

FIRSTBANCSHARES
OF TEXAS, INC.

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Third Quarter 2016 Shareholders' Report

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Dear Shareholders

As I write this 3rd quarter report, we are one day away from “Election Day”. I thought it would never come! Regardless of the outcome, we will finally see an end to uncertainty and the country can hopefully move forward with the necessary work needed to deal with the challenges we face.

The Company completed another solid quarter resulting in a good first nine months. Through the first nine months of the year, earnings were \$6.7 million representing a \$1.8 million increase over the same nine month period in 2015. This represented a 36.7% improvement over last year. We continue to see some weakness in some of our Midland energy customers, but all are still performing and with the improvement in energy prices over the last 60 days. We are hopeful most, if not all of these companies will make it through this cycle. Many of our oilfield service company customers are showing signs of improvement within the last two months due to an increase in drilling activity.

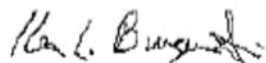
We are starting to see signs of renewed asset growth recently. As of September 30, 2016, Total Assets stood at \$971.7 million vs. \$961.2 million at year end 2015 and \$954.2 million at September 30, 2015. As of the time this letter is being written, Total Assets have grown to just under \$1.0 billion.

We have purposefully slowed loan growth this year as we wait for economic conditions to improve. Loans are down from \$680.9 million at year end 2015 to \$669.7 million. However, they are up from \$652.6 million at September 30, 2015.

We officially opened our Horseshoe Bay branch in September and we are seeing good growth so far. As of September 30, we had slightly over \$15 million in deposits and close to \$11.0 million in loans on the books. We have developed a strong presence in the market already through the efforts of our new Horseshoe Bay bank team. Everyone has become involved in some aspect of the market already, both in Horseshoe Bay and Marble Falls.

As we approach the holiday season, we hope all is well with your families and we hope you are able to spend some quality time together.

Sincerely,



Ken L. Burgess, Jr.
CEO & President

FIRST BANCSHARES OF TEXAS, INC.

CONSOLIDATED STATEMENT OF FINANCIAL CONDITION

(Dollar amounts in thousands)

	September 30,		December 31,
	(Unaudited)	(Unaudited)	(Audited)
	<u>2016</u>	<u>2015</u>	<u>2015</u>
ASSETS			
Cash and due from banks	\$ 12,938	\$ 8,818	\$ 10,541
Federal funds sold	9,868	11,000	3,514
Cash and cash equivalents	<u>22,806</u>	19,818	14,055
Interest bearing deposits in banks	87,925	52,146	48,828
Securities available for sale, at fair value	22,713	24,841	24,204
Securities held to maturity	124,048	158,575	147,049
Investment in First Bancshares of Texas Statutory Trust I	93	93	93
Investment in FirstCapital GP, LLC	808	840	846
Investments in partnerships	1,628	1,138	1,343
Restricted investment held at cost	2,194	1,956	1,957
Loans held for sale	2,285	5,342	4,382
Loans and leases receivable, net of allowance for loan and lease losses	669,755	652,580	680,975
Accrued interest receivable	2,743	2,856	3,491
Premises and equipment	21,644	21,445	21,320
Deferred tax asset, net	3,863	3,222	3,430
Foreclosed assets	33	73	-
Cash surrender value of life insurance	8,356	8,106	8,169
Prepaid FDIC assessment	-	-	-
Other assets	857	1,202	1,089
TOTAL ASSETS	<u>\$ 971,751</u>	<u>\$ 954,233</u>	<u>\$ 961,231</u>
LIABILITIES AND SHAREHOLDERS' EQUITY			
Non-interest bearing deposits	\$ 234,484	\$ 235,464	\$ 244,784
Interest bearing deposits	588,947	583,482	575,138
Total deposits	<u>823,431</u>	818,946	819,922
Accrued expenses and other liabilities	2,959	2,368	2,561
Securities sold under agreement to repurchase	39,006	39,108	42,902
Subordinated debentures	3,093	3,093	3,093
Other borrowed funds	5,223	1,125	1,113
Total liabilities	<u>873,712</u>	864,640	869,591
SHAREHOLDERS' EQUITY			
Common stock	9,510	9,466	9,477
Preferred stock	883	937	937
Treasury stock, at cost	-	-	-
Surplus			
Common	32,457	32,016	32,117
Preferred	7,909	8,400	8,400
Capital Surplus	<u>40,366</u>	40,416	40,517
Retained earnings	46,671	38,284	40,235
Accumulated other comprehensive income - unrealized gain on available for sale securities, net of tax	609	490	474
Accumulated other comprehensive income - unrealized loss on securities transferred from available for sale to held to maturity, net of tax	-	-	-
Total shareholders' equity	<u>98,039</u>	89,593	91,640
TOTAL LIABILITIES AND SHAREHOLDERS' EQUITY	<u>\$ 971,751</u>	<u>\$ 954,233</u>	<u>\$ 961,231</u>

FIRST BANCSHARES OF TEXAS, INC.

CONSOLIDATED STATEMENT OF INCOME

For the Nine Months Ended September

(Dollar amounts in thousands)

	(Unaudited)	(Unaudited)
	<u>2016</u>	<u>2015</u>
Interest Income:		
Loans and leases, including fees	\$ 27,892	\$ 24,943
Debt Securities		
Taxable	2,032	2,250
Tax exempt	941	851
Federal funds sold	31	25
Deposits with banks	429	584
Other interest	299	97
TOTAL INTEREST INCOME	<u>31,624</u>	<u>28,750</u>
Interest Expense:		
Deposits	2,078	2,340
Other borrowed money	370	280
Subordinated debentures	82	73
TOTAL INTEREST EXPENSE	<u>2,530</u>	<u>2,693</u>
Net Interest Income (Loss)	29,094	26,057
Provision for loan and lease losses	<u>1,673</u>	<u>2,105</u>
Net Interest Income (Loss) After Provision	<u>27,421</u>	<u>23,952</u>
Non-Interest Income:		
Trust department income	278	283
Service charges on deposit accounts	802	554
Other service charges and fees	560	627
Net realized gain (loss) on sales of securities	-	403
Appreciation in cash surrender value of life insurance	187	184
Gain/Loss on sale of loans	889	1,083
Gain/Loss on sale of foreclosed assets	-	-
Gain/Loss on sale of fixed assets	10	7
TOTAL NON-INTEREST INCOME	<u>2,726</u>	<u>3,141</u>
Non-Interest Expenses:		
Salaries and employee benefits	12,237	11,892
Occupancy and equipment expense	3,097	3,127
Advertising	385	373
Community and philanthropic support	218	174
IT and data processing expense	664	606
Legal, professional, accounting, and exam fees	825	978
FDIC assessment	405	407
Reduction in value of foreclosed assets	-	-
Other expenses	2,490	2,458
TOTAL NON-INTEREST EXPENSES	<u>20,321</u>	<u>20,015</u>
Income Before Income Taxes	9,826	7,078
Income tax expense	<u>3,117</u>	<u>2,153</u>
NET INCOME	<u>\$ 6,709</u>	<u>\$ 4,925</u>

FIRST BANCSHARES OF TEXAS, INC.

