	37,616
<b>Total assets</b>	<b>\$ 1,654,277</b>	<b>\$ 1,677,551</b>
<b>Liabilities and Stockholders' Equity</b>		
Noninterest-bearing demand deposits	\$ 311,137	\$ 327,713
Interest-bearing demand deposits	871,748	933,269
Savings deposits	202,996	214,114
Time deposits	125,571	67,629
Total deposits	1,511,452	1,542,725
Accrued interest payable	314	106
Other liabilities	11,468	12,033
Total liabilities	1,523,234	1,554,864
Commitments and contingencies	-	-
<b>Stockholders' Equity</b>		
Preferred stock, no par value, 5,000,000 shares authorized; none issued and outstanding	-	-
Common stock of \$1.25 par value. Authorized 10,000,000 shares; issued and outstanding 5,889,687 shares at March 31, 2023 and December 31, 2022	7,362	7,362
Retained earnings	195,718	199,091
Accumulated other comprehensive loss, net	(72,037)	(83,766)
Total stockholders' equity	131,043	122,687
<b>Total liabilities and stockholders' equity</b>	<b>\$ 1,654,277</b>	<b>\$ 1,677,551</b>

See accompanying notes to consolidated financial statements.

National Bankshares, Inc.  
Consolidated Statements of Income  
Three Months Ended March 31, 2023 and 2022  
(Unaudited)

(in thousands, except share and per share data)	March 31,	
	2023	2022
<b>Interest Income</b>		
Interest and fees on loans	\$ 9,333	\$ 8,100
Interest on interest-bearing deposits	228	49
Interest on securities – taxable	4,118	2,473
Interest on securities – nontaxable	365	428
Total interest income	14,044	11,050
<b>Interest Expense</b>		
Interest on time deposits	359	37
Interest on other deposits	2,454	618
Interest on borrowings	285	-
Total interest expense	3,098	655
Net interest income	10,946	10,395
Provision for credit losses	2	134
Net interest income after provision for credit losses	10,944	10,261
<b>Noninterest Income</b>		
Service charges on deposit accounts	592	562
Other service charges and fees	53	55
Credit and debit card fees, net	467	440
Trust income	445	443
BOLI income	239	238
Gain on sale of mortgage loans	16	61
Gain on sale of securities	12	-
Other income	375	492
Total noninterest income	2,199	2,291
<b>Noninterest Expense</b>		
Salaries and employee benefits	4,434	3,978
Occupancy, furniture and fixtures	542	492
Data processing and ATM	873	787
FDIC assessment	117	111
Net costs of other real estate owned	11	10
Franchise taxes	375	362
Professional services	753	225
Other operating expenses	559	648
Total noninterest expense	7,664	6,613
Income before income taxes	5,479	5,939
Income tax expense	948	1,053
<b>Net Income</b>	\$ 4,531	\$ 4,886
Basic and fully diluted net income per common share	\$ 0.77	\$ 0.81
Weighted average number of common shares outstanding, basic and diluted	5,889,687	6,047,230
Dividends declared per common share	\$ 1.00	\$ -

See accompanying notes to consolidated financial statements.

National Bankshares, Inc.  
Consolidated Statements of Comprehensive Income (Loss)  
Three Months Ended March 31, 2023 and 2022  
(Unaudited)

(in thousands)	March 31,	
	2023	2022
Net Income	\$ 4,531	\$ 4,886
<b>Other Comprehensive Income (Loss), Net of Tax</b>		
Unrealized holding gain (loss) on available for sale securities net of tax of \$3,121 and (\$8,992) for the periods ended March 31, 2023 and March 31, 2022, respectively	11,738	(33,826)
Reclassification adjustment for gain included in net income, net of tax of (\$3) in 2023	(9)	-
Other comprehensive income (loss), net of tax	11,729	(33,826)
<b>Total Comprehensive Income (Loss)</b>	<b>\$ 16,260</b>	<b>\$ (28,940)</b>

See accompanying notes to consolidated financial statements.

National Bankshares, Inc.  
Consolidated Statements of Changes in Stockholders' Equity  
(Unaudited)  
Three Months Ended March 31, 2023 and 2022

(in thousands except per share and share data)	Common Stock	Retained Earnings	Accumulated Other Comprehensive Loss	Total
Balances at December 31, 2021	\$ 7,580	\$ 188,229	\$ (4,058)	\$ 191,751
Net income	-	4,886	-	4,886
Common stock repurchased, 41,185 shares	(52)	(1,470)	-	(1,522)
Other comprehensive loss, net of tax of (\$8,992)	-	-	(33,826)	(33,826)
<b>Balances at March 31, 2022</b>	<b>\$ 7,528</b>	<b>\$ 191,645</b>	<b>\$ (37,884)</b>	<b>\$ 161,289</b>
Balances at December 31, 2022	\$ 7,362	\$ 199,091	\$ (83,766)	\$ 122,687
Adoption of ASU 2016-13	-	(2,014)	-	(2,014)
Net income	-	4,531	-	4,531
Cash dividends of \$1.00 per share	-	(5,890)	-	(5,890)
Other comprehensive income, net of tax of \$3,118	-	-	11,729	11,729
<b>Balances at March 31, 2023</b>	<b>\$ 7,362</b>	<b>\$ 195,718</b>	<b>\$ (72,037)</b>	<b>\$ 131,043</b>

See accompanying notes to consolidated financial statements.

National Bankshares, Inc.  
Consolidated Statements of Cash Flows  
Three Months Ended March 31, 2023 and 2022  
(Unaudited)

(in thousands)	March 31, 2023	March 31, 2022
<b>Cash Flows from Operating Activities</b>		
Net income	\$ 4,531	\$ 4,886
Adjustments to reconcile net income to net cash provided by operating activities:		
Provision for credit losses	2	134
Depreciation of bank premises and equipment	163	154
Amortization of premiums and accretion of discounts, net	253	359
Gain on sales of securities available for sale, net	(12)	-
Gain on sales of repossessed assets	5	-
Increase in cash value of bank-owned life insurance	(239)	(238)
Origination of mortgage loans held for sale	(1,239)	(2,333)
Proceeds from sale of mortgage loans held for sale	1,255	3,009
Gain on sale of mortgage loans held for sale	(16)	(61)
Net change in:		
Accrued interest receivable	(6)	(329)
Other assets	200	479
Accrued interest payable	208	3
Other liabilities	(772)	622
Net cash provided by operating activities	<u>4,333</u>	<u>6,685</u>
<b>Cash Flows from Investing Activities</b>		
Proceeds from calls, principal payments, sales and maturities of securities available for sale	20,411	13,890
Purchase of securities available for sale	-	(70,341)
Net change in restricted stock	12	(96)
Purchase of loan participations	(2,280)	(4,687)
Collection of loan participations	3,126	92
Loan originations and principal collections, net	(5,166)	(11,545)
Proceeds from sale of repossessed assets	9	-
Recoveries on loans charged off	173	40
Proceeds from sale and purchases of premises and equipment, net	(223)	(196)
Net cash provided by (used in) investing activities	<u>16,062</u>	<u>(72,843)</u>
<b>Cash Flows from Financing Activities</b>		
Net change in time deposits	57,942	(2,119)
Net change in other deposits	(89,215)	51,285
Common stock repurchased	-	(1,522)
Cash dividends paid	(5,890)	-
Net cash (used in) provided by financing activities	<u>(37,163)</u>	<u>47,644</u>
Net change in cash and due from banks	(16,768)	(18,514)
Cash and due from banks at beginning of period	71,429	138,789
Cash and due from banks at end of period	<u>\$ 54,661</u>	<u>\$ 120,275</u>

(Continued)

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**Supplemental Disclosures of Cash Flow Information**

Interest paid on deposits	\$	2,890	\$	652
Income taxes paid		1,015		-

**Supplemental Disclosure of Noncash Activities**

Loans charged against the allowance for credit losses	\$	92	\$	60
Loans transferred to repossessed assets		7		-
Unrealized holding gain (loss) on securities available for sale		14,847		(42,818)
Lease liabilities arising from obtaining right-of-use assets		-		25

See accompanying notes to consolidated financial statements.



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**National Bankshares, Inc.**  
**Notes to Consolidated Financial Statements**  
**March 31, 2023**  
**(Unaudited)**

**\$ in thousands, except per share data**

**Note 1: General**

The consolidated financial statements of National Bankshares, Inc. (“NBI”) and its wholly-owned subsidiaries, The National Bank of Blacksburg (the “Bank” or “NBB”) and National Bankshares Financial Services, Inc. (“NBFS”) (collectively, the “Company”), conform to accounting principles generally accepted in the United States of America (“GAAP”) and to general practices within the banking industry. The accompanying interim period consolidated financial statements are unaudited; however, in the opinion of Management, all adjustments consisting of normal recurring adjustments, which are necessary for a fair presentation of the consolidated financial statements, have been included. The results of operations for the three month period ended March 31, 2023 are not necessarily indicative of results of operations for the full year or any other interim period. The interim period consolidated financial statements and financial information included in this Form 10-Q should be read in conjunction with the notes to consolidated financial statements included in the Company’s 2022 Form 10-K. The Company posts all reports required to be filed under the Securities Exchange Act of 1934 on its web site at [www.nationalbankshares.com](http://www.nationalbankshares.com).

Risks and Uncertainties

The Company is closely monitoring risks that may impact its business, including high inflation, along with U.S. monetary policy maneuvers to reduce inflation. Inflation and U.S. monetary policy maneuvers to reduce it may impact the Company’s customers’ demand for banking services and ability to qualify for and/or repay loans. These risks could adversely affect the Company’s business, financial condition, results of operations, cash flows, credit risk, asset valuations and capital position.

Recent Accounting Pronouncements

In March 2020, the Financial Accounting Standards Board (“FASB”) issued Accounting Standards Update (“ASU”) 2020-04 “Reference Rate Reform (Topic 848): Facilitation of the Effects of Reference Rate Reform on Financial Reporting.” These amendments provide temporary optional guidance to ease the potential burden in accounting for reference rate reform. The ASU provides optional expedients and exceptions for applying generally accepted accounting principles to contract modifications and hedging relationships, subject to meeting certain criteria, that reference the London Interbank Offered Rate (“LIBOR”) or another reference rate expected to be discontinued. It is intended to help stakeholders during the global market-wide reference rate transition period. The guidance is effective for all entities as of March 12, 2020 through December 31, 2022. Subsequently, in January 2021, the FASB issued ASU 2021-01 “Reference Rate Reform (Topic 848): Scope.” This ASU clarifies that certain optional expedients and exceptions in Topic 848 for contract modifications and hedge accounting apply to derivatives that are affected by the discounting transition. The ASU also amends the expedients and exceptions in Topic 848 to capture the incremental consequences of the scope clarification and to tailor the existing guidance to derivative instruments affected by the discounting transition. An entity may elect to apply ASU 2021-01 on contract modifications that change the interest rate used for margining, discounting, or contract price alignment retrospectively as of any date from the beginning of the interim period that includes March 12, 2020, or prospectively to new modifications from any date within the interim period that includes or is subsequent to January 7, 2021, up to the date that financial statements are available to be issued. An entity may elect to apply ASU 2021-01 to eligible hedging relationships existing as of the beginning of the interim period that includes March 12, 2020, and to new eligible hedging relationships entered into after the beginning of the interim period that includes March 12, 2020. The Company has a small number of participation loans that reference LIBOR. The Company is working with the primary banks to determine appropriate actions.

In December 2022, the FASB issued ASU 2022-06, “Reference Rate Reform (Topic 848): Deferral of the Sunset Date of Topic 848”. ASU 2022-06 extends the period of time preparers can utilize the reference rate reform relief guidance in Topic 848. The objective of the guidance in Topic 848 is to provide relief during the temporary transition period, so the FASB included a sunset provision within Topic 848 based on expectations of when LIBOR would cease being published. In 2021, the UK Financial Conduct Authority delayed the intended cessation date of certain tenors of LIBOR to June 30, 2023.

To ensure the relief in Topic 848 covers the period of time during which a significant number of modifications may take place, the ASU defers the sunset date of Topic 848 from December 31, 2022, to December 31, 2024, after which entities will no longer be permitted to apply the relief in Topic 848. The ASU is effective for all entities upon issuance. The Company is assessing ASU 2022-06 and its impact on the Company’s transition away from LIBOR.

In June 2022, the FASB issued ASU 2022-03, “Fair Value Measurement (Topic 820): Fair Value Measurement of Equity Securities Subject to Contractual Sale Restrictions”. ASU 2022-03 clarifies that a contractual restriction on the sale of an equity security is not

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considered part of the unit of account of the equity security and, therefore, is not considered in measuring fair value. The ASU is effective for fiscal years, including interim periods within those fiscal years, beginning after December 15, 2023. Early adoption is permitted. The Company does not expect the adoption of ASU 2022-03 to have a material impact on its consolidated financial statements.

### Recently Adopted Accounting Standards

#### *ASU 2016-13*

On January 1, 2023, the Company adopted ASU 2016-13 “Financial Instruments – Credit Losses (Topic 326): Measurement of Credit Losses on Financial Instruments” and related ASUs. Prior to adoption, the Company followed applicable GAAP and used an incurred loss model to estimate an allowance for loan losses and a liability for credit risk on unfunded commitments. The Company also used a methodology to determine whether securities in an unrealized loss position were other-than-temporarily impaired and whether credit risk was present.

ASU 2016-13 makes significant changes to the accounting for credit losses on financial instruments presented on an amortized cost basis and disclosures about them. The new current expected credit loss (“CECL”) impairment model requires an estimate of expected credit losses, measured over the contractual life of an instrument, which considers historical experience, current conditions and reasonable and supportable forecasts of future economic conditions. The standard provides significant flexibility and requires a high degree of judgment with regards to pooling financial assets with similar risk characteristics and adjusting the relevant historical loss information in order to develop an estimate of expected lifetime losses. ASU 2016-13 permits the use of estimation techniques that are practical and relevant to the Company’s circumstances, as long as they are applied consistently over time and faithfully estimate expected credit losses in accordance with the standard.

The Company applied the standard’s provisions as a cumulative-effect adjustment of \$2,014, net of tax, to retained earnings as of January 1, 2023. On the adoption date, the allowance for credit losses (“ACL”) on loans increased from \$8,225 to \$10,567 and the ACL for unfunded commitments increased from \$35 to \$242. Based upon the nature and characteristics of our securities portfolios (including issuer specific matters) at the adoption date, macroeconomic conditions and forecasts at that date, and other management judgments, adoption did not result in an ACL on securities available for sale. Results for reporting periods beginning after January 1, 2023 will be presented under Topic 326, while periods prior to January 1, 2023 will be reported in accordance with GAAP applicable for the time period. The following presents the Company’s policies governing determination of the ACL on its financial instruments.

#### ACL on Securities Available for Sale

The Company evaluates securities available for sale that are in an unrealized loss position on the reporting date. Securities are analyzed to determine whether the decline in the fair value below the amortized cost basis (impairment) is due to credit-related factors or noncredit-related factors. Any impairment that is not credit-related is recognized in other comprehensive income, net of applicable taxes. Credit-related impairment is recognized as an ACL on the Consolidated Balance Sheets, limited to the amount by which the amortized cost basis exceeds the fair value, with a corresponding adjustment to earnings. Both the ACL and the adjustment to net income may be subsequently reversed if conditions change. If the Company intends to sell an impaired security, or more likely than not will be required to sell such a security, before recovering its amortized cost basis, the entire impairment amount must be recognized in earnings with a corresponding adjustment to the security’s amortized cost basis. Because the security’s amortized cost basis would be adjusted to fair value, there would be no ACL in this situation.

In evaluating impairment, the Company considers whether the securities are issued by the federal government or its agencies, whether downgrades by bond rating agencies have occurred, and the results of reviews of the issuers’ financial condition, among other factors. If the Company determines a credit impairment, the ACL on securities available for sale would be established through a provision for credit losses on securities available for sale in the Consolidated Statements of Income. If Management believes it has confirmed that the loss on a security is uncollectible, or when either of the criteria regarding intent or requirement to sell is met, the loss is charged against the ACL. Accrued interest receivable is excluded from the estimate of credit losses.

#### ACL on Loans (“ACLL”)

The Company estimates the ACLL based on amortized cost basis, which is the amount at which the loan is originated, adjusted for net deferred fees or costs, collection of cash, and charge-offs. In the event that collection of principal becomes uncertain, the Company has policies in place to reverse accrued interest in a timely manner. Therefore, the Company has made a policy election to exclude accrued interest from the measurement of the ACLL. Intrinsic to the Company’s policy on estimating the ACLL are policies regarding loan pools, nonaccruals, past due status, collateral valuation, charge-offs and risk ratings. Please refer to the Company’s 2022 Form 10-K, Note 1: Summary of Significant Accounting Policies for additional information on these policies.

The Company measures expected credit losses on loans on a collective (pool) basis, when the loans share similar risk characteristics, such as collateral type and intended use, repayment source, and (if applicable) the borrower’s business model. The Company has identified the following pools of loans with similar risk characteristics for measuring expected credit losses:

Real Estate Construction	Commercial Non Real Estate
Construction, residential	Commercial and industrial
Construction, other	
	Public Sector and IDA
Consumer Real Estate	Public sector and IDA
Equity lines	
Residential closed-end first liens	Consumer Non Real Estate
Residential closed-end junior liens	Credit cards
Investor-owned residential real estate	Automobile
	Other consumer loans
Commercial Real Estate	
Multifamily real estate	
Commercial real estate, owner occupied	
Commercial real estate, other	

The Company's methodologies for estimating the ACLL consider available relevant information about the collectability of cash flows, including historical losses, reasonable and supportable forecasts of economic conditions, and current economic and portfolio conditions. The difference between cash flow estimates and amortized cost is the ACLL.

The Company uses a discounted cash flow ("DCF") method for all of its pools except for bankcards, which are measured using the historical loss rate adjusted for the forecast. For loans using the DCF method, cash flows are projected at the instrument level and discounted using the loan's effective interest rate. Cash flows are generated using each loan's payment attributes, adjusted for pool-level information on the probability of default ("PD"), loss given default and prepayment speeds. Default is defined as full or partial charge-off, nonaccrual status or past due 90 days or more. PDs for each pool are calculated using the Company's historical data, modified by peer data, to ensure a full economic cycle is reflected in the estimate. PDs are then adjusted for the forecast.

The Company designated national unemployment as its forecast variable. Multiple forecasts from reputable and independent third parties are sourced to inform the Company's reasonable and supportable forecasting of current expected credit losses. The forecast is applied over a horizon selected by Management at each reporting date, typically of one year and not to exceed two years, after which loss rates revert to long term historical loss experience on a straight line basis over a period determined by Management, of up to three years. The forecast horizon and reversion period are applied consistently to the entire portfolio.

The results of DCF calculations are modified by allocations for qualitative factors to account for changes in variables that may affect credit risk. The Company considers and allocates for changes in lending policies, Management experience, economic conditions, loans past due, competitive, legal and regulatory environments and other factors. Qualitative factors are benchmarked to historical data and are adjusted based upon quantitative analysis.

Loans that do not share risk characteristics are evaluated on an individual basis. The Company designates loans that have been determined to meet the regulatory definitions of "special mention" or "classified" (together known as "criticized") as individually evaluated. The fair value of individually evaluated loans is measured using the fair value of collateral ("collateral method") or the DCF method.

The collateral method is applied to individually evaluated loans for which foreclosure is probable. The collateral method is also applied to individually evaluated loans when borrowers are experiencing financial difficulty and repayment is expected to be provided substantially through the operation or sale of the collateral ("collateral dependent"). The ACLL is measured based on the difference between the fair value of the collateral and the amortized cost basis of the loan as of the measurement date. When repayment is expected to be from the operation of the collateral, the ACLL is calculated as the amount by which the amortized cost basis of the loan exceeds the present value of expected cash flows from the operation of the collateral. When repayment is expected to be from the sale of the collateral, the ACLL is calculated as the amount by which the loan's amortized cost basis exceeds the fair value of the underlying collateral less estimated cost to sell. The ACLL may be zero if the fair value of the collateral at the measurement date exceeds the amortized cost basis of the loan.

The DCF method is applied to individually evaluated loans that do not meet the criteria for collateral method measurement. Cash flows are projected and discounted using the same method as for collectively evaluated loans, but the PD is increased to reflect increased risk, up to 100% for nonaccrual loans.

Expected credit losses are reflected in the ACLL through a charge to provision for credit losses on the Consolidated Statements of Income. When the Company deems all or a portion of a loan to be uncollectible the appropriate amount is written off against the ACLL. The Company applies judgment to determine when a financial asset is deemed uncollectible; however, generally speaking, an asset will be considered uncollectible no later than when all efforts at collection have been exhausted. Subsequent recoveries, if any, are credited to the ACLL when received.

#### ACL on Unfunded Commitments

Financial instruments include off-balance sheet credit instruments such as undrawn portions of revolving lines of credit, commercial letters of credit, and loan commitments that have not yet been funded. The contractual amount of those instruments represents the

Company's exposure to credit loss in the event of nonperformance by the borrower. The Company records an ACL on unfunded commitments, unless the commitments to extend credit are unconditionally cancelable. The estimate includes consideration of the likelihood that funding will occur, which is based on a historical funding study derived from internal information, and an estimate of expected credit losses on commitments expected to be funded over its estimated life, which are the same loss rates that are used in computing the ACLL. The ACL on unfunded commitments is recorded as a liability on the Company's Consolidated Balance Sheets, included in other liabilities, and is adjusted through the provision for credit loss expense in the Company's Consolidated Statements of Income.

*ASU 2022-02*

On January 1, 2023, concurrent with its adoption of ASU 2016-13, the Company adopted ASU 2022-02, "Financial Instruments-Credit Losses (Topic 326), Troubled Debt Restructurings and Vintage Disclosures." The amendments eliminate the accounting guidance for troubled debt restructurings ("TDRs") by creditors that have adopted the CECL model and enhance the disclosure requirements for loan refinancings and restructurings made with borrowers experiencing financial difficulty. Disclosures about periods prior to adoption will be presented under GAAP applicable for that period.

Similar to its policy under previous GAAP, the Company continues to identify modifications to loans and to determine whether the borrower is experiencing financial difficulty. If the Company determines that the borrower is experiencing financial difficulty, the loan's risk rating is evaluated to determine whether it falls within the regulatory definition of "criticized" and requires individual evaluation. Under previous GAAP, modifications to loans when the borrower was experiencing financial difficulty were designated as TDR and were individually evaluated for the duration of the loan. Under CECL, if a previously modified loan with financial difficulty is subsequently upgraded to a pass rating, it will no longer be individually evaluated.

**Note 2: Loans and Allowance for Credit Losses**

Loans

The loan portfolio, excluding mortgage loans held for sale, was comprised of the following.

	<b>March 31, 2023</b>	<b>December 31, 2022</b>
Real estate construction	\$ 54,052	\$ 54,579
Consumer real estate	223,438	221,052
Commercial real estate	438,843	437,888
Commercial non real estate	60,516	57,652
Public sector and IDA	47,359	48,074
Consumer non real estate	33,188	33,948
Gross loans	857,396	853,193
Less unearned income and deferred fees and costs	(431)	(449)
Loans, net of unearned income and deferred fees and costs	\$ 856,965	\$ 852,744
Allowance for credit losses on loans	(10,650)	(8,225)
Total loans, net	\$ 846,315	\$ 844,519

Accrued interest receivable on loans, which is excluded from the amortized cost of loans, totaled \$2,558 and \$2,516 at March 31, 2023 and December 31, 2022, respectively.

## Past Due and Nonaccrual Loans

The following tables present the aging of past due loans, by loan pool, as of the dates indicated.

	March 31, 2023					
	Accruing Current Loans	Accruing Loans 30 – 89 Days Past Due	Accruing Loans 90 or More Days Past Due	Nonaccrual Loans	Total Loans	Accruing and Nonaccrual 90 or More Days Past Due
<b>Real Estate Construction</b>						
Construction, 1-4 family residential	\$ 13,143	\$ -	\$ -	\$ -	\$ 13,143	\$ -
Construction, other	40,909	-	-	-	40,909	-
<b>Consumer Real Estate</b>						
Equity line	14,503	23	-	-	14,526	-
Residential closed-end first liens	121,466	836	27	90	122,419	117
Residential closed-end junior liens	2,476	-	-	-	2,476	-
Investor-owned residential real estate	83,924	93	-	-	84,017	-
<b>Commercial Real Estate</b>						
Multifamily residential real estate	131,952	-	-	-	131,952	-
Commercial real estate owner-occupied	124,882	8	-	2,472	127,362	247
Commercial real estate, other	179,529	-	-	-	179,529	1
<b>Commercial Non Real Estate</b>						
Commercial and industrial	60,201	62	1	252	60,516	-
<b>Public Sector and IDA</b>						
States and political subdivisions	47,359	-	-	-	47,359	-
<b>Consumer Non-Real Estate</b>						
Credit cards	4,557	5	1	-	4,563	1
Automobile	10,328	75	-	-	10,403	-
Other consumer loans	18,146	72	4	-	18,222	4
<b>Total</b>	<b>\$ 853,375</b>	<b>\$ 1,174</b>	<b>\$ 33</b>	<b>\$ 2,814</b>	<b>\$ 857,396</b>	<b>\$ 370</b>

December 31, 2022

	Accruing Current Loans	Accruing Loans 30 – 89 Days Past Due	Accruing Loans 90 or More Days Past Due	Nonaccrual Loans	Total Loans	Accruing and Nonaccrual 90 or More Days Past Due
<b>Real Estate Construction</b>						
Construction, 1-4 family residential	\$ 12,538	\$ -	\$ -	\$ -	\$ 12,538	\$ -
Construction, other	42,041	-	-	-	42,041	-
<b>Consumer Real Estate</b>						
Equity line	15,010	16	-	-	15,026	-
Residential closed-end first liens	121,807	750	-	91	122,648	91
Residential closed-end junior liens	2,446	-	-	-	2,446	-
Investor-owned residential real estate	80,524	408	-	-	80,932	-
<b>Commercial Real Estate</b>						
Multifamily residential real estate	127,312	-	-	-	127,312	-
Commercial real estate owner-occupied	126,640	-	-	2,493	129,133	252
Commercial real estate, other	181,443	-	-	-	181,443	-
<b>Commercial Non Real Estate</b>						
Commercial and industrial	57,373	16	-	263	57,652	-
<b>Public Sector and IDA</b>						
States and political subdivisions	48,074	-	-	-	48,074	-
<b>Consumer Non-Real Estate</b>						
Credit cards	4,592	3	2	-	4,597	2
Automobile	9,833	102	-	-	9,935	-
Other consumer loans	19,317	93	6	-	19,416	6
<b>Total</b>	<b>\$ 848,950</b>	<b>\$ 1,388</b>	<b>\$ 8</b>	<b>\$ 2,847</b>	<b>\$ 853,193</b>	<b>\$ 351</b>

The following table presents nonaccrual loans, by loan class, as of the dates indicated:

	CECL			Incurred Loss
	March 31, 2023			December 31, 2022
	Nonaccrual Loans			Nonaccrual Loans
	With No Allowance	With an Allowance	Total	
<b>Consumer Real Estate</b>				
Residential closed-end first liens	\$ -	\$ 90	\$ 90	\$ 91
<b>Commercial Real Estate</b>				
Commercial real estate owner-occupied	-	2,472	2,472	2,493
<b>Commercial Non Real Estate</b>				
Commercial and industrial	-	252	252	263
<b>Total</b>	<b>\$ -</b>	<b>\$ 2,814</b>	<b>\$ 2,814</b>	<b>\$ 2,847</b>

During the three months ended March 31, 2023, no accrued interest receivable was reversed against interest income.

The following table presents certain past due indicators as of the dates indicated.

	March 31,		December 31,
	2023	2022	2022
Ratio of ACLL to nonaccrual loans	378.46 %	272.12%	288.90 %
Ratio of loans past due 90 days or more and still accruing to loans, net of unearned income and deferred fees and costs	0.00 %	0.05%	0.00 %

Allowance for Credit Losses on Loans

The activity in the ACLL by portfolio segment follows:

**Activity in the Allowance for Credit Losses on Loans for the Three Months Ended March 31, 2023**

	Real Estate Construction	Consumer Real Estate	Commercial Real Estate	Commercial Non Real Estate	Public Sector and IDA	Consumer Non Real Estate	Unallocated	Total
Balance, Dec. 31, 2022	\$ 450	\$ 2,199	\$ 3,642	\$ 930	\$ 319	\$ 506	\$ 179	\$ 8,225
Adoption of ASU 2016-13	(21)	1,261	700	216	(15)	72	129	2,342
Charge-offs	-	-	-	(12)	-	(80)	-	(92)
Recoveries	-	102	12	2	-	57	-	173
Provision for (recovery of) credit losses	22	(260)	20	58	(10)	-	172	2
<b>Balance, March 31, 2023</b>	<b>\$ 451</b>	<b>\$ 3,302</b>	<b>\$ 4,374</b>	<b>\$ 1,194</b>	<b>\$ 294</b>	<b>\$ 555</b>	<b>\$ 480</b>	<b>\$ 10,650</b>

**Activity in the Allowance for Loan Losses for the Three Months Ended March 31, 2022**

	Real Estate Construction	Consumer Real Estate	Commercial Real Estate	Commercial Non Real Estate	Public Sector and IDA	Consumer Non Real Estate	Unallocated	Total
Balance, Dec. 31, 2021	\$ 422	\$ 1,930	\$ 3,121	\$ 1,099	\$ 297	\$ 444	\$ 361	\$ 7,674
Charge-offs	-	-	-	-	-	(60)	-	(60)
Recoveries	-	-	12	3	-	25	-	40
Provision for (recovery of) loan losses	171	5	290	(158)	10	6	(190)	134
<b>Balance, March, 31, 2022</b>	<b>\$ 593</b>	<b>\$ 1,935</b>	<b>\$ 3,423</b>	<b>\$ 944</b>	<b>\$ 307</b>	<b>\$ 415</b>	<b>\$ 171</b>	<b>\$ 7,788</b>

**Activity in the Allowance for Loan Losses for the Year Ended December 31, 2022**

	Real Estate Construction	Consumer Real Estate	Commercial Real Estate	Commercial Non Real Estate	Public Sector and IDA	Consumer Non Real Estate	Unallocated	Total
Balance, Dec. 31, 2021	\$ 422	\$ 1,930	\$ 3,121	\$ 1,099	\$ 297	\$ 444	\$ 361	\$ 7,674
Charge-offs	-	(13)	-	(2)	-	(352)	-	(367)
Recoveries	-	29	49	11	-	123	-	212
Provision for (recovery of) loan losses	28	253	472	(178)	22	291	(182)	706
<b>Balance, Dec. 31, 2022</b>	<b>\$ 450</b>	<b>\$ 2,199</b>	<b>\$ 3,642</b>	<b>\$ 930</b>	<b>\$ 319</b>	<b>\$ 506</b>	<b>\$ 179</b>	<b>\$ 8,225</b>

Information about the ACLL for individually evaluated loans and collectively evaluated loans by portfolio segment follows.