THIRD QUARTER CONSOLIDATED FINANCIAL HIGHLIGHTS

(Dollar amounts in thousands)

Earnings Summary

For the Nine Months Ended September 30		<u>2016</u>		<u>2015</u>
Interest Income	\$	31,624	\$	28,750
Interest Expense		2,530		2,693
Provision for loan losses		1,673		2,105
Net Income		6,709		4,925

Performance Ratios (annualized)

For the Nine Months Ended September 30		<u>2016</u>		<u>2015</u>
Return on Average Assets		0.92%		0.68%
Return on Common Shareholders' Average Equity		9.97%		7.98%
Net Interest Margin		4.22%		3.81%

Period-End Data

As of September 30		<u>2016</u>		<u>2015</u>
Total Assets	\$	971,751	\$	954,233
Average Assets		976,929		969,767
Investments*		239,409		239,589
Loans, net		672,040		657,922
Deposits		823,431		818,946
Shareholders' Equity				
Common		89,247		80,256
Preferred		8,792		9,337

Per Share Data

For the Nine Months Ended September 30		<u>2016</u>		<u>2015</u>
Net Income	\$	0.68	\$	0.49
Book Value	\$	9.38	\$	8.47
Number of Shareholders				
Common		510		495
Preferred		83		86

*Includes interest-bearing deposits in banks, securities, investments in subsidiaries, investments in partnerships, and restricted investments held at cost

FIRST BANCSHARES OF TEXAS, INC.

CONSOLIDATED YIELD ANALYSIS (Dollar amounts in thousands)

	September 30,					
	(Unaudited) 2016			(Unaudited) 2015		
	Avg. Balance	Interest Inc./Exp.	Yield/Cost	Avg. Balance	Interest Inc./Exp.	Yield/Cost
ASSETS						
Interest-bearing deposits	\$ 68,037	\$ 429	0.84%	\$ 129,832	\$ 583	0.60%
Federal funds sold and resell agreements	7,415	31	0.56%	11,187	25	0.30%
Securities:						
Taxable	115,984	2,032	2.34%	132,651	2,250	2.26%
Tax-exempt	44,992	941	2.79%	40,304	851	2.82%
Total securities	<u>160,976</u>	<u>2,973</u>	2.46%	<u>172,955</u>	<u>3,101</u>	2.39%
Restricted investments held at cost	3,616	299	11.05%	3,044	97	4.28%
Loans, net of unearned discount	697,147	27,892	5.34%	612,116	24,943	5.45%
Total earning assets and average rate earned	<u>937,191</u>	<u>31,624</u>	4.51%	<u>929,135</u>	<u>28,750</u>	4.14%
Cash and due from banks	11,607			10,796		
Investments in subsidiaries	924			932		
Premises and equipment, net	21,616			21,852		
Accrued interest receivable and other assets	5,591			7,052		
Total assets	<u>\$ 976,929</u>			<u>\$ 969,767</u>		
LIABILITIES						
Interest-bearing deposits:						
NOW & MMA	\$ 225,211	\$ 358	0.21%	\$ 183,691	\$ 289	0.21%
Savings	46,361	90	0.26%	47,102	111	0.32%
COD	306,254	1,630	0.71%	347,144	1,940	0.75%
Total interest-bearing deposits	<u>577,826</u>	<u>2,078</u>	0.48%	<u>577,936</u>	<u>2,340</u>	0.54%
Non-interest bearing demand deposits	230,474			241,565		
Total deposits	<u>808,300</u>	<u>2,078</u>		<u>819,501</u>	<u>2,340</u>	
Securities sold under agreement to repurchase	63,177	322	0.68%	56,379	263	0.62%
Other borrowed funds	3,862	48	1.66%	1,143	17	2.04%
Subordinated debentures	3,093	82	3.54%	3,093	73	3.16%
Total interest-bearing liabilities and average rate paid	<u>647,958</u>	<u>2,530</u>	0.52%	<u>638,551</u>	<u>2,693</u>	0.56%
Accrued expenses and other liabilities	3,048			2,287		
Total liabilities	<u>881,480</u>			<u>882,403</u>		
Shareholders' equity	<u>95,449</u>			<u>87,364</u>		
Total liabilities and shareholders' equity	<u>\$ 976,929</u>			<u>\$ 969,767</u>		
Net interest income		<u>\$ 29,094</u>			<u>\$ 26,057</u>	
Net interest spread			<u>3.99%</u>			<u>3.57%</u>
Net interest margin			<u>4.22%</u>			<u>3.81%</u>

For these computations:

- (i) average balances are presented on a daily average basis,
- (ii) information is shown on a tax-equivalent basis assuming a 34% tax rate,
- (iii) average loans include loans on non-accrual status, and
- (iv) average securities include unrealized gains and losses on securities available for sale, while yields are based on average amortized cost

MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

Introduction

As a bank financial holding company, we generate most of our revenue from interest on loans and investments, trust fees, fees from the sale of mortgage loans and service charges on our deposits. Our primary source of funding for our loans and investments are deposits held by our bank. Our largest expenses are interest on these deposits and salaries and related employee benefits. We usually measure our performance by calculating our return on average assets, return on average equity, our regulatory leverage and risk based capital ratios and our efficiency ratio, which is calculated by dividing non-interest expense by the sum of net interest income (on a tax equivalent basis) and non-interest income.

Critical Accounting Policies

We prepare consolidated financial statements based on the selection of certain accounting policies, generally accepted accounting principles and customary practices in the banking industry. These policies, in certain areas, require us to make significant estimates and assumptions.

We deem a policy critical if (1) the accounting estimate required us to make assumptions about matters that are highly uncertain at the time we make the accounting estimate; and (2) different estimates that reasonably could have been used in the current period, or changes in the accounting estimate that are reasonably likely to occur from period to period, would have a material impact on the financial statements.

The following discussion addresses (1) our allowance for loan losses and its provision for loan losses and (2) our valuation of securities, which we deem to be our most critical accounting policies. We have other significant accounting policies and continue to evaluate the materiality of their impact on our consolidated financial statements, but we believe these other policies either do not generally require us to make estimates and judgments that are difficult or subjective, or it is less likely they would have a material impact on our reported results for a given period.

Allowance for Loan Losses:

The allowance for loan losses is established through a provision for loan losses charged to expense. Loans are charged against the allowance for loan losses when management believes the collectability of the principal is unlikely.