**Allowance for Credit Losses on Loans as of March 31, 2023**

	Real Estate Construction	Consumer Real Estate	Commercial Real Estate	Commercial Non Real Estate	Public Sector and IDA	Consumer Non Real Estate	Unallocated	Total
Individually evaluated	\$ 1	\$ 84	\$ 201	\$ 148	\$ -	\$ -	\$ -	\$ 434
Collectively evaluated	450	3,218	4,173	1,046	294	555	480	10,216
<b>Total</b>	<b>\$ 451</b>	<b>\$ 3,302</b>	<b>\$ 4,374</b>	<b>\$ 1,194</b>	<b>\$ 294</b>	<b>\$ 555</b>	<b>\$ 480</b>	<b>\$ 10,650</b>

**Allowance for Loan Losses as of December 31, 2022**

	Real Estate Construction	Consumer Real Estate	Commercial Real Estate	Commercial Non Real Estate	Public Sector and IDA	Consumer Non- Real Estate	Unallocated	Total
Individually evaluated	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -
Collectively evaluated	450	2,199	3,642	930	319	506	179	8,225
<b>Total</b>	<b>\$ 450</b>	<b>\$ 2,199</b>	<b>\$ 3,642</b>	<b>\$ 930</b>	<b>\$ 319</b>	<b>\$ 506</b>	<b>\$ 179</b>	<b>\$ 8,225</b>

Information about individually evaluated loans and collectively evaluated loans by portfolio segment follows.

**Loans as of March 31, 2023**

	Real Estate Construction	Consumer Real Estate	Commercial Real Estate	Commercial Non Real Estate	Public Sector and IDA	Consumer Non Real Estate	Total
Individually evaluated	\$ 294	\$ 1,061	\$ 2,480	\$ 295	\$ -	\$ -	\$ 4,130
Collectively evaluated	53,758	222,377	436,363	60,221	47,359	33,188	853,266
<b>Total</b>	<b>\$ 54,052</b>	<b>\$ 223,438</b>	<b>\$ 438,843</b>	<b>\$ 60,516</b>	<b>\$ 47,359</b>	<b>\$ 33,188</b>	<b>\$ 857,396</b>

**Loans as of December 31, 2022**

	Real Estate Construction	Consumer Real Estate	Commercial Real Estate	Commercial Non Real Estate	Public Sector and IDA	Consumer Non- Real Estate	Total
Individually evaluated	\$ -	\$ 186	\$ 2,583	\$ 263	\$ -	\$ -	\$ 3,032
Collectively evaluated	54,579	220,866	435,305	57,389	48,074	33,948	850,161
<b>Total</b>	<b>\$ 54,579</b>	<b>\$ 221,052</b>	<b>\$ 437,888</b>	<b>\$ 57,652</b>	<b>\$ 48,074</b>	<b>\$ 33,948</b>	<b>\$ 853,193</b>

A summary of ratios pertaining to the ACLL follows.

	As of and for the		
	Three Months Ended March 31, 2023	2022	Year Ended December 31, 2022
Ratio of ACLL to the end of period loans, net of unearned income and deferred fees and costs	1.24 %	0.95%	0.96 %
Ratio of net charge-offs (recoveries), annualized, to average loans, net of unearned income and deferred fees and costs	(0.04) %	0.01%	0.02 %



In accordance with CECL, the Company identifies individually evaluated loans when their risk characteristics become different from their pool. Under previous GAAP, the Company identified loans for potential impairment through a variety of means, including, but not limited to, ongoing loan review, renewal processes, delinquency data, market communications, and public information. When the Company determined that it was probable all principal and interest amounts due would not be collected in accordance with the contractual terms of the loan agreement, the loan was generally deemed impaired and individually evaluated. For further information on the impairment process under previous GAAP, please refer to the Company's 2022 Annual Report on Form 10-K. A summary of individually evaluated loans for the dates indicated follows.

**Individually Evaluated Loans under Incurred Loss as of December 31, 2022**

	Principal Balance	Recorded Investment <sup>(1)</sup>	Recorded Investment <sup>(1)</sup> for Which There is No Related Allowance	Recorded Investment <sup>(1)</sup> for Which There is a Related Allowance	Related Allowance
<b>Consumer Real Estate</b>					
Investor-owned residential real estate	\$ 186	\$ 186	\$ 186	\$ -	\$ -
<b>Commercial Real Estate</b>					
Commercial real estate, owner occupied	3,248	2,583	2,583	-	-
<b>Commercial Non Real Estate</b>					
Commercial and industrial	285	263	263	-	-
<b>Total</b>	<b>\$ 3,719</b>	<b>\$ 3,032</b>	<b>\$ 3,032</b>	<b>\$ -</b>	<b>\$ -</b>

(1) Recorded investment is net of charge-offs and interest paid while a loan is in nonaccrual status.

The following table shows the average recorded investment and interest income recognized for individually evaluated loans under the incurred loss model for the period indicated. Only classes with individually evaluated loans are presented.

	<b>For the Three Months Ended March 31, 2022</b>	
	Average Recorded Investment <sup>(1)</sup>	Interest Income Recognized
<b>Consumer Real Estate</b>		
Investor-owned residential real estate	\$ 190	\$ 3
<b>Commercial Real Estate</b>		
Commercial real estate, owner occupied	2,640	1
Commercial real estate, other	2,720	17
<b>Commercial Non-Real Estate</b>		
Commercial and industrial	292	-
<b>Total</b>	<b>\$ 5,842</b>	<b>\$ 21</b>

(1) Recorded investment is net of charge-offs and interest paid while a loan is in nonaccrual status.

**Collateral Dependent Loans**

The Company reviews individually evaluated loans for collateral dependency. As of March 31, 2023, none of the Company's individually evaluated loans were considered collateral dependent.

## Credit Quality

The Company categorizes loans by risk based on relevant information about the ability of borrowers to service their debt, including: collateral and financial information, historical payment experience, credit documentation and current economic trends, among other factors. At origination, each loan is assigned a risk rating. Ongoing analysis of the loan portfolio adjusts risk ratings on an individual loan basis to reflect updated information. General descriptions of risk ratings are as follows:

- Pass: loans with acceptable credit quality are rated pass.
- Special mention: loans with potential weaknesses due to challenging economic or financial conditions are rated special mention.
- Classified: loans with well-defined weaknesses that heighten the risk of default are rated classified.

The following tables present the amortized cost basis of the loan portfolio, by year of origination, loan class, and credit quality, as of the date indicated.

Balance at March 31, 2023	Term Loans Amortized Cost Basis by Origination Year						Prior	Revolving	Revolving Loans Converted to Term	Total
	2019	2020	2021	2022	2023					
<b>Construction, residential</b>										
Pass	\$ -	\$ 213	\$ 1,370	\$ 5,000	\$ 554	\$ -	\$ 6,006	\$ -	\$ 13,143	
Classified	-	-	-	-	-	-	-	-	-	
Total	\$ -	\$ 213	\$ 1,370	\$ 5,000	\$ 554	\$ -	\$ 6,006	\$ -	\$ 13,143	
<b>Construction, other</b>										
Pass	\$ 1,253	\$ 1,502	\$ 26,880	\$ 5,229	\$ 1,573	\$ 2,807	\$ 1,371	\$ -	\$ 40,615	
Classified	-	-	294	-	-	-	-	-	294	
Total	\$ 1,253	\$ 1,502	\$ 27,174	\$ 5,229	\$ 1,573	\$ 2,807	\$ 1,371	\$ -	\$ 40,909	
<b>Equity lines</b>										
Pass	\$ -	\$ -	\$ -	\$ -	\$ -	\$ 53	\$ 14,465	\$ 8	\$ 14,526	
Classified	-	-	-	-	-	-	-	-	-	
Total	\$ -	\$ -	\$ -	\$ -	\$ -	\$ 53	\$ 14,465	\$ 8	\$ 14,526	
<b>Residential closed-end first liens</b>										
Pass	\$ 6,191	\$ 15,467	\$ 32,829	\$ 27,691	\$ 4,381	\$ 35,532	\$ -	\$ -	\$ 122,091	
Classified	-	27	-	-	-	301	-	-	328	
Total	\$ 6,191	\$ 15,494	\$ 32,829	\$ 27,691	\$ 4,381	\$ 35,833	\$ -	\$ -	\$ 122,419	
<b>Residential closed-end junior liens</b>										
Pass	\$ 7	\$ -	\$ 87	\$ 405	\$ 82	\$ 1,895	\$ -	\$ -	\$ 2,476	
Classified	-	-	-	-	-	-	-	-	-	
Total	\$ 7	\$ -	\$ 87	\$ 405	\$ 82	\$ 1,895	\$ -	\$ -	\$ 2,476	
<b>Investor-owned residential real estate</b>										
Pass	\$ 5,379	\$ 15,052	\$ 20,412	\$ 14,414	\$ 2,301	\$ 24,079	\$ 1,547	\$ 100	\$ 83,284	
Classified	-	-	-	-	-	733	-	-	733	
Total	\$ 5,379	\$ 15,052	\$ 20,412	\$ 14,414	\$ 2,301	\$ 24,812	\$ 1,547	\$ 100	\$ 84,017	
<b>Multifamily residential real estate</b>										
Pass	\$ 1,856	\$ 11,973	\$ 41,285	\$ 27,249	\$ 4,851	\$ 44,731	\$ 7	\$ -	\$ 131,952	
Classified	-	-	-	-	-	-	-	-	-	
Total	\$ 1,856	\$ 11,973	\$ 41,285	\$ 27,249	\$ 4,851	\$ 44,731	\$ 7	\$ -	\$ 131,952	
<b>Commercial real estate, owner occupied</b>										
Pass	\$ 19,563	\$ 24,191	\$ 5,088	\$ 16,648	\$ 1,899	\$ 54,991	\$ 2,452	50	\$ 124,882	
Classified	-	-	-	-	-	2,480	-	-	2,480	
Total	\$ 19,563	\$ 24,191	\$ 5,088	\$ 16,648	\$ 1,899	\$ 57,471	\$ 2,452	50	\$ 127,362	
<b>Commercial real estate, other</b>										
Pass	\$ 22,410	\$ 19,838	\$ 36,961	\$ 23,541	\$ 262	\$ 76,142	\$ 375	\$ -	\$ 179,529	
Classified	-	-	-	-	-	-	-	-	-	
Total	\$ 22,410	\$ 19,838	\$ 36,961	\$ 23,541	\$ 262	\$ 76,142	\$ 375	\$ -	\$ 179,529	
<b>Commercial and industrial</b>										
Pass	\$ 1,064	\$ 10,123	\$ 15,106	\$ 8,959	\$ 2,258	\$ 6,691	\$ 16,020	\$ -	\$ 60,221	
Classified	36	-	-	7	-	252	-	-	295	
Total	\$ 1,100	\$ 10,123	\$ 15,106	\$ 8,966	\$ 2,258	\$ 6,943	\$ 16,020	\$ -	\$ 60,516	
YTD gross charge-offs	\$ 12	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ 12	

<b>Public sector and IDA</b>																		
Pass	\$	42	\$	247	\$	18,419	\$	6,650	\$	-	\$	22,001	\$	-	\$	-	\$	47,359
Classified		-		-		-		-		-		-		-		-		-
<b>Total</b>	<b>\$</b>	<b>42</b>	<b>\$</b>	<b>247</b>	<b>\$</b>	<b>18,419</b>	<b>\$</b>	<b>6,650</b>	<b>\$</b>	<b>-</b>	<b>\$</b>	<b>22,001</b>	<b>\$</b>	<b>-</b>	<b>\$</b>	<b>-</b>	<b>\$</b>	<b>47,359</b>
<b>Credit cards</b>																		
Pass	\$	-	\$	-	\$	-	\$	-	\$	-	\$	-	\$	4,563	\$	-	\$	4,563
Classified		-		-		-		-		-		-		-		-		-
<b>Total</b>	<b>\$</b>	<b>-</b>	<b>\$</b>	<b>-</b>	<b>\$</b>	<b>-</b>	<b>\$</b>	<b>-</b>	<b>\$</b>	<b>-</b>	<b>\$</b>	<b>-</b>	<b>\$</b>	<b>4,563</b>	<b>\$</b>	<b>-</b>	<b>\$</b>	<b>4,563</b>
YTD gross charge-offs	\$	-	\$	-	\$	-	\$	-	\$	-	\$	-	\$	8	\$	-	\$	8
<b>Automobile</b>																		
Pass	\$	519	\$	1,119	\$	2,453	\$	4,255	\$	1,884	\$	173	\$	-	\$	-	\$	10,403
Classified		-		-		-		-		-		-		-		-		-
<b>Total</b>	<b>\$</b>	<b>519</b>	<b>\$</b>	<b>1,119</b>	<b>\$</b>	<b>2,453</b>	<b>\$</b>	<b>4,255</b>	<b>\$</b>	<b>1,884</b>	<b>\$</b>	<b>173</b>	<b>\$</b>	<b>-</b>	<b>\$</b>	<b>-</b>	<b>\$</b>	<b>10,403</b>
YTD gross charge-offs	\$	-	\$	-	\$	1	\$	30	\$	-	\$	-	\$	-	\$	-	\$	31
<b>Other consumer</b>																		
Pass	\$	543	\$	1,412	\$	3,245	\$	9,416	\$	2,577	\$	174	\$	855	\$	-	\$	18,222
Classified		-		-		-		-		-		-		-		-		-
<b>Total</b>	<b>\$</b>	<b>543</b>	<b>\$</b>	<b>1,412</b>	<b>\$</b>	<b>3,245</b>	<b>\$</b>	<b>9,416</b>	<b>\$</b>	<b>2,577</b>	<b>\$</b>	<b>174</b>	<b>\$</b>	<b>855</b>	<b>\$</b>	<b>-</b>	<b>\$</b>	<b>18,222</b>
YTD gross charge-offs	\$	-	\$	-	\$	6	\$	13	\$	-	\$	-	\$	22	\$	-	\$	41
<b>Total Loans</b>																		
Pass	\$	58,826	\$	101,136	\$	204,134	\$	149,458	\$	22,622	\$	273,833	\$	43,098	\$	159	\$	853,266
Classified		36		27		294		7		-		3,766		-		-		4,130
<b>Total</b>	<b>\$</b>	<b>58,862</b>	<b>\$</b>	<b>101,163</b>	<b>\$</b>	<b>204,428</b>	<b>\$</b>	<b>149,465</b>	<b>\$</b>	<b>22,622</b>	<b>\$</b>	<b>277,599</b>	<b>\$</b>	<b>43,098</b>	<b>\$</b>	<b>159</b>	<b>\$</b>	<b>857,396</b>
YTD gross charge-offs	\$	12	\$	-	\$	7	\$	43	\$	-	\$	-	\$	30	\$	-	\$	92

The following table presents the recorded investment by loan pool and credit quality as of December 31, 2022.

	December 31, 2022		
	Pass	Special Mention	Classified
<b>Real Estate Construction</b>			
Construction, 1-4 family residential	\$ 12,538	\$ -	\$ -
Construction, other	41,741	-	300
<b>Consumer Real Estate</b>			
Equity lines	15,026	-	-
Residential closed-end first liens	122,187	-	461
Residential closed-end junior liens	2,446	-	-
Investor-owned residential real estate	80,143	-	603
<b>Commercial Real Estate</b>			
Multifamily residential real estate	127,312	-	-
Commercial real estate owner-occupied	126,550	-	-
Commercial real estate, other	181,443	-	-
<b>Commercial Non Real Estate</b>			
Commercial and industrial	57,381	-	8
<b>Public Sector and IDA</b>			
States and political subdivisions	48,074	-	-
<b>Consumer Non-Real Estate</b>			
Credit cards	4,597	-	-
Automobile	9,932	-	3
Other consumer	19,398	-	18
<b>Total</b>	<b>\$ 848,768</b>	<b>\$ -</b>	<b>\$ 1,393</b>

### Loan Modifications to Borrowers Experiencing Financial Difficulty

There were no loans to borrowers experiencing financial difficulty that were modified during the three months ended March 31, 2023. The Company analyzed its modified loan portfolio for loans that defaulted during the three month period ended March 31, 2023, and that were modified within 12 months prior to default. The Company designates three circumstances that indicate default: one or more payments that occur more than 90 days past the due date, charge-off, or foreclosure after the date of modification. Of the Company's modifications at March 31, 2023, none of the defaulted modifications were modified within 12 months prior to default.

### ACL on Unfunded Commitments

The following table presents the balance and activity in the ACL for unfunded commitments for the three months ended March 31, 2023:

<b>Allowance for Credit Losses on Unfunded Commitments</b>	
Balance, December 31, 2022	\$ 35
Adoption of ASU 2016-13	207
Provision for credit losses	-
<b>Balance, March 31, 2023</b>	<b>\$ 242</b>

### **Note 3: Securities**

The amortized cost and estimated fair value of securities available for sale along with gross unrealized gains and losses are summarized as follows:

	<b>March 31, 2023</b>				
	<b>Amortized Cost</b>	<b>Gross Unrealized Gains</b>	<b>Gross Unrealized Losses</b>	<b>Allowance for Credit Losses</b>	<b>Fair Value</b>
<b>Available for Sale:</b>					
U.S. Treasuries	\$ 993	\$ -	\$ 46	\$ -	\$ 947
U.S. Government agencies and corporations	382,592	-	48,648	-	333,944
States and political subdivisions	181,214	3	31,255	-	149,962
Mortgage-backed securities	167,964	-	7,511	-	160,453
Corporate debt securities	6,502	-	761	-	5,741
<b>Total securities available for sale</b>	<b>\$ 739,265</b>	<b>\$ 3</b>	<b>\$ 88,221</b>	<b>\$ -</b>	<b>\$ 651,047</b>

	<b>December 31, 2022</b>				
	<b>Amortized Cost</b>	<b>Gross Unrealized Gains</b>	<b>Gross Unrealized Losses</b>	<b>Fair Value</b>	
<b>Available for Sale:</b>					
U.S. Treasuries	\$ 992	\$ -	\$ 56	\$	936
U.S. Government agencies and corporations	391,538	39	55,002	\$	336,575
States and political subdivisions	190,192	26	38,018	\$	152,200
Mortgage-backed securities	170,694	22	9,239	\$	161,477
Corporate debt securities	6,501	-	837	\$	5,664
<b>Total securities available for sale</b>	<b>\$ 759,917</b>	<b>\$ 87</b>	<b>\$ 103,152</b>	<b>\$</b>	<b>\$ 656,852</b>

No allowance for credit loss on securities available for sale was recorded as of March 31, 2023.

The deferred tax asset for the net unrealized loss on securities available for sale was \$18,526 as of March 31, 2023 and \$21,644 as of December 31, 2022. The deferred tax asset is included in other assets on the Consolidated Balance Sheets.

The amortized cost and fair value of single maturity securities available for sale at March 31, 2023, by contractual maturity, are shown below. Expected maturities may differ from contractual maturities because borrowers may have the right to call or prepay obligations with or without call or prepayment penalties. Mortgage-backed securities included in these totals are categorized by final maturity.

	March 31, 2023	
	Amortized Cost	Fair Value
<b>Available for Sale:</b>		
Due in one year or less	\$ 3,229	\$ 3,172
Due after one year through five years	148,141	138,200
Due after five years through ten years	316,859	273,664
Due after ten years	271,036	236,011
<b>Total securities available for sale</b>	<b>\$ 739,265</b>	<b>\$ 651,047</b>

Information pertaining to securities with gross unrealized losses aggregated by investment category and length of time that the individual securities have been in a continuous loss position, follows.

	March 31, 2023			
	Less Than 12 Months		12 Months or More	
	Fair Value	Unrealized Loss	Fair Value	Unrealized Loss
U.S. Treasuries	\$ -	\$ -	\$ 947	\$ 46
U.S. Government agencies and corporations	50,869	2,032	283,074	46,616
States and political subdivisions	9,432	1,214	139,371	30,041
Mortgage-backed securities	18,576	242	141,868	7,269
Corporate debt securities	873	127	4,868	634
<b>Total available for sale securities</b>	<b>\$ 79,750</b>	<b>\$ 3,615</b>	<b>\$ 570,128</b>	<b>\$ 84,606</b>

	December 31, 2022			
	Less Than 12 Months		12 Months or More	
	Fair Value	Unrealized Loss	Fair Value	Unrealized Loss
U.S. Treasuries	\$ 936	\$ 56	\$ -	\$ -
U.S. Government agencies and corporations	144,574	12,699	190,950	42,303
States and political subdivisions	94,657	18,373	52,134	19,645
Mortgage-backed securities	144,198	7,326	15,165	1,913
Corporate debt securities	4,843	655	821	182
<b>Total temporarily impaired securities</b>	<b>\$ 389,208</b>	<b>\$ 39,109</b>	<b>\$ 259,070</b>	<b>\$ 64,043</b>

The Company evaluates securities available for sale that are in unrealized loss positions to determine whether the impairment is due to credit-related factors or noncredit-related factors. Consideration is given to the extent to which the fair value is less than cost, the financial condition and near-term prospects of the issuer, and the intent and ability of the Company to retain its investment in the security for a period of time sufficient to allow for any anticipated recovery in fair value.

At March 31, 2023, the Company had 602 securities with a fair value of \$649,878 in an unrealized loss position. The Company does not have the intent to sell any of these securities and believes that it is more likely than not that the Company will not have to sell any such securities before a recovery of cost. The contractual terms of the investments do not permit the issuers to settle the securities at a price less than the cost basis of the investments. The fair value is expected to recover as the securities approach their maturity date or repricing date or if market yields for such investments decline. Accordingly, the unrealized losses are attributed to noncredit-related factors, including changes in interest rates and other market conditions. No allowance for credit losses on securities available for sale was recorded as of March 31, 2023.

### Restricted Stock

The Company held restricted stock of \$929 as of March 31, 2023 and \$941 at December 31, 2022. Restricted stock is reported separately from available for sale securities. As a member of the Federal Reserve and the Federal Home Loan Bank of Atlanta (“FHLB”), NBB is required to maintain certain minimum investments in the common stock of those entities. Required levels of investment are based upon NBB’s capital and a percentage of qualifying assets. The Company purchases stock from or sells stock back to the correspondents based on their calculations. The stock is held by member institutions only and is not actively traded.

Redemption of FHLB stock is subject to certain limitations and conditions. At its discretion, the FHLB may declare dividends on the stock. In addition to dividends, NBB also benefits from its membership with FHLB through eligibility to borrow from the FHLB, using as collateral NBB’s capital stock investment in the FHLB and qualifying NBB real estate mortgage loans totaling \$646,100 at March 31, 2023. Management reviews for impairment based upon the ultimate recoverability of the cost basis of the FHLB stock, and at March 31, 2023, did not determine any impairment.

### Realized Securities Gains and Losses

During the first three months of 2023, the Company realized net securities gains of \$12 on the sale of securities with an amortized cost basis of \$17,987. The sales were part of the Company’s interest rate risk management strategy. There were no sales of securities during 2022.

### **Note 4: Defined Benefit Plan**

Components of Net Periodic Benefit Cost:

	<b>Pension Benefits</b>	
	<b>Three Months Ended March 31,</b>	
	<b>2023</b>	<b>2022</b>
Service cost	\$ 203	\$ 324
Interest cost	273	204
Expected return on plan assets	(518)	(629)
Amortization of prior service cost	-	-
Recognized net actuarial loss	17	110
Net periodic benefit (income) cost	\$ (25)	\$ 9

The service cost component of net periodic benefit cost is included in salaries and employee benefits expense in the Consolidated Statements of Income. All other components are included in other noninterest expense in the Consolidated Statements of Income. For the three months ended March 31, 2023, the Company did not make a contribution to the defined benefit plan.

### **Note 5: Fair Value Measurements**

Fair value is defined as the exchange price that would be received for an asset or paid to transfer a liability (an exit price) in the principal or most advantageous market for the asset or liability in an orderly transaction between market participants on the measurement date. GAAP requires that valuation techniques maximize the use of the observable inputs and minimize the use of the unobservable inputs. GAAP also establishes a fair value hierarchy which prioritizes the valuation inputs into three broad levels. Based on the underlying inputs, each fair value measurement in its entirety is reported in one of the three levels. These levels are:

Level 1 – Valuation is based on quoted prices in active markets for identical assets and liabilities.

Level 2 – Valuation is based on observable inputs including:

- quoted prices in active markets for similar assets and liabilities,
- quoted prices for identical or similar assets and liabilities in less active markets,
- inputs other than quoted prices that are observable, and
- model-based valuation techniques for which significant assumptions can be derived primarily from or corroborated by observable data in the market.

Level 3 – Valuation is based on model-based techniques that use one or more significant inputs or assumptions that are unobservable in the market.

Fair value is best determined by quoted market prices. However, in many instances, there are no quoted market prices for the Company’s various financial instruments. In cases where quoted market prices are not available, fair values are based on estimates using present value or other valuation techniques. Those techniques are significantly affected by the assumptions used, including the discount

rate and estimates of future cash flows. Accordingly, fair value estimates may not be realized in an immediate settlement of the instrument. Accounting guidance for fair value excludes certain financial instruments and all nonfinancial instruments from disclosure requirements. Consequently, the aggregate fair value amounts presented may not necessarily represent the underlying fair value of the Company.

The following describes the valuation techniques used by the Company to measure certain financial assets and liabilities recorded at fair value on a recurring basis in the consolidated financial statements:

### Financial Instruments Measured at Fair Value on a Recurring Basis

#### Securities Available for Sale

Securities available for sale are recorded at fair value on a recurring basis. Fair value measurement is based upon quoted market prices, when available (Level 1). If quoted market prices are not available, fair values are measured utilizing independent valuation techniques of identical or similar securities for which significant assumptions are derived primarily from or corroborated by observable market data. Third party vendors compile prices from various sources and may determine the fair value of identical or similar securities by using pricing models that consider observable market data (Level 2). The carrying value of restricted Federal Reserve Bank of Richmond and FHLB stock approximates fair value based upon the redemption provisions of each entity and is therefore excluded from the following tables. The following tables present the balances of financial assets measured at fair value on a recurring basis as of the dates indicated.

#### March 31, 2023

Description	Balance	Fair Value Measurements Using		
		Level 1	Level 2	Level 3
U.S. Treasuries	\$ 947	\$ -	\$ 947	\$ -
U.S. Government agencies and corporations	333,944	-	333,944	-
States and political subdivisions	149,962	-	149,962	-
Mortgage-backed securities	160,453	-	160,453	-
Corporate debt securities	5,741	-	5,741	-
Total securities available for sale	\$ 651,047	\$ -	\$ 651,047	\$ -

#### December 31, 2022

Description	Balance	Fair Value Measurements Using		
		Level 1	Level 2	Level 3
U.S. Treasuries	\$ 936	\$ -	\$ 936	\$ -
U.S. Government agencies and corporations	336,575	-	336,575	-
States and political subdivisions	152,200	-	152,200	-
Mortgage-backed securities	161,477	-	161,477	-
Corporate debt securities	5,664	-	5,664	-
Total securities available for sale	\$ 656,852	\$ -	\$ 656,852	\$ -

The Company's securities portfolio is valued using Level 2 inputs. The Company relies on an independent third party vendor to provide market valuations. The inputs used to determine value include: benchmark yields, reported trades, broker/dealer quotes, issuer spreads, two-sided markets, benchmark securities, bids, offers and reference data including market research publications. The third party vendor also monitors market indicators, industry activity and economic events as part of the valuation process. Central to the final valuation is the assumption that the indicators used are representative of the fair value of securities held within the Company's portfolio. Level 2 inputs are subject to a certain degree of uncertainty and changes in these assumptions or methodologies in the future, if any, may impact securities fair value, deferred tax assets or liabilities, or expense.

#### Interest Rate Loan Contracts and Forward Contracts

The Company originates consumer real estate loans which it intends to sell to a correspondent lender. Interest rate loan contracts and forward contracts result from originating loans held for sale and are derivatives reported at fair value. The Company enters interest rate lock commitments with customers who apply for a loan which the Company intends to sell to a correspondent lender. The interest rate loan contract ends when the loan closes or the customer withdraws their application. Fair value of the interest rate loan contract is based upon the correspondent lender's pricing quotes at the report date. Fair value is adjusted for the estimated probability of the loan closing with the borrower.

At the time the Company enters into an interest rate loan contract with a customer, it also enters into a best efforts forward sales commitment with the correspondent lender. If the loan has been closed and funded, the best efforts commitment converts to a mandatory

forward sales commitment. Fair value is based on the gain or loss that would occur if the Company were to pair-off the transaction with the investor at the measurement date. This is a Level 3 input. The Company has elected to measure and report best efforts commitments at fair value.

Interest rate loan contracts and forward contracts are valued based on quotes from the correspondent lender at the reporting date. Pricing changes daily and if a loan has not been sold to the correspondent by the next reporting date, the fair value may be different from that reported currently. Changes in fair value measurement impacts net income.

At December 31, 2022, there were no interest rate loan contracts or forward contracts. The following table presents the Company's interest rate loan contracts and forward contracts as of March 31, 2023:

March 31, 2023	Description	Balance	Fair Value Measurements Using		
			Level 1	Level 2	Level 3
	Interest rate loan contracts	\$ 2	\$ -	\$ -	\$ 2
	Forward contracts	(2)	-	-	(2)

March 31, 2023	Valuation Technique	Unobservable Input	Range (Weighted Average)
Interest rate loan contracts	Market approach	Pull-through rate	81.30%
Forward contracts	Market approach	Pull-through rate	81.30%
Interest rate loan contracts	Market approach	Current reference price	100.83% – 102.22% (101.24%)
Forward contracts	Market approach	Current reference price	100.83% – 102.22% (101.24%)

#### Financial Instruments Measured at Fair Value on a Non-Recurring Basis

Certain financial instruments are measured at fair value on a nonrecurring basis in accordance with GAAP. Adjustments to the fair value of these assets usually result from the application of lower-of-cost-or-market accounting or write-downs of individual assets. The following describes the valuation techniques used by the Company to measure certain assets recorded at fair value on a nonrecurring basis in the consolidated financial statements.