The allowance is an amount management believes is appropriate to absorb estimated inherent losses on existing loans that are deemed uncollectible based upon management's review and evaluation of the loan portfolio. The allowance for loan losses is comprised of three elements: (i) specific reserves determined in accordance with current authoritative accounting guidance based on probable losses on specific classified loans; (ii) general reserves determined in accordance with current authoritative accounting guidance that consider historical loss rates; and (iii) qualitative reserves determined in

accordance with current authoritative accounting guidance based upon general economic conditions and other qualitative risk factors both internal and external to the Company.

The allowance for loan losses is increased by charges to income and decreased by charge-offs (net of recoveries). Management's periodic evaluation of the appropriateness of the allowance is based on general economic conditions, the financial condition of borrowers, the value and liquidity of collateral, delinquency, prior loan loss experience, and the results of periodic reviews of the portfolio. For purposes of determining our general reserve, the loan portfolio, less cash secured loans, government guaranteed loans and classified loans, is multiplied by the Company's historical loss rate. The Company's methodology is constructed so that specific allocations are increased in accordance with deterioration in credit quality and a corresponding increase in risk of loss. In addition, the Company adjusts our allowance for qualitative factors such as current local economic conditions and trends, including unemployment, lending staff, policies and procedures, credit concentrations, trends and severity of problem loans and trends in volume and terms of loans. This additional allocation based on qualitative factors serves to compensate for additional areas of uncertainty inherent in our portfolio that are not reflected in our historic loss factors.

Although we believe we use the best information available to make loan loss allowance determinations, future adjustments could be necessary if circumstances or economic conditions differ substantially from the assumptions used in making our initial determinations. A downturn in the economy and employment could result in increased levels of non-performing assets and charge-offs, increased loan loss provisions and reductions in income. Additionally as an integral part of their examination process, bank regulatory agencies periodically review our allowance for loan losses. The bank regulatory agencies could require the recognition of additions to the loan loss allowance based on their judgment of information available to them at the time of their examination.

Accrual of interest is discontinued on a loan and payments applied to principal when management believes, after considering economic and business conditions and collection efforts, the borrower's financial condition is such that collection of interest is doubtful. Generally all loans past due greater than 90 days, based on contractual terms, are placed on non-accrual. Loans are returned to accrual status when all the principal and interest amounts contractually due are brought current and future payments are reasonably assured. Consumer loans are generally charged-off when a loan becomes past due 90 days. For other loans in the portfolio, facts and circumstances are evaluated in making charge-off decisions.

Loans are considered impaired when, based on current information and events, it is probable we will be unable to collect all amounts due in accordance with the original contractual terms of the loan agreement, including scheduled principal and interest payments. If a loan is impaired, a specific valuation allowance is allocated, if necessary. Interest payments on impaired loans are typically applied to principal unless collectability of the principal amount is reasonably assured, in which case interest is recognized on a cash basis. Impaired loans, or portions thereof, are charged-off when deemed uncollectible.

The Company's policy requires measurement of the allowance for an impaired collateral dependent loan based on the fair value of the collateral. Other loan impairments are measured based on the present value of expected future cash flows or the loan's observable market price.

From time to time, the Company modifies its loan agreement with a borrower. A modified loan is considered a troubled debt restructuring when two conditions are met: (i) the borrower is experiencing financial difficulty and (ii) concessions are made by the Company that would not otherwise be considered for a borrower with similar credit risk characteristics. Modifications to loan terms may include a lower interest rate, a reduction of principal, or a longer term to maturity. Each of these loans is evaluated for impairment and a specific reserve is recorded based on probable losses, taking into consideration the related collateral and modified loan terms and cash flow. As of September 30, 2016, troubled debt restructurings totaled \$8.7 million with \$96 thousand of the total also being classified as non-accrual.

Valuation of Securities:

Management classifies debt and equity securities as held-to-maturity or available-for-sale, based on its intent. Debt securities that management has the positive intent and ability to hold to maturity are classified as held-to-maturity and recorded at cost, adjusted for amortization of premiums and accretion of discounts, which are recognized as adjustments to interest income using the interest method. Securities not classified as held-to-maturity or trading are classified as available-for-sale and recorded at estimated fair value, with all unrealized gains and unrealized losses judged to be temporary, net of deferred income taxes, excluded from earnings and reported as a separate component of shareholders' equity. Available-for-sale securities that have unrealized losses that are judged other than temporary are included in gain (loss) on sale of securities and a new cost basis is established.

Fair value of these securities is determined based on methodologies in accordance with current authoritative accounting guidance. Fair values are volatile and may be influenced by a number of factors, including market interest rates, prepayment speeds, discount rates and yield curves. Fair values for our investment securities are based on quoted market prices, where available. If quoted market prices are not available, fair values are based on the quoted prices of similar instruments or an estimate of fair value by using a range of fair value estimates in the marketplace as a result of the illiquid market specific to the type of security.

When the fair value of a security is below its amortized cost, and depending on the length of time the condition exists and the extent the fair market value is below amortized cost, additional analysis is performed to determine whether an other-than-temporary impairment condition exists. Available-for-sale and held-to-maturity securities are analyzed quarterly for possible other-than-temporary impairment. The analysis considers (i) whether we have the intent to sell our securities before recovery or maturity, (ii) whether it is more likely than not that we will have to sell our securities before recovery or maturity, (iii) the length of time and extent to which the fair value has been less than costs, and (iv) the financial condition of the issuer. Often, the information available to conduct these assessments is limited and rapidly changing, making estimates of fair value subject to judgment.

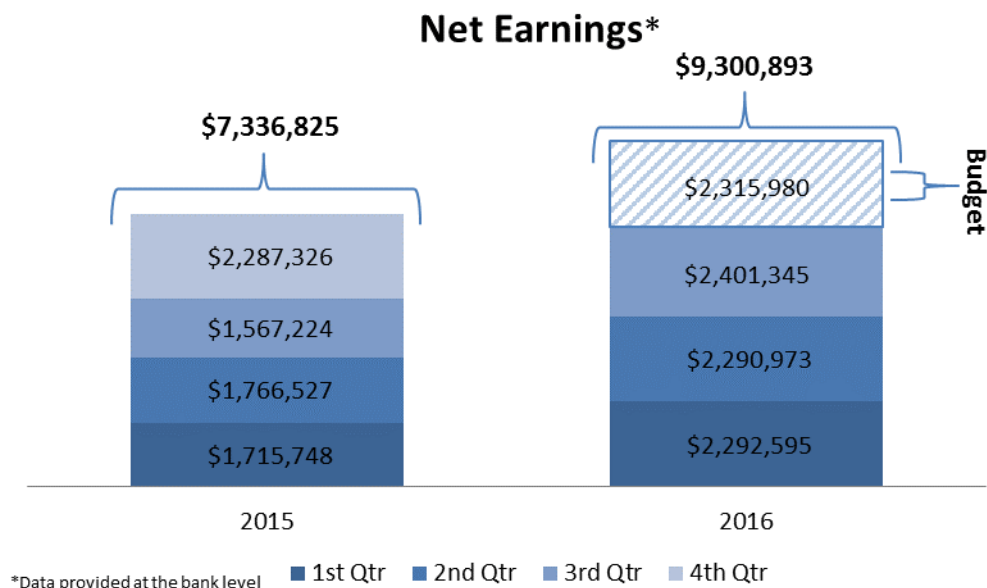
If actual information or conditions are different than estimated, the extent of the impairment of the security may be different than previously estimated, which could have a material effect on the Company's results of operations and financial condition.