#### Loans Held for Sale

Loans held for sale are carried at the lower of cost or fair value. These loans currently consist of one-to-four family residential loans originated for sale in the secondary market. Fair value is based on the price secondary markets are currently offering for similar loans using observable market data which is not materially different than cost due to the short duration between origination and sale (Level 2). As such, the Company records any fair value adjustments on a nonrecurring basis. No nonrecurring fair value adjustments were recorded on loans held for sale at March 31, 2023 or December 31, 2022.

#### Collateral Dependent Loans

Loans the Company has identified as collateral dependent that do not share risk characteristics are individually evaluated on a non-recurring basis. For collateral dependent loans, the ACL is measured as the difference between the fair value of the collateral and the amortized cost basis of the loan as of the measurement date. When repayment is expected from the operation of the collateral, credit losses are estimated as the amount by which the amortized cost basis of the loan exceeds the present value of expected cash flows from the operation of the collateral. When repayment is expected from the sale of the collateral, credit losses are measured as the amount by which the amortized costs basis of the loan exceeds the fair value of the underlying collateral less estimated cost to sell. The ACL may be zero if the fair value of the collateral at the measurement date exceeds the amortized cost basis of the financial asset.

For real estate loans, fair value of collateral is determined by the "as-is" value of appraisals that are less than 24 months of age and are prepared by independent, licensed appraisers. Appraisals are based upon observable market data analyzed through an income or sales valuation approach, and adjusted by estimated selling costs. Valuation falls within Level 2 categorization. The Company may further discount appraisals for marketing strategies, which results in Level 3 categorization.

The value of business equipment is based upon an outside appraisal (Level 2) if deemed significant, or the net book value on the applicable business' financial statements (Level 3) if not considered significant. Likewise, values for inventory and accounts receivables collateral are based on financial statement balances or aging reports (Level 3).

At March 31, 2023, none of the Company's individually evaluated loans were measured using the collateral method. As of December 31, 2022, measurement of the Company's impaired loans did not result in any specific allocations.



### Other Real Estate Owned (“OREO”)

Certain assets such as OREO are measured at fair value less cost to sell. Valuation of OREO is determined using current appraisals from independent parties, a Level 2 input. The Company works with a realtor to determine the list price, which may be set at appraised value or at a different amount based on the realtor’s advice and Management’s judgement of marketability. Discounts to appraisals for selling costs or for marketability result in a Level 3 estimate.

The following table summarizes the Company’s OREO that was measured at fair value on a nonrecurring basis.

Date	Description	Balance	Level 1	Level 2	Level 3
<b>March 31, 2023</b>	OREO, net of valuation allowance	\$ 662	\$ -	\$ -	\$ 662
December 31, 2022	OREO, net of valuation allowance	662	-	-	662

The following table presents information about OREO and Level 3 Fair Value Measurements for the dates indicated.

Date	Valuation Technique	Unobservable Input	Range (Weighted Average)
<b>March 31, 2023</b>	Discounted appraised value	Selling cost	<b>7.00%</b>
<b>March 31, 2023</b>	Discounted appraised value	Discount for lack of marketability	<b>34.72%</b>
December 31, 2022	Discounted appraised value	Selling cost	7.00%
December 31, 2022	Discounted appraised value	Discount for lack of marketability	34.72%

At March 31, 2023 and December 31, 2022, the Company held a single OREO property, measured using appraised value, discounted for marketability and selling cost. During 2022, the Company reduced the list price as part of a marketing strategy and recorded an additional discount for marketability.

There is uncertainty in determining discounts to appraised value. If the final sale price is different from the list price, the amount of selling costs will also be different from those estimated. Future changes to marketability assumptions or updated appraisals may indicate a lower fair value, with a corresponding impact to net income. Ultimate proceeds from the sale of OREO property may be less than the estimated fair value, reducing net income.

### Fair Value Summary

The following presents the recorded amount, fair value, and placement in the fair value hierarchy of the Company’s financial instruments as of the dates indicated. Fair values are estimated using the exit price notion.

	March 31, 2023			
	Recorded Amount	Level 1	Level 2	Level 3
<b>Financial Assets:</b>				
Cash and due from banks	\$ 11,695	\$ 11,695	\$ -	\$ -
Interest-bearing deposits	42,966	42,966	-	-
Securities available for sale	651,047	-	651,047	-
Restricted securities	929	-	929	-
Loans, net	846,315	-	-	803,330
Accrued interest receivable	6,007	-	6,007	-
Bank-owned life insurance	43,551	-	43,551	-
Interest rate loan contracts	2	-	-	2
<b>Financial Liabilities:</b>				
Deposits	\$ 1,511,452	\$ -	\$ 1,385,881	\$ 125,931
Accrued interest payable	314	-	314	-
Forward loan contracts	2	-	-	2

	December 31, 2022			
	Recorded Amount	Level 1	Level 2	Level 3
<b>Financial Assets:</b>				
Cash and due from banks	\$ 12,403	\$ 12,403	\$ -	\$ -
Interest-bearing deposits	59,026	59,026	-	-
Securities available for sale	656,852	-	656,852	-
Restricted securities	941	-	941	-
Loans, net	844,519	-	-	781,749
Accrued interest receivable	6,001	-	6,001	-
Bank-owned life insurance	43,312	-	43,312	-
<b>Financial Liabilities:</b>				
Deposits	\$ 1,542,725	\$ -	\$ 1,475,096	\$ 67,542
Accrued interest payable	106	-	106	-

#### Note 6: Components of Accumulated Other Comprehensive Income (Loss)

The following tables provide information about components of accumulated other comprehensive loss as of the dates indicated:

	Net Unrealized Gain (Loss) on Securities	Adjustments Related to Pension Benefits	Accumulated Other Comprehensive Loss
<b>Balance at December 31, 2021</b>	\$ 2,854	\$ (6,912)	\$ (4,058)
Unrealized holding loss on available for sale securities, net of tax of (\$8,992)	(33,826)	-	(33,826)
<b>Balance at March 31, 2022</b>	\$ (30,972)	\$ (6,912)	\$ (37,884)
<b>Balance at December 31, 2022</b>	\$ (81,421)	\$ (2,345)	\$ (83,766)
Unrealized holding gain on available for sale securities, net of tax of \$3,121	11,738	-	11,738
Reclassification adjustment, net of tax of (\$3)	(9)	-	(9)
<b>Balance at March 31, 2023</b>	\$ (69,692)	\$ (2,345)	\$ (72,037)

#### Note 7: Revenue Recognition

Substantially all of the Company's revenue is generated from contracts with customers. Noninterest revenue streams such as service charges on deposit accounts, other service charges and fees, credit and debit card fees, trust income, and annuity and insurance commissions are recognized in accordance with ASC Topic 606, "Revenue from Contracts with Customers". Topic 606 does not apply to revenue associated with financial instruments, including revenue from loans and securities. In addition, certain noninterest income streams such as financial guarantees, derivatives, and certain credit card fees are outside the scope of the guidance. Noninterest revenue streams within the scope of Topic 606 are discussed below.

##### *Service Charges on Deposit Accounts*

Service charges on deposit accounts consist of monthly service fees, overdraft and nonsufficient funds fees, ATM fees, wire transfer fees, and other deposit account related fees. The Company's performance obligation for monthly service fees is generally satisfied, and the related revenue recognized, over the period in which the service is provided. Payment for service charges on deposit accounts is primarily received immediately or in the following month through a direct charge to customers' accounts. ATM fees are primarily generated when a Company cardholder uses a non-Company ATM or a non-Company cardholder uses a Company ATM. Wire transfer fees, overdraft and nonsufficient funds fees and other deposit account related fees are transactional based, and therefore, the Company's performance obligation is satisfied, and related revenue recognized, at a point in time.

##### *Other Service Charges and Fees*

Other service charges include safe deposit box rental fees, check ordering charges, and other service charges. Safe deposit box rental fees are charged to the customer on an annual basis and recognized upon receipt of payment. The Company determined that since rentals and renewals occur fairly consistently over time, revenue is recognized on a basis consistent with the duration of the performance

obligation. Check ordering charges are transactional based, and therefore the Company's performance obligation is satisfied, and related revenue recognized, at a point in time.

#### *Credit and Debit Card Fees*

Credit and debit card fees are primarily comprised of interchange fee income and merchant services income. Interchange fees are earned whenever the Company's debit and credit cards are processed through card payment networks such as Visa and MasterCard. Merchant services income mainly represents commission fees based upon merchant processing volume. The Company's performance obligation for interchange fee income and merchant services income are largely satisfied, and related revenue recognized, when the services are rendered or upon completion. Payment is typically received immediately or in the following month. In compliance with Topic 606, credit and debit card fee income is presented net of associated expense.

#### *Trust Income*

Trust income is primarily comprised of fees earned from the management and administration of trusts and estates and other customer assets. The Company's performance obligation is generally satisfied over time and the resulting fees are recognized monthly, based upon the month-end market value of the assets under management and the applicable fee rate. Payment is generally received a few days after month end through a direct charge to customers' accounts. The Company does not earn performance-based incentives. Estate management fees are based upon the size of the estate. A partial fee is recognized half-way through the estate administration and the remainder of the fee is recognized when remaining assets are distributed and the estate is closed.

#### *Insurance and Investment*

Insurance income primarily consists of commissions received on insurance product sales. The Company acts as an intermediary between the Company's customer and the insurance carrier. The Company's performance obligation is generally satisfied upon the issuance of the insurance policy. Shortly after the insurance policy is issued, the carrier remits the commission payment to the Company, and the Company recognizes the revenue.

Investment income consists of recurring revenue streams such as commissions from sales of mutual funds and other investments. Commissions from the sale of mutual funds and other investments are recognized on trade date, which is when the Company has satisfied its performance obligation. The Company also receives periodic service fees (i.e., trailers) from mutual fund companies typically based on a percentage of net asset value. Trailer revenue is recorded over time, usually monthly or quarterly, as net asset value is determined.

#### *OREO Gains and Losses*

The Company records a gain or loss from the sale of OREO when control of the property transfers to the buyer, which generally occurs at the time of an executed deed. When the Company finances the sale of OREO to the buyer, the Company assesses whether the buyer is committed to perform their obligations under the contract and whether collectability of the transaction price is probable. Once these criteria are met, the OREO asset is derecognized and the gain or loss on sale is recorded upon the transfer of control of the property to the buyer.

The following presents noninterest income, segregated by revenue streams in-scope and out-of-scope of Topic 606, for the three months ended March 31, 2023 and March 31, 2022

	<b>Three Months Ended March 31,</b>	
	<b>2023</b>	<b>2022</b>
<b>Noninterest Income</b>		
<i>In-scope of Topic 606:</i>		
Service charges on deposit accounts	\$ 592	\$ 562
Other service charges and fees	53	55
Credit and debit card fees, net	467	440
Trust income	445	443
Insurance and Investment (included within Other Income on the Consolidated Statements of Income)	285	208
Noninterest Income (in-scope of Topic 606)	\$ 1,842	\$ 1,708
Noninterest Income (out-of-scope of Topic 606)	357	583
Total noninterest income	\$ 2,199	\$ 2,291

**Note 8: Leases**

The Company's leases are recorded under ASC Topic 842, "Leases". The Company examines its contracts to determine whether they are or contain a lease. A contract with a lease is further examined to determine whether the lease is a short-term, operating or finance lease. As permitted by ASC Topic 842, the Company elected not to capitalize short-term leases, defined by the standard as leases with terms of 12 months or less. The Company also elected the practical expedient not to separate non-lease components from lease components within a single contract.

Right-of-use assets and lease liabilities are recognized for operating and finance leases. Right-of-use assets represent the Company's right to use the underlying asset for the lease term and are calculated as the sum of the lease liability and if applicable, prepaid rent, initial direct costs and any incentives received from the lessor. Lease liabilities represent the Company's obligation to make lease payments and are presented at each reporting date as the net present value of the remaining contractual cash flows. Cash flows are discounted at the Company's incremental borrowing rate in effect at the commencement date of the lease.

*Lease payments*

Lease payments for short-term leases are recognized as lease expense on a straight-line basis over the lease term, or for variable lease payments, in the period in which the obligation was incurred. Payments for leases with terms longer than 12 months are included in the determination of the lease liability. Payments may be fixed for the term of the lease or variable. Variable payments result when the lease agreement includes a clause providing for escalation of lease payments at specified dates. If the escalation factor is known, such as a specified percentage increase per year or a stated increase at a specified time, the variable payment is included in the cash flows used to determine the lease liability. If the variable payment is based upon an unknown escalator, such as the consumer price index at a future date, the increase is not included in the cash flows used to determine the lease liability. One of the Company's leases provides a known escalator that is included in the determination of the lease liability. The remaining leases do not have variable payments during the term of the lease.

*Options to Extend, Residual Value Guarantees, and Restrictions and Covenants*

Of the Company's seven operating leases as of March 31, 2023, four leases offer the option to extend the lease term. Two of the leases have two options of five years each and one lease has two options of three years each. Another lease has one option to extend the term for an additional five years. The Company exercised a previous option to extend this lease in 2020. At the time of capitalization, the Company was not reasonably certain whether it would exercise the options and did not include the time period in the calculation of the lease liability. The lease agreements provide that the lease payment will increase at the exercise date based on the Consumer Price Index for All Urban Consumers ("CPI-U"). Because the CPI-U at the exercise date is unknown, the increase is not included in the cash flows determining the lease liability. None of the Company's leases provide for residual value guarantees and none provide restrictions or covenants that would impact dividends or require incurring additional financial obligations.

The contracts in which the Company is lessee are with parties external to the Company and not related parties. The Company's lease right of use asset is included in other assets and the lease liability is included in other liabilities. The following tables present information about leases:

	March 31, 2023	December 31, 2022
Lease liability	\$ 1,365	\$ 1,444
Right-of-use asset	\$ 1,336	\$ 1,415
Weighted average remaining lease term	4.95 years	5.14 years
Weighted average discount rate	3.29 %	3.29%

**For the Three Months Ended March 31,**

	2023	2022
<b>Lease Expense</b>		
Operating lease expense	\$ 92	\$ 76
Short-term lease expense	1	1
Total lease expense	\$ 93	\$ 77
Cash paid for amounts included in lease liabilities	\$ 94	\$ 78
Right-of-use assets obtained in exchange for operating lease liabilities commencing during the period	\$ -	\$ 25

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The following table presents a maturity schedule of undiscounted cash flows that contribute to the lease liability:

<b>Undiscounted Cash Flow for the Period</b>	<b>As of March 31, 2023</b>
Twelve months ending March 31, 2024	\$ 356
Twelve months ending March 31, 2025	340
Twelve months ending March 31, 2026	234
Twelve months ending March 31, 2027	203
Twelve months ending March 31, 2028	188
Thereafter	160
Total undiscounted cash flows	\$ 1,481
Less: discount	(116)
Lease liability	\$ 1,365

The contracts in which the Company is lessee are not with related parties.