The Company utilizes independent third party pricing services to value its investment securities. The Company reviews the prices supplied by the independent pricing services as well as the underlying pricing methodologies for reasonableness and to ensure such prices are aligned with traditional pricing matrices. The Company's investment portfolio consists of traditional investments, substantially all in U. S. Treasury securities, obligations of U. S. government-sponsored enterprises and agencies, mortgage pass-through securities, and general obligation or revenue based municipal bonds. Pricing for such securities is relatively straightforward and generally not difficult to obtain.

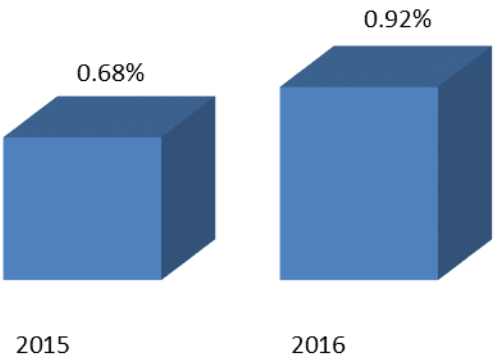
Results of Operations

Performance Summary:

We ended the third quarter with year-to-date net earnings at the consolidated level of \$6.7 million, an increase of approximately \$1.8 million compared to earnings through the third quarter in 2015. Return on average assets at the consolidated level as of September 30, 2016 and 2015 was .92% and .68%, respectively. The return on common shareholder's average equity for the same period was 9.97% and 7.98%. On a basic net earnings per share basis at the holding company level, net earnings were \$0.68 as of September 30, 2016 compared to \$0.49 for September 30, 2015.



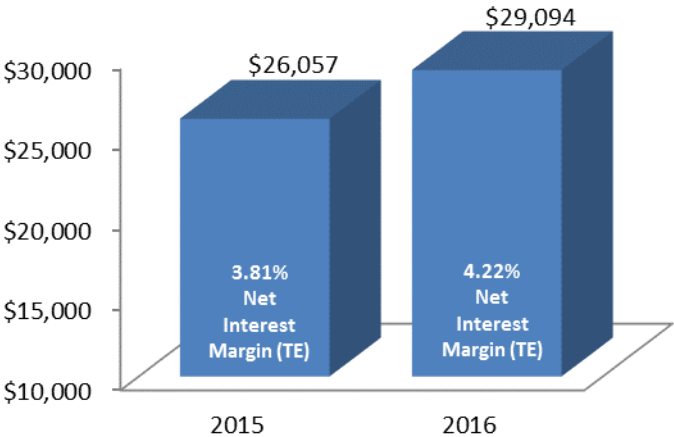
Return on Average Assets



Net Interest Income:

Net interest income is the difference between interest income on earning assets and interest expense on liabilities incurred to fund those assets. Our earning assets consist primarily of loans and investment securities. Our liabilities to fund those assets consist primarily of non-interest bearing and interest-bearing deposits. Net interest income was \$29.1 million for the nine months ended September 30, 2016 compared to \$26.1 million for the same period in 2015. This increase in net interest income period over period is primarily attributable to our loan growth. Loans grew by approximately \$18.2 million period over period resulting in interest income on loans (including fees) increasing by \$2.9 million for the period ending September 30, 2016 compared to the same period in 2015. Our year-to-date net interest margin at September 30, 2016 was 4.22%, which was higher compared to 3.81% for the same period in 2015. Net interest margin is calculated by dividing the Company’s net interest income by average earning assets for the period.

Net Interest Income & Net Interest Margin (\$000's)



Non-Interest Income:

Non-interest income for the nine month period ended September 30, 2016 was \$2.7 million, a decrease of \$415 thousand or 13.2% over the same period in 2015. The following schedule shows each of the major components of year-to-date non-interest income for the periods ended September 30, 2016 as compared to September 30, 2015.

Non-Interest Income	Year-to-Date September 30		Incr./ (Decr.)	% Change
	2016	2015		
Trust department income	\$278,288	\$283,417	(\$5,129)	(1.81)%
Service charges on deposit accounts	801,868	553,463	248,405	44.88 %
Other service charges and fees	560,872	626,471	(65,599)	(10.47)%
Appreciation in cash surrender value of life insurance	187,043	183,716	3,327	1.81 %
Gain/(Loss) on sale of securities	-	403,953	(403,953)	0.00 %
Gain/(Loss) on sale of loans	888,670	1,083,217	(194,547)	(17.96)%
Gain/(Loss) on sale of other real estate	-	0	-	0.00 %
Gain/(Loss) on sale of other assets	9,600	6,843	2,757	40.29 %
Total Non-Interest Income	\$2,726,342	\$3,141,080	(\$414,739)	(13.20)%

Trust department income for the nine month period ended September 30, 2016 was \$278 thousand. This was a decrease of \$5 thousand from the same period in 2015. Assets managed by the Wealth Management and Trust Division totaled \$54.2 million as of September 30, 2016.

Service charges on deposit accounts increased by \$248 thousand or 44.88% period over period. A major contributor to this increase are non-sufficient funds charges (NSFs). These charges increased by \$108 thousand from September 30, 2015 to September 30, 2016.

Other service charges and fees decreased by \$66 thousand or 10.47%. These charges are mostly comprised of debit card interchange fees and fees collected from customers associated with the cost of doing business.

The company recorded a gains of \$404 thousand in 2015 on the sales of investment securities. No sales of investment securities have taken place in 2016.

Mortgage fee income (net of related processing costs) decreased from \$1.1 million to \$889 thousand, a decrease of \$195 thousand or 17.96% from September 30, 2015 compared to September 30, 2016. Our volume of mortgage loans sold to the secondary market has decreased in part due to a restructure of our mortgage division in 2015.