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## Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations

\$ in thousands, except per share data

The purpose of this discussion and analysis is to provide information about the financial condition and results of operations of the Company. Please refer to the financial statements and other information included in this report as well as the Company's 2022 Annual Report on Form 10-K for an understanding of the following discussion and analysis. References in the following discussion and analysis to "we" or "us" refer to the Company unless the context indicates that the reference is to the Bank.

### Cautionary Statement Regarding Forward-Looking Statements

We make forward-looking statements in this Form 10-Q that are subject to significant risks and uncertainties. These forward-looking statements include statements regarding our profitability, liquidity, allowance for loan losses, interest rate sensitivity, market risk, growth strategy, and financial and other goals, and are based upon our management's views and assumptions as of the date of this report. The words "believes," "expects," "may," "will," "should," "projects," "contemplates," "anticipates," "forecasts," "intends," or other similar words or terms are intended to identify forward-looking statements.

These forward-looking statements are based upon or are affected by factors that could cause our actual results to differ materially from historical results or from any results expressed or implied by such forward-looking statements. These factors include, but are not limited to, effects of or changes in:

- interest rates,
- general and local economic conditions,
- monetary and fiscal policies of the U.S. Government, including policies of the U.S. Treasury, the Office of the Comptroller of the Currency, the Federal Reserve, the Consumer Financial Protection Bureau and the Federal Deposit Insurance Corporation, and the impact of any policies or programs implemented pursuant to financial reform legislation,
- unanticipated increases in the level of unemployment in the Company's market,
- the quality or composition of the loan and/or investment portfolios,
- demand for loan products,
- deposit flows,
- competition,
- demand for financial services in the Company's market,
- the real estate market in the Company's market,
- laws, regulations and policies impacting financial institutions,
- technological risks and developments, and cyber-threats, attacks or events,
- the Company's technology initiatives,
- geopolitical conditions, including acts or threats of terrorism and/or military conflicts, or actions taken by the U.S. or other governments in response to acts or threats of terrorism and/or military conflicts,
- the occurrence of significant natural disasters, including severe weather conditions, floods, health related issues, and other catastrophic events,
- the Company's ability to identify, attract, and retain experienced management, relationship managers, and support personnel, particularly in a competitive labor environment,
- performance by the Company's counterparties or vendors,
- applicable accounting principles, policies and guidelines, and
- the impact of the COVID-19 pandemic, including the adverse impact on our business and operations and on our customers.

These risks and uncertainties should be considered in evaluating the forward-looking statements contained in this report. We caution readers not to place undue reliance on those statements, which speak only as of the date of this report. This discussion and analysis should be read in conjunction with the description of our "Risk Factors" in Item 1A of the most recently filed Form 10-K.

### Cybersecurity

The Company considers cybersecurity risk to be one of the greatest risks to its business. We have deployed a multi-faceted approach to limit the risk and impact of unauthorized access to customer accounts and to information relevant to customer accounts. We use digital technology safeguards, internal policies and procedures, and employee training to reduce the exposure of our systems to cyber-intrusions. The Company also requires assurances from key vendors regarding their cybersecurity.

We control functionalities of online and mobile banking to reduce risk. We do not offer online account openings or loan originations. We do not permit customers to submit address changes through online banking, and we limit the dollar amount of online banking transfers to other banks. We require a special vetting process for commercial customers who wish to originate ACH transfers and for customers who submit wire requests through online banking.

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Further, the Company has a program to identify, mitigate and manage its cybersecurity risks. The program includes penetration testing and vulnerability assessment, technological defenses such as antivirus software, patch management, firewall management, email and web protections, an intrusion prevention system, a cybersecurity insurance policy which covers some but not all losses arising from cybersecurity breaches, as well as ongoing employee training. The cost of these measures was \$63 for the three months ended March 31, 2023 and \$94 for the three months ended March 31, 2022. These costs are included in various categories of noninterest expense.

However, it is not possible to fully eliminate exposure. The potential for financial and reputational losses due to cyber-breaches is increased by the possibility of human error, unknown system susceptibilities, and the rising sophistication of cyber-criminals to attack systems, disable safeguards and gain access to accounts and related information. We maintain insurance for these risks but insurance policies are subject to exceptions, exclusions and terms whose applications have not been widely interpreted in litigation. Accordingly, insurance can provide less than complete protection against the losses that result from cybersecurity breaches and pursuing recovery from insurers can result in significant expense. In addition, some risks such as reputational damage and loss of customer goodwill, which can result from cybersecurity breaches, cannot be insured against.

### **Critical Accounting Policies**

The Company's consolidated financial statements are prepared in accordance with GAAP. The financial information contained within our statements is, to a significant extent, based on measures of the financial effects of transactions and events that have already occurred. A variety of factors could affect the ultimate value obtained when earning income, recognizing an expense, recovering an asset or relieving a liability. Although the economics of the Company's transactions may not change, the timing of events that would impact the transactions could change.

Critical accounting policies are most important to the portrayal of the Company's financial condition or results of operations and require Management's most difficult, subjective, and complex judgments about matters that are inherently uncertain. If conditions occur that differ from our assumptions, depending upon the severity of such differences, the Company's financial condition or results of operations may be materially impacted. The Company has designated three policies as critical, including those governing the allowance for credit losses, goodwill and the pension plan. The Company evaluates its critical accounting estimates and assumptions on an ongoing basis and updates them as needed. Please refer to the Company's 2022 Form 10-K, Note 1: Summary of Significant Accounting Policies for information on these and other accounting policies. For information on the Company's policies on the ACLL beginning with adoption of CECL on January 1, 2023, please refer to Note 1: General.

### **Overview**

National Bankshares, Inc. is a financial holding company that was organized in 1986 under the laws of Virginia and is registered under the Bank Holding Company Act of 1956. NBI common stock is listed on the Nasdaq Capital Market and is traded under the symbol "NKSH."

NBI has two wholly-owned subsidiaries, the National Bank of Blacksburg and National Bankshares Financial Services, Inc. NBB is a community bank and does business as National Bank from 24 office locations and three loan production offices. NBB is the source of nearly all of the Company's revenue. NBFS does business as National Bankshares Investment Services and National Bankshares Insurance Services. Income from NBFS is not significant at this time, nor is it expected to be so in the near future.

### **Non-GAAP Financial Measures**

This report refers to certain financial measures that are computed under a basis other than GAAP ("non-GAAP"). The Company uses certain non-GAAP financial measures to provide meaningful supplemental information regarding the Company's operational performance and to enhance investors' overall understanding of such financial performance. The methodology for determining these non-GAAP measures may differ among companies and are supplementary to our financial condition, results of operations and cash flows computed in accordance with GAAP. Details on non-GAAP measures follow.

#### *Adjusted Return on Average Assets and Adjusted Return on Average Equity*

The adjusted return on average assets and adjusted return on average equity are measures of profitability, calculated by annualizing net income and dividing by average year-to-date assets or equity, respectively. Larger nonrecurring income or expenses are not annualized, in order to reduce distortion within the ratios. During the three months ended March 31, 2023, the recorded income from the adjustment of basis in partnership interests, the net gain on the sale of securities and expenses incurred to respond to a threatened proxy contest initiated by an activist stockholder were removed from the annualization. For the three months ended March 31, 2022, the income recorded from the adjustment of basis in partnership interests was removed from the annualization. The tables below present the reconciliation of adjusted annualized net income, which is not a measurement under GAAP, for the three month periods ended March 31, 2023 and 2022.

	<b>Three Months Ended</b>	
	<b>March 31, 2023</b>	<b>March 31, 2022</b>
<b>Annualized Net Income</b>		
Net income (GAAP)	\$ 4,531	\$ 4,886
Less: items deemed by Management to be non-recurring:		
Partnership income net of tax of (\$44) and (\$77) for the periods ended March 31, 2023 and 2022, respectively	(164)	(290)
Securities gain, net of tax of (\$3) for the period ended March 31, 2023	(9)	-
Proxy contest-related expense, net of tax of \$93	348	-
Adjusted net income	\$ 4,706	\$ 4,596
Adjusted net income, annualized	\$ 19,085	\$ 18,639
Add: items deemed by Management to be non-recurring:		
Partnership income net of tax of \$44 and \$77 for the periods ended March 31, 2023 and 2022, respectively	164	290
Securities gain, net of tax of \$3 for the period ended March 31, 2023	9	-
Proxy contest-related expense, net of tax of (\$93)	(348)	-
Annualized net income for ratio calculation (non-GAAP)	\$ 18,910	\$ 18,929

Unrealized losses on securities available for sale decrease total assets and stockholders' equity through accumulated other comprehensive loss. Along with the return on average assets, the Company considers the ratio, adjusted to exclude the impact of unrealized losses. Along with the return on average equity, the Company considers the ratio, adjusted to exclude accumulated other comprehensive loss. The adjustments to average assets and average stockholders' equity are presented in the table below.

	<b>Three Months Ended</b>	
	<b>March 31, 2023</b>	<b>March 31, 2022</b>
<b>Average Assets Excluding Unrealized Loss on Securities</b>		
Average assets (GAAP)	\$ 1,625,041	\$ 1,703,280
Average unrealized loss on securities	98,823	6,836
Average deferred tax asset, unrealized loss on securities	(20,753)	(1,436)
Average assets excluding unrealized loss on securities (non-GAAP)	\$ 1,703,111	\$ 1,708,680
<b>Average Stockholders' Equity Excluding AOCI</b>		
Average stockholders' equity (GAAP)	\$ 123,996	\$ 185,324
Average accumulated other comprehensive loss	80,415	12,312
Average stockholders' equity excluding AOCI (non-GAAP)	\$ 204,411	\$ 197,636

The return on average assets and return on average equity under GAAP and adjusted for non-GAAP considerations, are presented in the table below:

	<b>Three Months Ended March 31,</b>	
	<b>2023</b>	<b>2022</b>
Return on average assets (GAAP)	1.13%	1.16%
Adjusted return on average assets (non-GAAP)	1.16%	1.11%
Adjusted return on average assets excluding unrealized losses on securities (non-GAAP)	1.11%	1.11%
Return on average equity (GAAP)	14.82%	10.69%
Adjusted return on average equity (non-GAAP)	15.25%	10.21%
Adjusted return on average equity excluding accumulated other comprehensive loss (non-GAAP)	9.25%	9.58%



### Net Interest Margin

The Company uses the adjusted net interest margin to measure profit on interest generating activities, as a percentage of total interest-earning assets. The adjusted net interest margin is calculated by dividing annualized fully taxable equivalent (“FTE”) net interest income by total average earning assets. The portion of interest income that is nontaxable is grossed up to the tax equivalent by adding the tax benefit. The tax rate utilized in calculating the tax benefit is 21%. The reconciliation of tax equivalent net interest income, which is not a measurement under GAAP, to net interest income, is reflected in the table below.

	Three Months Ended	
	March 31, 2023	March 31, 2022
<b>Net Interest Income, FTE</b>		
Total interest income (GAAP)	\$ 14,044	\$ 11,050
FTE adjustment	209	227
Total interest income (non-GAAP)	14,253	11,277
Total interest expense (GAAP)	3,098	655
Net interest income, FTE (non-GAAP)	\$ 11,155	\$ 10,622
Average balance of interest-earning assets	\$ 1,667,191	\$ 1,525,651
Net interest margin	2.88%	2.81 %

Further detail on the net interest margin is provided under the Net Interest Income discussion.

### Efficiency Ratio

The efficiency ratio is computed by dividing noninterest expense by the sum of FTE net interest income and noninterest income, excluding certain items Management deems unusual or non-recurring. This is a non-GAAP financial measure that the Company believes provides investors with important information regarding operational efficiency. The components of the efficiency ratio calculation are summarized in the following table.

	Three Months Ended	
	March 31, 2023	March 31, 2022
<b>Noninterest Expense for Efficiency Ratio</b>		
Noninterest expense (GAAP)	\$ 7,664	\$ 6,613
Less: proxy contest-related expense	(441)	-
Noninterest expense for efficiency ratio (non-GAAP)	\$ 7,223	\$ 6,613
<b>Total Income for Efficiency Ratio</b>		
Noninterest income (GAAP)	\$ 2,199	\$ 2,291
Less: securities gains	(12)	-
Less: partnership income	(208)	(367)
Noninterest income (non-GAAP)	1,979	1,924
Net interest income, FTE (non-GAAP)	11,155	10,622
Total income for efficiency ratio (non-GAAP)	\$ 13,134	\$ 12,546
Efficiency ratio	54.99%	52.71 %

## Performance Summary

The following table presents the Company's key performance indicators for the three months ended March 31, 2023 and March 31, 2022. Income and expense items are annualized for the ratios, except for basic and fully diluted earnings per share.

	<u>Three Months Ended March 31,</u>	
	<u>2023</u>	<u>2022</u>
Net Income	\$ 4,531	\$ 4,886
Return on average assets	1.13 %	1.16 %
Adjusted return on average assets <sup>(1)</sup>	1.16 %	1.11 %
Adjusted return on average assets excluding unrealized losses on securities <sup>(1)</sup>	1.11 %	1.11 %
Return on average equity	14.82 %	10.69 %
Adjusted return on average equity <sup>(1)(2)</sup>	15.25 %	10.21 %
Adjusted return on average equity excluding accumulated other comprehensive loss <sup>(1)(2)</sup>	9.25 %	9.58 %
Basic and fully diluted earnings per share <sup>(2)</sup>	\$ 0.77	\$ 0.81
Net interest margin <sup>(1)</sup>	2.79 %	2.65 %
Efficiency ratio <sup>(1)</sup>	54.99 %	52.71 %

<sup>(1)</sup> See "Non-GAAP Financial Measures" above.

<sup>(2)</sup> During the three months ended March 31, 2022, the Company repurchased 41,185 shares under its publicly announced stock repurchase plan. The repurchase reduced stockholders equity by \$1,522.

Net income and earnings per share for the three months ended March 31, 2023 decreased when compared with the same period of 2022. Contributing to the decrease were pre-tax expenses totaling \$441 incurred to respond to a threatened proxy contest initiated by an activist stockholder. The Company announced on March 31, 2023 that the activist had withdrawn its nominees for the Company's Board of Directors with no concessions or negotiated settlement with the Company.

For the three months ended March 31, 2023, adjusted return on average assets and adjusted return on average equity, excluding the impact of unrealized losses on available for sale securities, remained at similar levels as those for the three months ended March 31, 2022. The Company's efficiency ratio continues to reflect the Company's commitment to control expenses.

## Key Assets and Liabilities

NBI's key assets and liabilities and their change from December 31, 2022 are shown in the following table.

	<u>March 31, 2023</u>	<u>December 31, 2022</u>	<u>Percent Change</u>
Interest-bearing deposits	\$ 42,966	\$ 59,026	(27.21) %
Securities available for sale	651,047	656,852	(0.88) %
Loans, net	846,315	844,519	0.21 %
Total assets	1,654,277	1,677,551	(1.39) %
Deposits	1,511,452	1,542,725	(2.03) %

## Asset Quality

Key indicators of the Company's asset quality are presented in the following table.

	<b>March 31, 2023</b>	<b>March 31, 2022</b>	<b>December 31, 2022</b>
Nonaccrual loans	\$ 2,814	\$ 2,862	\$ 2,847
Loans past due 90 days or more, and still accruing	33	381	8
Other real estate owned	662	957	662
ACLL to loans net of unearned income and deferred fees and costs	1.24 %	0.95%	0.96%
Net charge-off (recovery) ratio	(0.04) %	0.01%	0.02%
Ratio of nonperforming assets to loans, net of unearned income and deferred fees and costs, plus other real estate owned	0.41 %	0.47%	0.41%
Ratio of ACLL to nonperforming loans	378.46 %	272.12%	288.90%

The Company adopted the CECL model on January 1, 2023, resulting in an increase to the ACLL of \$2,342, from the \$8,225 allowance for loan losses at December 31, 2022. For information on the Company's policies on the ACLL, please refer to Note 1: General. Please refer to the Company's 2022 Form 10-K, Note 1: Summary of Significant Accounting Policies for information on the Company's application of previous GAAP in determining the allowance for loan losses.

The Company's risk analysis under the CECL model at March 31, 2023 determined an ACLL of \$10,650, or 1.24% of loans net of unearned income and deferred fees and costs. This compares with an allowance of \$8,225 as of December 31, 2022, or 0.96% of loans. The allowance for loan losses at March 31, 2022 was \$7,788, or 0.95% of loans. To determine the appropriate level of the ACLL, the Company considers credit risk for individually evaluated loans and for groups of loans evaluated collectively.

### **Individually Evaluated Loans**

Individually evaluated loans were \$4,130 as of March 31, 2023, an increase from \$3,032 as of December 31, 2022. The increase was due to a change in the way that the Company identifies individually evaluated loans under CECL. Please refer to Note 1: General for information on the Company's identification of individually evaluated loans. None of the Company's individually evaluated loans as of March 31, 2023 were determined to be collateral dependent and were measured using the DCF method, resulting in an allocation of \$434.

### **Collectively Evaluated Loans**

Collectively evaluated loans totaled \$853,266, with an ACLL of \$10,216 as of March 31, 2023. At December 31, 2022, collectively evaluated loans totaled \$850,161, with an allowance of \$8,225.

Collectively evaluated loans are divided into pools based upon risk characteristics. Utilizing historical loss information, the Company calculates a probability of default and loss given default for each pool, which is adjusted for a reasonable and supportable forecast. Loan pools are allocated additional loss estimates based upon the Company's analysis of qualitative factors including economic measures, asset quality indicators, loan characteristics, and changes to internal Company policies and management.

### *Reasonable and Supportable Forecast*

To estimate cash flows, the Company adjusted its historical loss information with a forecast of the national unemployment rate. The forecast applied at March 31, 2023 projects that unemployment will rise over the next 12 months, which increases the loss estimate. The Company determined that 12 months represents a reasonable and supportable forecast period as of March 31, 2023, and set a period of 12 months to revert to historical losses on a straight-line basis.

### *Qualitative Factors: Economic*

The Company sources economic data pertinent to its market from the most recently available publications, including business and personal bankruptcy filings, the residential vacancy rate and the inventory of new and existing homes.

Higher bankruptcy filings indicate heightened credit risk and increase the ACLL, while lower bankruptcy filings have a beneficial impact on credit risk. Compared with data available at December 31, 2022, business bankruptcy filings slightly increased and personal bankruptcy filings slightly decreased.

Residential vacancy rates and housing inventory impact the Company's residential construction customers and the consumer real estate market. Higher levels increase credit risk. The residential vacancy rate available at March 31, 2023 improved from the data incorporated into the December 31, 2022 calculation, resulting in a lower allocation. Housing data available as of March 31, 2023 showed slightly lower inventory than at December 31, 2022, resulting in a lower allocation.

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### *Qualitative Factors: Asset Quality Indicators*

Accruing past due loans are analyzed at the class level and compared with previous levels. Increases in past due loans indicate heightened credit risk. Accruing loans past due 30-89 days were 0.14% of total loans at March 31, 2023, a decrease from 0.16% at December 31, 2022. Accruing loans past due 90 days or more were a very small percentage of the loan portfolio as of March 31, 2023 and at December 31, 2022.

### *Qualitative Factors: Other Considerations*

The Company considers other factors that impact credit risk, including the interest rate environment, the competitive, legal and regulatory environments, changes in lending policies and loan review, changes in lending management, and high risk loans.

The interest rate environment impacts variable rate loans. When interest rates increase, the payment on variable rate loans increases, which may increase credit risk. The Federal Reserve increased the target Fed Funds rate multiple times in 2022, as well as in February and March of 2023, resulting in an increased allocation as of March 31, 2023, compared with the allocation for December 31, 2022.

The competitive, legal and regulatory environments were evaluated for changes that would impact credit risk. Higher competition for loans increases credit risk, while lower competition decreases credit risk. Competition remained at similar levels to those at December 31, 2022. The legal and regulatory environments also remain in a similar posture to December 31, 2022.

Lending policies, loan review procedures and Management's experience influence credit risk. Except for the adoption of CECL, policies, procedures and management remain similar to those at December 31, 2022.

Levels of high risk loans are considered in the determination of the level of the ACLL. A decrease in the level of high risk loans within a class decreases the required allocation for the loan class, and an increase in the level of high risk loans within a class increases the required allocation for the loan class. Total high risk loans increased 7.33% from the level at December 31, 2022, resulting in an increased allocation.

### *Unallocated Surplus*

The unallocated surplus as of March 31, 2023 is \$480, or 4.72% in excess of the calculated requirement. The unallocated surplus at December 31, 2022 was \$179, or 2.23% in excess of the calculated requirement. The surplus provides some mitigation of current economic uncertainty that may impact credit risk.

### **Conclusion**

The calculation of the appropriate level for the ACLL incorporates analysis of multiple factors and requires Management's prudent and informed judgment. The Company augmented the calculated requirement with an unallocated surplus. Based on analysis of historical indicators, asset quality and economic factors, Management believes the level of ACLL is reasonable for the credit risk in the loan portfolio as of March 31, 2023.

### **Provision for Credit Loss**

The calculation of the ACLL resulted in a provision for credit losses of \$2 for the three month period ended March 31, 2023, compared with a provision of \$134 for the three month period ended March 31, 2022. The provision for 2023 and 2022 reflect loan growth and changes in factors detailed in "Asset Quality" above.

### **Loan Modifications**

In the ordinary course of business the Company modifies loan terms on a case-by-case basis for a variety of reasons. Modifications may include rate reductions, payment extensions of varying lengths of time, a change in amortization term or method or other arrangements. Modifications to consumer loans generally involve short-term payment extensions to accommodate specific, temporary circumstances. Modifications to commercial loans may include, but are not limited to, changes in interest rate, maturity, amortization and financial covenants.

The Company reviews modifications to determine whether the borrower is experiencing financial difficulty, including indicators of default, bankruptcy, going concern, insufficient projected cash flows and inability to obtain financing from other sources. If a modification is made to a borrower experiencing financial difficulty, the loan's risk rating is downgraded to special mention or classified, resulting in individual evaluation for the ACL.

### *Modifications That Are Not for Borrowers Experiencing Financial Difficulty*

During the three months ended March 31, 2023, the Company provided 201 modifications for competitive reasons to loans totaling \$30,508. During the three months ended March 31, 2022, the Company provided 235 modifications to loans totaling \$39,182. The modifications were not to borrowers experiencing financial difficulty.

## Other Real Estate Owned

As of March 31, 2023, OREO of \$662 is comprised of one construction property. Loans in various stages of foreclosure totaled \$95, all of which are secured by residential real estate. Loans currently in the process of foreclosure may increase OREO in future quarters. It is not possible to accurately predict the future total of OREO because property sold at foreclosure may be acquired by third parties and OREO properties are regularly marketed and sold. The Company continues to monitor risk levels within the loan portfolio. If the Company's market experiences an economic downturn, real estate values could decline and foreclosure activity could increase. A decline in value may result in loss recognition for OREO, while an increase in foreclosures may increase the number of OREO properties.

## Net Interest Income

The following table shows interest-earning assets and interest-bearing liabilities, the interest earned or paid, the average yield or rate on the daily average balance outstanding, net interest income and net yield on average interest-earning assets for the periods indicated.

	Three Months Ended March 31,					
	2023			2022		
	Average Balance	Interest	Average Yield/Rate	Average Balance	Interest	Average Yield/Rate
<b>Interest-earning assets:</b>						
Loans <sup>(1)(2)(3)(4)</sup>	\$ 855,093	\$ 9,414	4.46 %	\$ 803,693	\$ 8,181	4.13 %
Taxable securities <sup>(5)(6)</sup>	678,543	4,118	2.46 %	628,311	2,473	1.60 %
Nontaxable securities <sup>(1)(5)</sup>	67,335	493	2.97 %	76,709	574	3.03 %
Interest-bearing deposits	19,715	228	4.69 %	114,254	49	0.17 %
Total interest-earning assets	\$ 1,620,686	\$ 14,253	3.57 %	\$ 1,622,967	\$ 11,277	2.82 %
<b>Interest-bearing liabilities:</b>						
Interest-bearing demand deposits	\$ 856,591	\$ 2,373	1.12 %	\$ 886,829	\$ 580	0.27 %
Savings deposits	208,376	81	0.16 %	212,920	38	0.07 %
Time deposits	91,666	359	1.59 %	77,989	37	0.19 %
Borrowings	23,962	285	4.82 %	-	-	-
Total interest-bearing liabilities	\$ 1,180,595	\$ 3,098	1.06 %	\$ 1,177,738	\$ 655	0.23 %
Net interest income and interest rate spread		\$ 11,155	2.51 %		\$ 10,622	2.59 %
Net yield on average interest-earning assets			2.79 %			2.65 %

<sup>(1)</sup> Interest on nontaxable loans and securities is computed on a fully taxable equivalent basis using a Federal income tax rate of 21%.

<sup>(2)</sup> Included in interest income are loan fees of \$40 for the three months ended March 31, 2023. For the three months ended March 31, 2022, interest income included loan fees of \$88.

<sup>(3)</sup> Nonaccrual loans are included in average balances for yield computations.

<sup>(4)</sup> Includes loans held for sale.

<sup>(5)</sup> Daily averages are shown at amortized cost.

<sup>(6)</sup> Includes restricted stock.

Federal Reserve interest rate increases beginning in March 2022 expanded interest income when results for the three months ended March 31, 2023 are compared with results for the three months ended March 31, 2022. During the first quarter of 2023, the Company responded to increased competition for deposits with a CD promotion and other deposit rate increases. Also during the first quarter of 2023, the Company obtained temporary advances from the FHLB that were repaid due to the success of the deposit strategy.

## Noninterest Income

	Three Months Ended March 31,		
	2023	2022	Percent Change
Service charges on deposits	\$ 592	\$ 562	5.34 %
Other service charges and fees	53	55	(3.64) %
Credit and debit card fees, net	467	440	6.14 %
Trust income	445	443	0.45 %
BOLI income	239	238	0.42 %
Gain on sale of mortgage loans	16	61	(73.77) %
Other income	375	492	(23.78) %
Gain on sale of securities	12	-	100.00 %
Total noninterest income	\$ 2,199	\$ 2,291	(4.02) %

The decrease in total noninterest income is primarily attributable to a decrease in the gain on sale of mortgage loans and other income. Federal Reserve interest rate increases, beginning in 2022, have dampened real estate refinance and purchase financing activity. Other income includes revenue from investment and insurance sales, adjustments to partnership basis and other miscellaneous components. These areas fluctuate with market conditions and competitive factors. Other income decreased for the three month period ended March 31, 2023 compared to the same period in 2022 due to a decrease in income from partnership interests.

## Noninterest Expense

	Three Months Ended March 31,		
	2023	2022	Percent Change
Salaries and employee benefits	\$ 4,434	\$ 3,978	11.46 %
Occupancy, furniture and fixtures	542	492	10.16 %
Data processing and ATM	873	787	10.93 %
FDIC assessment	117	111	5.41 %
Net costs of other real estate owned	11	10	10.00 %
Franchise taxes	375	362	3.59 %
Professional services	753	225	234.67 %
Other operating expenses	559	648	(13.73) %
Total noninterest expense	\$ 7,664	\$ 6,613	15.89 %

The increase in total noninterest expense is primarily attributable to salaries and employee benefits expense and professional services expense.

Salaries and employee benefits includes employee salaries, payroll taxes, insurance and fringe benefits, ESOP contribution accruals, the service component of net periodic pension cost, and salary continuation expenses. The expense increased when the three month period ended March 31, 2023 are compared with the same period ended March 31, 2022. Like many employers, the Company faced challenges to hiring enough qualified employees in recent years. Since increasing its starting salary in 2022, the Company has been able to attract a better pool of applicants and fill needed positions.

Professional services expense increased primarily due to the \$441 expense incurred to respond to the previously mentioned proxy contest.

## Income Tax

Income tax expense was \$948 for the three months ended March 31, 2023 and \$1,053 for the same period of 2022. The Company's federal statutory tax rate is 21%. The Company's effective tax rate was 17.30% for the three month period ended March 31, 2023, compared with 17.73% for the three month period ended March 31, 2022.

## Balance Sheet

Year-to-date daily averages for the major balance sheet categories are as follows:

<b>Assets</b>	<b>March 31, 2023</b>	<b>December 31, 2022</b>	<b>Percent Change</b>
Interest-bearing deposits	\$ 19,715	\$ 88,963	(77.84) %
Securities available for sale, at fair value	645,097	683,183	(5.57) %
Loans, net of unearned income and deferred fees and costs and the allowance for credit losses	844,411	825,110	2.34 %
Total assets	1,625,041	1,705,614	(4.72) %
<b>Liabilities and stockholders' equity</b>			
Noninterest-bearing demand deposits	\$ 308,908	\$ 338,269	(8.68) %
Interest-bearing demand deposits	856,591	910,989	(5.97) %
Savings deposits	208,376	216,414	(3.71) %
Time deposits	91,666	77,686	18.00 %
Stockholders' equity	123,996	145,641	(14.86) %

The declines in interest-bearing deposits and non-time customer deposits were the result of increased competition for customer deposits. The decline in stockholders' equity resulted from other comprehensive loss related to the securities available for sale portfolio. Changes in securities, loans and deposits are discussed below.

## Securities

	<b>March 31, 2023</b>	<b>December 31, 2022</b>	<b>Percent Change</b>
Amortized cost	\$ 739,265	\$ 759,917	(2.72) %
Unrealized loss	(88,218)	(103,065)	14.41 %
Securities available for sale	\$ 651,047	\$ 656,852	(0.88) %

Securities available for sale are presented at fair value as of each reporting date. During the three months ended March 31, 2023, the amortized cost of securities available for sale decreased from December 31, 2022 by \$20,652, while a partial reversal of unrealized losses increased the fair value from December 31, 2022. The decrease in amortized cost was primarily due to sale of securities with an amortized cost of \$17,987, which resulted in a net gain of \$12. The sales were part of the Company's interest rate risk management strategy.

Most of the Company's securities were purchased during periods prior to the Federal Reserve's interest rate increases that began in March of 2022. The fair value of bonds moves inversely to interest rate changes, as well as expectations of interest rate changes. The Company's Asset Liability Management Committee is closely monitoring interest rate risk on all of the Company's financial assets and liabilities. At this time, there are no credit risk concerns on securities available for sale and no associated ACL. Please refer to Note 1: General and Note 3: Securities for additional information.