During the second quarter of 2016, the bank recorded an \$8 thousand gain on the sale of bank-owned automobile and a \$2 thousand gain on the sale of a repossessed asset. The \$7 thousand gain in 2015 is attributable to a gain recognized on the sale of a bank-owned vehicle and a loss on a repossessed asset during the first quarter.

Non-Interest Expense:

Non-interest expense for the nine month period ended September 30, 2016 was \$20.3 million as compared to \$20 million for the same period ended September 30, 2015. This represents an increase of \$306 thousand or 1.53%.

Non-Interest Expense	Year-to-Date September 30		Incr./ (Decr.)	% Change
	2016	2015		
Legal, professional, accounting, and exam fees	824,454	977,506	(153,052)	(15.66)%
FDIC assessments	405,000	407,250	(2,250)	(0.55)%
Other expense	2,489,799	2,458,655	31,145	1.27 %
Total Non-Interest Expense	\$20,321,196	\$20,015,002	\$306,194	1.53 %

The largest category of expense for the Company is salaries and employee benefits. This component of non-interest expense increased by \$345 thousand for the nine month period ended September 30, 2016 as compared to September 30, 2015 and represented an increase of 2.90%. Benefit costs continue to rise, which is the primary reason for the increase.

Occupancy and equipment expense decreased \$29 thousand or 0.94% period over period. This decrease is attributable to various assets fully depreciating. We expect this category to rise in the fourth quarter and going forward as our Horseshoe Bay location opened during the third quarter.

Advertising costs increased \$12 thousand or 3.13% from September 30, 2015 compared to the same period ended September 30, 2016. This increase is attributable to the continued costs associated with the Company's rebranding initiative.

Community and philanthropic supported related expenses increased \$45 thousand or 25.9% year over year. We continue to focus on supporting the markets we serve through sponsorships and donations, which is the primary reason we have experienced increased expense in this category.

IT and data processing expenses increased \$58 thousand period over period. Most of this increase relates to core services necessary for maintaining data processing. We contract with a major national core processing vendor to provide our data processing services and their pricing primarily relates to transaction volume and account volume.

Legal, professional, accounting, and exam fees decreased \$153 thousand or 15.66% for the nine month period ended September 30, 2016 compared to September 30, 2015. OCC assessment fees decreased by \$9 thousand period over period. The OCC assessments are based on the call report data asset size as of December and June of each year. Audit expenses decreased \$138 thousand period over period. In 2015, the bank paid an audit firm a one-time fee to perform audit services related to the increased regulation the bank will face when it crosses \$1 billion in assets. The bank did not incur this same expense in 2016. Legal fees decreased by \$14 thousand period over period. Other consulting and professional fees increased by \$8 thousand period over period.

The Bank experienced a decrease in FDIC assessments, or deposit insurance costs. The cost for year-to-date 2015 was \$407 thousand and for the same time period in 2016 decreased to \$405 thousand. This was a decrease of 0.55%. The FDIC assessment is based on the difference between average assets and average equity each calendar quarter-end period at the bank level.

All other expenses increased by \$31 thousand or 1.27% period over period. This increase is attributable to an increase in fraud related expenses in the first quarter of 2016.

Balance Sheet Review

Our portfolio is comprised of loans made to businesses, professionals, and individuals located in the primary trade areas served by our bank. As of September 30, 2016, the Company had total net loans outstanding of \$672 million as compared to \$657.9 million for the same period in 2015, resulting in growth of \$18.2 million or 2.77%.

Composition of Loans (\$ in 000's)	September 30 2016	September 30 2015	Incr./ (Decr.)	% change
Real estate loans (held for sale)	2,285,100	5,342,296	(3,057,196)	(57.23)%
Loans to governmental entities	27,972	223,873	(195,902)	(87.51)%
Commercial & industrial loans	179,418,617	178,637,233	781,383	0.44 %
Consumer loans	7,951,264	8,091,571	(140,307)	(1.73)%
Other loans	19,595,465	22,874,638	(3,279,173)	(14.34)%
Total Loans before loan loss reserve	\$683,415,019	\$667,256,345	\$16,158,674	2.42 %
Less: Loan loss reserve	(11,374,531)	(9,334,189)	2,040,342	21.86 %
Total Loans	\$672,040,488	\$657,922,156	\$18,199,016	2.77 %

Real estate loans represent loans primarily for new home construction, home ownership and investment, and commercial real estate. Real estate loans held for investment represent construction and development loans for both residential and commercial real estate projects. This category also includes longer-term loans for the purpose of financing residential and commercial real estate. Real estate loans held for investment increased from \$452.1 million at September 30, 2015 to \$474.1 million as of September 30, 2016, an increase of \$22 million or 4.88%. Real estate loans held for sale decreased by \$3.1 million from September 30, 2015 to September 30, 2016. Real estate loans held for sale represent loans originated for the purpose of purchasing or refinancing one-to-four family residential properties. These loans are originated by the bank with the intent to sell to secondary market investors. The loans are generally sold within 30 days after origination.

Loans to governmental entities decreased by \$196 thousand period over period. Loans in this category generally produce tax free income much like a municipal bond.

Commercial & industrial loans increased from \$178.6 million at September 30, 2015 to \$179.4 million at September 30, 2016, an increase of \$781 thousand or 0.44%. Loans in this category include oil and gas production loans, loans to oil and gas service companies, and loans to manufacturing and wholesale supply companies and miscellaneous other commercial businesses.

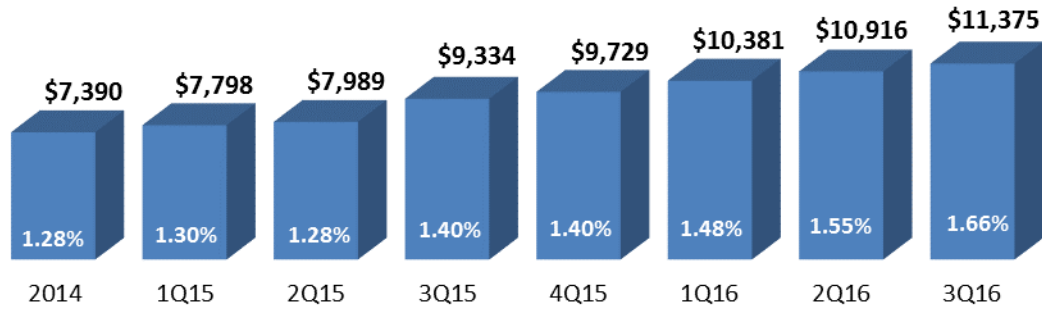
Consumer loans decreased by \$140 thousand or 1.73% from September 30, 2015 to September 30, 2016. The Company is interested in making consumer loans of all types, but consumer lending is not its primary focus. The Company currently has consumer credit underwriting software and a seasoned consumer credit underwriting manager. Management anticipates that our consumer loan portfolio will increase over the next several years.

All other loans decreased by \$3.3 million from September 30, 2015 to September 30, 2016. Included in this category are loans to finance agriculture, loans to purchase securities, and loans to non-depository institutions.

Asset Quality:

The allowance for loan losses is the amount we determine as of a specific date to be appropriate to absorb probable losses on existing loans in which full collectability is unlikely based on our review and evaluation of the loan portfolio. The provision for loan loss expense was \$1.7 million for the period ended September 30, 2016 as compared to \$2.1 million for same period in 2015. Beginning in the third quarter of 2015, management and the Board decided to increase our loan loss reserves to recognize the fact that we are operating in a higher risk environment due to lower oil prices. Our allowance for loan losses as a percentage of our total loan portfolio was 1.66% as of September 30, 2016, as compared to 1.40% as of September 30, 2015. As a percent of average loans, net loan charge-offs were 0.01% as of September 30, 2016 and 0.04% for the same period in 2015. Comparatively, the peer group averages for the same periods were 0.08% and 0.09%, respectively.

Allowance for Loan Losses (\$000's) % of Total Loans



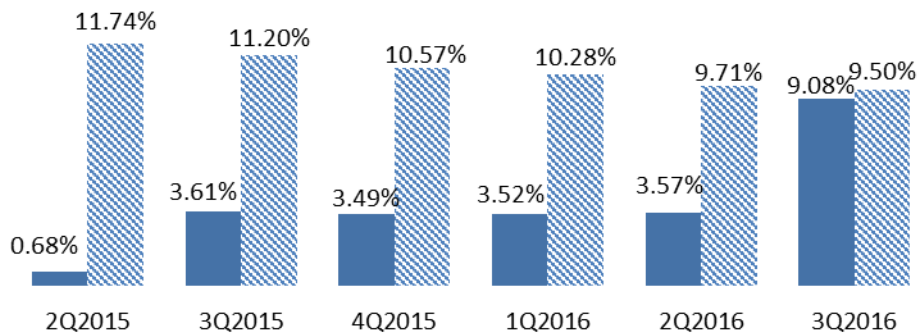
■ *Data provided at the bank level

As of September 30, 2016, past due loans over 90 days as a percentage of total loans were 0.20% compared to 0.00% for the same period in 2015.

Loans placed on non-accrual status as a percentage of total loans were 0.21% as of September 30, 2016 compared to 0.08% at September 30, 2015. Our peer group for the same time period was 0.69% and 0.84%, respectively.

Another common measure of asset quality is the Texas Ratio. The Texas Ratio is calculated as the sum of restructured loans plus non-accrual loans plus real estate acquired in foreclosure divided by the sum of equity capital plus the allowance for loan losses. As of September 30, 2016, the Bank's Texas Ratio was 9.08% as compared to the peer group of 9.50%. For the same period in 2015 the Company had a Texas Ratio of 3.61% as compared to its peer group of 11.20%.

Texas Ratio*



*Data provided at the bank level

■ Bank ▨ Peer Group

Interest-Bearing Deposits in Banks:

The Company had interest-bearing deposits in banks of \$87.9 million as of September 30, 2016, as compared to \$52.1 million as of September 30, 2015. The average yield on these balances were 0.85% for the period in 2016 as compared to 0.60% for the same period in 2015. These balances were held with various regional banks located within the state of Texas. Management evaluates the financial strength of each bank it holds balances with on a quarterly basis to assure the safety of the investment in each bank.

Available-for-Sale and Held-to-Maturity Securities:

At September 30, 2016, available-for-sale securities had a fair value of \$22.7 million and held-to-maturity securities had an amortized cost of \$124 million. For the same period in 2015 these figures were \$24.8 and \$158.6 million, respectively. The decline in held-to-maturity securities is primarily attributable to several agencies in our portfolio maturing or being called.

As of September 30, 2016, the portion of the securities portfolio classified as available-for-sale had a market gain of approximately \$923 thousand and the portion of the portfolio classified as held-to-maturity had an approximate market gain of \$2.5 million. For the same period in 2015, these amounts were \$742 thousand and \$1.3 million, respectively. The Company did not hold any securities as of September 30, 2016 or 2015 that would be classified as below investment grade or with any impairment. Our overall tax-equivalent yield to maturity on our portfolio at September 30, 2016 was 2.90%. The overall tax-equivalent yield to maturity on our portfolio for the same period in 2015 was 2.82%. All yields are computed on a tax-equivalent basis assuming a marginal tax rate of 34.00%. Yields on available-for-sale securities are based on amortized cost. Maturities of mortgage-backed securities are based on contractual maturities and could differ due to prepayments of underlying mortgages. Maturities of other securities are reported at the earlier of maturity date or call date.

Deposits:

Deposits represent our primary source of funding. Total deposits were \$823.4 million as of September 30, 2016 compared to \$818.9 million as of the same period in 2015, an increase of \$4.5 million or 0.55%.

Composition of Deposits (\$ in 000's)	September 30 2016	September 30 2015	Incr./ (Decr.)	% change
Non-interest bearing demand	\$234,483,565	\$235,463,888	(\$980,323)	(0.42)%
Interest-bearing demand	65,283,279	58,977,276	6,306,004	10.69 %
Money market and savings	212,053,849	168,252,931	43,800,918	26.03 %
Certificates of deposits ≥ \$100,000	276,691,000	316,084,692	(39,393,692)	(12.46)%
Certificates of deposits < \$100,000	34,919,000	40,168,283	(5,249,283)	(13.07)%
Total Deposits	\$823,430,694	\$818,947,070	\$4,483,623	0.55 %

The average cost of interest-bearing deposits as of September 30, 2016 was 0.36% which compares to .40% for the same period in 2015. Our peer group's ratios for the same period end were .49% and .48%, respectively.

Capital Resources:

We evaluate capital resources by our ability to maintain adequate regulatory capital ratios to do business in the banking industry. Issues related to capital resources arise primarily when we are growing at an accelerated rate exceeding the rate of growth in our earnings or if we experience significant asset quality deterioration.