## Loans

	<b>March 31, 2023</b>	<b>December 31, 2022</b>	<b>Percent Change</b>
Real estate construction loans	\$ 54,052	\$ 54,579	(0.97) %
Consumer real estate loans	223,438	221,052	1.08 %
Commercial real estate loans	438,843	437,888	0.22 %
Commercial non real estate loans	60,516	57,652	4.97 %
Public sector and IDA	47,359	48,074	(1.49) %
Consumer non real estate	33,188	33,948	(2.24) %
Less: unearned income and deferred fees and costs	(431)	(449)	4.01 %
Loans, net of unearned income and deferred fees and costs	\$ 856,965	\$ 852,744	0.49 %

Loans increased slightly from December 31, 2022. Loan demand has contracted under current economic conditions but the Company is positioned to continue to make every loan that meets its underwriting standards.

### Deposits

	<b>March 31, 2023</b>	<b>December 31, 2022</b>	<b>Percent Change</b>
Noninterest-bearing demand deposits	\$ 311,137	\$ 327,713	(5.06)%
Interest-bearing demand deposits	871,748	933,269	(6.59)%
Saving deposits	202,996	214,114	(5.19)%
Time deposits	125,571	67,629	85.68%
<b>Total deposits</b>	<b>\$ 1,511,452</b>	<b>\$ 1,542,725</b>	<b>(2.03)%</b>

The Company's deposits experienced increased competitive pressure during the first quarter of 2023, continuing a trend that began impacting the Company during the fourth quarter of 2022. The Company responded to the trend early in the quarter with special CD offering rates, as well as improved rates on other deposits that substantially reversed the trend later in the quarter, at costs well below the cost of borrowing.

The Company's deposit base is diverse, including individuals, businesses and municipalities within its market area. The Company does not have any brokered deposits. Depositors are insured up to the FDIC maximum of \$250 thousand. Municipal deposits, which account for approximately one-fourth of the Company's deposits, have additional security from bonds pledged as collateral, in accordance with state regulation. Of the Company's non-municipal deposits, approximately 24% are uninsured.

### Liquidity

Liquidity measures the Company's ability to meet its financial commitments at a reasonable cost. Demands on the Company's liquidity include funding additional loan demand and accepting withdrawals of existing deposits. The Company has diverse liquidity sources, including customer and purchased deposits, customer repayments of loan principal and interest, sales, calls and maturities of securities, Federal Reserve discount window borrowing, short-term borrowing, and FHLB advances. During the first quarter of 2023, the Company accessed FHLB borrowings to reinforce liquidity. The advances were fully repaid during March 2023, due to the success of the Company's deposit strategy. As of March 31, 2023, the Company did not have purchased deposits, discount window borrowings or short-term borrowings.

The Company considers its security portfolio for typical liquidity needs, within accounting, legal and strategic parameters. Portions of the securities portfolio are pledged to meet state requirements for public funds deposits. Discount window borrowings also require pledged securities. Increased/decreased liquidity from public funds deposits or discount window borrowings results in increased/decreased liquidity from pledging requirements. The Company monitors public funds pledging requirements and unpledged available for sale securities accessible for liquidity needs.

Regulatory capital levels determine the Company's ability to use purchased deposits and the Federal Reserve discount window. As of March 31, 2023, the Company is considered well capitalized and does not have any restrictions on purchased deposits or borrowing ability at the Federal Reserve discount window.

As of March 31, 2023, the Company had \$402,089 of borrowing capacity from the FHLB and an unsecured federal funds line of credit with an unaffiliated bank of \$10,000, with no amounts advanced against those lines. Additionally, the Company had \$15,629 of unused capacity at the Federal Reserve Bank discount window. In an abundance of caution, the Company pledged additional securities to the Federal Reserve Bank discount window during April 2023, increasing borrowing capacity to \$67,878 as of April 30, 2023.

The Company monitors factors that may increase its liquidity needs. Some of these factors include deposit trends, large depositor activity, maturing deposit promotions, interest rate sensitivity, maturity and repricing timing gaps between assets and liabilities, the level of unfunded loan commitments and loan growth. As of March 31, 2023, the Company's liquidity is sufficient to meet projected trends.

To monitor and estimate liquidity levels, the Company performs stress testing under varying assumptions on credit sensitive liabilities and the sources and amounts of balance sheet and external liquidity available to replace outflows. The Company's Contingency Funding Plan sets forth avenues for rectifying liquidity shortfalls. As of March 31, 2023, the analysis indicated adequate liquidity under the tested scenarios.

The Company utilizes several other strategies to maintain sufficient liquidity. Loan and deposit growth are managed to keep the loan to deposit ratio within the Company's internally-set target range. As of March 31, 2023, the loan to deposit ratio was 56.70%. The investment strategy takes into consideration the term of the investment, and securities in the available for sale portfolio are laddered based upon projected funding needs.



## **Capital Resources**

Total stockholders' equity at March 31, 2023 was \$131,043, an increase of \$8,356, or 6.81%, from the \$122,687 at December 31, 2022. The increase in stockholders' equity reflects net income for the three months ended March 31, 2023, reduced by payment of a special one-time cash dividend, and increased by improvement in the unrealized loss on securities available for sale.

During the first quarter of 2023, the Company paid a special one-time cash dividend of \$1.00 per common share. The dividend rewarded stockholders for the Company's positive performance during 2022, which included a one-time gain on the sale of a private equity investment.

The Company qualifies as a small bank holding company under the Federal Reserve's Small Bank Holding Company Policy Statement, which exempts bank holding companies with less than \$3 billion in assets from reporting consolidated regulatory capital ratios and from minimum regulatory capital requirements. NBB is subject to various capital requirements administered by banking agencies, including an additional capital conservation buffer in order to make capital distributions or discretionary bonus payments. Risk-based capital ratios are calculated in compliance with OCC rules based on the Basel III Capital Rules. The Bank's ratios are well above the required minimums as of March 31, 2023. Risk based capital ratios for NBB are shown in the following tables.

	<b>NBB</b>	<b>Regulatory Capital Minimum Ratios</b>	<b>Regulatory Capital Minimum Ratios with Capital Conservation Buffer</b>
Common Equity Tier I Capital Ratio	<b>17.00%</b>	4.50%	7.00%
Tier I Capital Ratio	<b>17.00%</b>	6.00%	8.50%
Total Capital Ratio	<b>18.00%</b>	8.00%	10.50%
Leverage Ratio	<b>11.01%</b>	4.00%	4.00%

## **Off-Balance Sheet Arrangements**

In the normal course of business, NBB extends lines of credit and letters of credit to its customers. Depending on their needs, customers may draw upon lines of credit at any time in any amount up to a pre-approved limit. Financial letters of credit guarantee payments to facilitate customer purchases. Performance letters of credit guarantee payment if the customer fails to complete a specific obligation.

While it would be possible for customers to fully draw on approved lines of credit and for beneficiaries to call all letters of credit, historically this has not occurred. In the event of a sudden and substantial draw on these lines, the Company would be able to access multiple options, including its lines of credit with correspondents, raising additional deposits, or selling securities available for sale or loans. The Company estimates an ACL on unfunded loan commitments under the CECL model.

The Company sells mortgages on the secondary market. Our agreement with the purchaser provides for strict underwriting and documentation requirements. Violation of the representations and warranties of the agreement would entitle the purchaser to recourse provisions. The Company has determined that its risk in this area is not significant because of a low volume of secondary market mortgage loans and high underwriting standards. The Company estimates a potential loss reserve for recourse provisions that is not material as of March 31, 2023. To date, no recourse provisions have been invoked. If funds were needed, the Company would access the same sources as noted above for funding lines and letters of credit. There were no material changes in off-balance sheet arrangements during the three months ended March 31, 2023.

## **Contractual Obligations**

The Company had no finance lease or purchase obligations and no long-term debt at March 31, 2023.

## **Item 3. Quantitative and Qualitative Disclosures About Market Risk**

Not applicable.

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#### **Item 4. Controls and Procedures**

The Company's management evaluated, with the participation of the Company's principal executive officer and principal financial officer, the effectiveness of the Company's disclosure controls and procedures (as defined in Rule 13a-15(e)) under the Securities Exchange Act of 1934, as amended (the "Exchange Act") as of the end of the period covered by this report. Based on that evaluation, the Company's principal executive officer and principal financial officer concluded that the Company's disclosure controls and procedures are effective as of March 31, 2023 to ensure that information required to be disclosed in the reports that the Company files or submits under the Exchange Act is recorded, processed, summarized and reported, within the time periods specified by the Company's management, including the Company's principal executive officer and principal financial officer, as appropriate, to allow timely decisions regarding required disclosure.

Effective January 1, 2023, the Company adopted ASC 326, Financial Instruments – Credit Losses. The Company implemented changes to the policies, processes, and controls over the estimation of the allowance for credit losses to support the adoption of ASC 326. Many controls under this new standard mirror controls under prior GAAP. New controls were established over the review of economic forecasting projections obtained from independent third parties. Except as related to the adoption of ASC 326, there were no changes in the Company's internal control over financial reporting (as defined in Rule 13a-15(f) of the Exchange Act) that occurred during the three months ended March 31, 2023, that have materially affected, or are reasonably likely to materially affect, the Company's internal control over financial reporting.

Because of the inherent limitations in all control systems, the Company believes that no system of controls, no matter how well designed and operated, can provide absolute assurance that all control issues have been detected.

#### **Part II**

#### **Other Information**

##### **Item 1. Legal Proceedings**

There are no pending or threatened legal proceedings to which the Company or any of its subsidiaries is a party or to which the property of the Company or any of its subsidiaries is subject that, in the opinion of Management, may materially impact the financial condition of the Company.

##### **Item 1A. Risk Factors**

Please refer to the "Risk Factors" previously disclosed in Item 1A of our 2022 Annual Report on Form 10-K and the factors discussed under "Cautionary Statement Regarding Forward-Looking Statements" in Part I. Item 2 of this Form 10-Q.

##### **Item 2. Unregistered Sales of Equity Securities and Use of Proceeds**

None.

##### **Item 3. Defaults Upon Senior Securities**

None.

##### **Item 4. Mine Safety Disclosures**

Not applicable.

##### **Item 5. Other Information**

None.

##### **Item 6. Exhibits**

## Index of Exhibits

<b>Exhibit No.</b>	<b>Description</b>	
3(i)	Amended and Restated Articles of Incorporation of National Bankshares, Inc.	(incorporated herein by reference to Exhibit 3.1 of the Form 8-K filed on March 16, 2006)
3(ii)	Amended and Restated Bylaws of National Bankshares, Inc.	(incorporated herein by reference to Exhibit 3(ii) of the Form 8-K filed on January 11, 2023)
4	Specimen copy of certificate for National Bankshares, Inc. common stock	(incorporated herein by reference to Exhibit 4(a) of the Annual Report on Form 10-K for fiscal year ended December 31, 1993)
+31(i)	Section 302 Certification of Chief Executive Officer	Filed herewith
+31(ii)	Section 302 Certification of Chief Financial Officer	Filed herewith
+32(i)	18 U.S.C. Section 1350 Certification of Chief Executive Officer	Filed herewith
+32(ii)	18 U.S.C. Section 1350 Certification of Chief Financial Officer	Filed herewith
+101	The following materials from National Bankshares, Inc.'s Quarterly Report on Form 10-Q for the period ended March 31, 2023 are formatted in iXBRL (Inline Extensible Business Reporting Language), furnished herewith: (i) Consolidated Balance Sheets at March 31, 2023 and December 31, 2022; (ii) Consolidated Statements of Income for the three month periods ended March 31, 2023 and 2022; (iii) Consolidated Statements of Comprehensive Income (Loss) for the three month periods ended March 31, 2023 and 2022; (iv) Consolidated Statements of Changes in Stockholders' Equity for the three month periods ended March 31, 2023 and 2022; (v) Consolidated Statements of Cash Flows for the three month periods ended March 31, 2023 and 2022; and (vi) Notes to Consolidated Financial Statements.	Filed herewith
104	Cover Page Interactive Data File (formatted in Inline XBRL and contained in Exhibit 101)	Filed herewith

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**Signatures**

Pursuant to the requirements of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned thereunto duly authorized.

NATIONAL BANKSHARES, INC.

Date: May 11, 2023

/s/ F. Brad Denardo

By: F. Brad Denardo  
Chairman, President and  
Chief Executive Officer  
(Principal Executive Officer)

Date: May 11, 2023

/s/ Lora M. Jones

By: Lora M. Jones  
Treasurer and  
Chief Financial Officer  
(Principal Financial Officer)  
(Principal Accounting Officer)

CERTIFICATIONS

I, F. Brad Denardo, certify that:

1. I have reviewed this quarterly report on Form 10-Q of National Bankshares, Inc.;
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;
4. The registrant's other certifying officer(s) and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:
  - (a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
  - (b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;
  - (c) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
  - (d) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and
5. The registrant's other certifying officer(s) and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):
  - (a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and
  - (b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: May 11, 2023

/s/ F. Brad Denardo

F. Brad Denardo  
Chairman, President and Chief Executive Officer  
(Principal Executive Officer)

CERTIFICATIONS

I, Lora M. Jones, certify that:

1. I have reviewed this quarterly report on Form 10-Q of National Bankshares, Inc.;
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;
4. The registrant's other certifying officer(s) and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:
  - (a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
  - (b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;
  - (c) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
  - (d) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and
5. The registrant's other certifying officer(s) and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):
  - (a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and
  - (b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: May 11, 2023

/s/ Lora M. Jones  
Lora M. Jones  
Treasurer and  
Chief Financial Officer  
(Principal Financial Officer)

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Exhibit 32 (i)

CERTIFICATION OF CHIEF EXECUTIVE OFFICER  
PURSUANT TO 18 U.S.C. SECTION 1350

In connection with the Form 10-Q of National Bankshares, Inc. for the quarter ended March 31, 2023, I, F. Brad Denardo, Chairman, President and Chief Executive Officer (Principal Executive Officer) of National Bankshares, Inc., hereby certify pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, to the best of my knowledge and belief, that:

(1) such Form 10-Q for the quarter ended March 31, 2023, fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934; and

(2) the information contained in such Form 10-Q for the quarter ended March 31, 2023, fairly presents, in all material respects, the financial condition and results of operations of National Bankshares, Inc.

/s/ F. Brad Denardo

F. Brad Denardo  
Chairman, President and Chief Executive Officer  
(Principal Executive Officer)  
May 11, 2023

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Exhibit 32 (ii)

CERTIFICATION OF CHIEF FINANCIAL OFFICER  
PURSUANT TO 18 U.S.C. SECTION 1350

In connection with the Form 10-Q of National Bankshares, Inc. for the quarter ended March 31, 2023, I, Lora M. Jones, Treasurer and Chief Financial Officer (Principal Financial Officer) of National Bankshares, Inc., hereby certify pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, to the best of my knowledge and belief, that:

(1) such Form 10-Q for the quarter ended March 31, 2023, fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934; and

(2) the information contained in such Form 10-Q for the quarter ended March 31, 2023, fairly presents, in all material respects, the financial condition and results of operations of National Bankshares, Inc.

/s/ Lora M. Jones

Lora M. Jones  
Treasurer and  
Chief Financial Officer  
(Principal Financial Officer)  
May 11, 2023