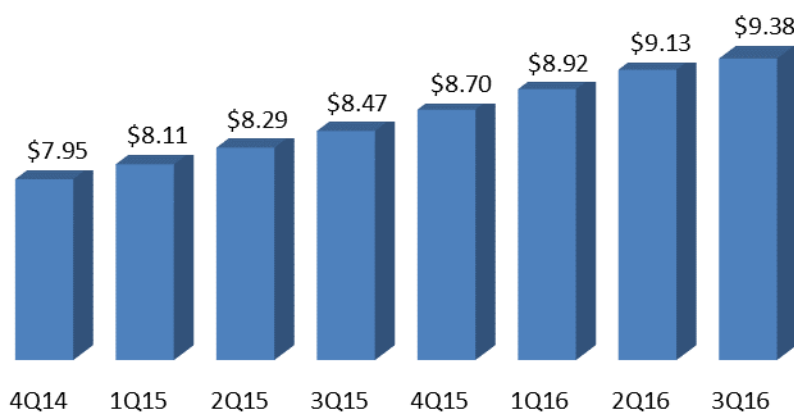
	Actual		Minimum Capital Required - Basel III Buffer Phase-In (2016)		Minimum Capital Required - Basel III Buffer Fully Phased-In (2019)		Required to be Considered Well Capitalized	
	Capital Amount	Ratio	Capital Amount	Ratio	Capital Amount	Ratio	Capital Amount	Ratio
	(000's)							
September 30, 2016								
Total Capital to Risk-Weighted Assets								
Consolidated	\$ 109,843	14.630 %	\$ 64,756	8.625 %	\$ 78,834	10.500 %	\$ 75,080	10.000 %
FirstCapital Bank of Texas, N.A.	108,153	14.423	64,676	8.625	78,736	10.500	74,987	10.000
Tier 1 Capital to Risk-Weighted Assets								
Consolidated	100,430	13.377	49,740	6.625	63,818	8.500	60,064	8.000
FirstCapital Bank of Texas, N.A.	98,752	13.169	49,679	6.625	63,739	8.500	59,989	8.000
Common Equity Tier 1								
Consolidated	88,638	11.806	38,478	5.125	52,556	7.000	48,802	6.500
FirstCapital Bank of Texas, N.A.	98,752	13.169	38,431	5.125	52,491	7.000	48,741	6.500
Leverage Ratio								
Consolidated	100,430	10.367	38,750	4.000	38,750	4.000	48,437	5.000
FirstCapital Bank of Texas, N.A.	98,752	10.209	38,691	4.000	38,691	4.000	48,364	5.000
September 30, 2015								
Total Capital to Risk-Weighted Assets								
Consolidated	101,522	13.480	60,266	8.000	79,099	10.500	75,332	10.000
FirstCapital Bank of Texas, N.A.	96,882	12.880	60,160	8.000	78,960	10.500	75,200	10.000
Tier 1 Capital to Risk-Weighted Assets								
Consolidated	92,103	12.230	45,199	6.000	64,032	8.500	60,266	8.000
FirstCapital Bank of Texas, N.A.	87,480	11.630	45,120	6.000	63,920	8.500	60,160	8.000
Common Equity Tier 1								
Consolidated	79,766	10.590	33,899	4.500	52,733	7.000	48,966	6.500
FirstCapital Bank of Texas, N.A.	87,480	11.630	33,840	4.500	52,640	7.000	48,880	6.500
Leverage Ratio								
Consolidated	92,103	9.490	38,839	4.000	38,839	4.000	48,549	5.000
FirstCapital Bank of Texas, N.A.	87,480	9.040	38,724	4.000	38,724	4.000	48,405	5.000

The Company and its bank subsidiary as of September 30, 2016, were “well capitalized” based on the ratios presented in the table above. Both the Company and its bank subsidiary are subject to regulatory capital requirements administered by the Federal Reserve and the Federal Deposit Insurance Corporation (“FDIC”). If we fail to meet the minimum capital requirements, regulatory agencies can initiate certain actions which could have a material effect on the financial statements. We believe by all measurements our capital ratios remain well above regulatory minimums.

Regulatory capital calculations set forth by the Federal Reserve allows the \$3 million in trust preferred securities to be included in Tier 1 capital of First Bancshares of Texas, Inc. Also included in this figure is Non-Cumulative Perpetual Preferred Stock with a par value of \$1.00 with 5,000,000 shares authorized, 882,544 Series 2009 shares issued and outstanding as of September 30, 2016. During the second quarter of 2016, the bank retired 54,500 shares of preferred stock.

The graph below illustrates at the holding company level, the increases in book value on common shares over an eight quarter period timeframe. Included on page 19 is a table of historical trades and valuations on our common stock.

FBOT Common Share Book Value Over Past Eight Quarters



Dividend Policy:

To pay dividends, we must maintain adequate capital above regulatory guidelines. In addition, if the applicable regulatory authority believes that a bank under its jurisdiction is engaged in or is about to engage in an unsafe or unsound practice (which, depending on the financial condition of the bank, could include the payment of dividends), the authority may require, after notice and hearing, that such bank cease and desist from the unsafe practice. The Federal Reserve Board, the FDIC and the OCC have each indicated that paying dividends that deplete a bank's capital base to an inadequate level would be an unsafe and unsound banking practice. The Federal Reserve Board, the OCC and the FDIC have issued policy statements that recommend that bank holding companies and insured banks should generally only pay dividends out of current operating earnings.

The Company has not paid dividends since its inception due to the need to maintain capital for growth purposes. We anticipate that we will continue to have strong growth and that we will not begin paying dividends in the immediate future. However, if growth slows, the Company could consider paying dividends at a later date.

CAPITALIZATION

The following table represents, on a consolidated basis, the capitalization of the Company as of September 30, 2016.

	At September 30, 2016
Long-Term Indebtedness:	
Junior subordinated debentures - trust preferred securities	\$ <u>3,093,000</u>
Total indebtedness	\$ 3,093,000
Shareholders' Equity:	
Common stock, par value \$1.00 per share, 15,000,000 shares authorized, 9,509,766 shares issued, 9,509,766 shares outstanding as of September 30, 2016	\$ 9,509,766
Preferred stock, par value \$1.00 per share, 5,000,000 shares authorized, 882,544 Series 2009 shares issued and outstanding as of September 30, 2016	882,544
Surplus	
Common	32,457,376
Preferred	<u>7,909,479</u>
Surplus	40,366,855
Treasury stock	-
Retained earnings	46,671,358
Accumulated other comprehensive income	<u>608,896</u>
Total shareholders' equity	\$ 98,039,419
Capital Ratios (Consolidated):	
Tier 1 leverage ratio	10.37%
Common Equity Tier 1 capital ratio	11.81%
Tier 1 risk-based capital ratio	13.38%
Total risk-based capital ratio	14.63%

HISTORICAL TRADES AND VALUATIONS

There have been very few trades in our common stock. The following table presents the low and high per share prices, number of shares traded and the number of trades per quarter for trades in our common stock of which we are aware since January 1, 2009:

<u>Quarter</u>	<u>Low</u>	<u>High</u>	<u>Number of Shares Traded</u>	<u>Number of Trades</u>	<u>Book Value as of Prior Quarter end</u>	<u>Multiple of Price to Book Value</u>	
						<u>Low</u>	<u>High</u>
1st Quarter 2009	\$ 6.00	\$ 6.00	43,133	9	3.95	1.52	1.52
2nd Quarter 2009	\$ 6.00	\$ 6.15	119,151	13	4.05	1.48	1.52
3rd Quarter 2009	\$ 6.00	\$ 6.15	45,850	9	4.12	1.46	1.49
4th Quarter 2009	\$ 6.15	\$ 6.35	43,337	9	4.24	1.45	1.50
1st Quarter 2010	\$ -	\$ -	0	0	4.32	0.00	0.00
2nd Quarter 2010	\$ 6.35	\$ 7.04	149,870	11	4.68	1.36	1.50
3rd Quarter 2010	\$ 7.08	\$ 7.25	160,570	21	4.79	1.48	1.51
4th Quarter 2010	\$ 7.25	\$ 7.34	77,000	9	4.89	1.48	1.50
1st Quarter 2011	\$ 7.50	\$ 7.50	22,500	7	5.01	1.50	1.50
2nd Quarter 2011	\$ 6.35	\$ 7.68	35,386	7	5.12	1.24	1.50
3rd Quarter 2011	\$ 7.86	\$ 8.16	70,306	15	5.30	1.48	1.54
4th Quarter 2011	\$ 8.16	\$ 8.43	140,730	31	5.51	1.48	1.53
1st Quarter 2012	\$ 8.50	\$ 8.51	16,194	9	5.68	1.50	1.50
2nd Quarter 2012	\$ 8.50	\$ 9.46	1,446,285	140	5.85	1.45	1.62
3rd Quarter 2012	\$ 8.77	\$ 9.62	40,160	22	6.41	1.37	1.50
4th Quarter 2012	\$ 9.62	\$ 9.91	21,751	7	6.61	1.46	1.50
1st Quarter 2013	\$ 9.56	\$ 10.06	35,334	4	6.71	1.42	1.50
2nd Quarter 2013	\$ 9.25	\$ 10.41	59,876	12	6.87	1.35	1.52
3rd Quarter 2013	\$ 9.76	\$ 10.55	58,932	10	6.93	1.41	1.52
4th Quarter 2013	\$ 10.00	\$ 10.82	135,149	11	7.10	1.41	1.52
1st Quarter 2014	\$ 10.87	\$ 11.01	89,103	5	7.24	1.50	1.52
2nd Quarter 2014	\$ 11.03	\$ 11.14	9,234	3	7.42	1.49	1.50
3rd Quarter 2014	\$ 11.24	\$ 11.54	30,632	8	7.58	1.48	1.52
4th Quarter 2014	\$ 11.54	\$ 11.81	79,783	8	7.75	1.49	1.52
1st Quarter 2015	\$ 11.81	\$ 12.10	51,216	8	7.95	1.49	1.52
2nd Quarter 2015	\$ 12.31	\$ 12.31	71,073	7	8.11	1.52	1.52
3rd Quarter 2015	\$ 12.55	\$ 12.59	94,568	13	8.29	1.51	1.52
4th Quarter 2015	\$ 12.55	\$ 12.93	67,134	17	8.47	1.48	1.53
1st Quarter 2016	\$ 13.04	\$ 13.18	37,432	9	8.70	1.50	1.51
2nd Quarter 2016	\$ 13.50	\$ 13.50	122,586	17	8.92	1.51	1.51
3rd Quarter 2016	\$ 13.82	\$ 13.82	43,449	7	9.13	1.51	1.51

The prices given are the result of limited trading and may not be representative of the actual value of our common stock. Trades between related parties are not included. As is evidenced in the table above, our stock has generally traded at a multiple of 1.5 times book value, as is reflected in the far right columns. We are not obligated to register our common stock or preferred stock with the SEC or, upon any registration, to create a market for our shares. Thus, a holder of our common stock may be unable to liquidate his investment and must be able to bear the economic risk of such investment indefinitely.

OFFICERS

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Chairman - First Bancshares of Texas, Inc.
& General Counsel

KENNETH L. BURGESS, JR.

Chairman - FirstCapital Bank of Texas, N.A.

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Chief Executive Officer

JAY W. ISAACS

President

TRACY BACON

Chief Operating Officer

PHYLLIS BECHNER

Chief Financial Officer

BRAD D. BULLOCK

Chief Risk Officer

J. GREG BURGESS

Chief Credit Officer

GEORGE H. REEVES

Chief Deposit & Technology Officer

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KENNETH TOMLINSON

Executive Vice President, Midland Lending Manager
& Senior Relationship Manager

JEREMY M. BISHOP

Branch President

BETHANY ETHEREDGE

Branch President

KATIE J. BOYD

Senior Vice President, Marketing & Training Manager

BILL J. HILL

Senior Vice President & Trust Officer

CHRIS L. MCGINNIS

Senior Vice President & IT Manager

RICK MITCHELL

Senior Vice President & Senior Relationship Manager

ROBIN RICHEY

Senior Vice President & Trust Administration

BRADY ROSS

Senior Vice President & Senior Relationship Manager

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Vice President & Loan Operations Manager

SHEA FERLAND

Vice President & Team Resources Manager

BLAKE SCOTT

Vice President, Accounting Department Manager
& Assistant Controller

LISA SHANKS

Vice President & Fraud Officer

CRYSTAL STURM

Vice President, Data Analytics & Project Manager
& Assistant Controller

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Assistant Vice President & IT Specialist

SHERYL RYAN

Assistant Vice President & Information Security Officer

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Banking Officer & Branch Manager

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Banking Officer & Credit Administration Manager

KAMI LITTLE

Banking Officer & BSA Officer

MARY LOGAN

Banking Officer, Branch Manager

TONI MABRY

Banking Officer & Branch Manager

CHAD MAXWELL

Banking Officer & Relationship Manager

EDGAR PAZ

Banking Officer & Loan Servicing Asst. I

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[LACIE McDOWELL](#)

Senior Vice President & Treasury Management

[RICKY RODRIGUEZ](#)

Senior Vice President & Operations Officer

[DONALD TAYLOR](#)

Senior Vice President & Senior Relationship Manager

[MURIELLE BARNES](#)

Vice President & Mortgage Underwriter

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Vice President & Loan Review Manager

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Vice President & Assistant Operations Manager

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Vice President, Assistant Credit Officer & CRA Officer

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Assistant Vice President & Branch Manager

[NICK PHELPS](#)

Assistant Vice President & IT Applications Analyst

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Assistant Vice President & Wire Transfer Manager

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Assistant Vice President & Branch Manager

[MEREDITH STOVER](#)

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[JESSICA AMBURN](#)

Banking Officer & Relationship Manager

[BRITTANY TRUSTY](#)

Banking Officer & Loan Review Analyst II

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[DAVE SWECKER](#)

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Underwriting Manager

[DARRELL HILL](#)

Senior Vice President & Senior Relationship Manager

[TRAVIS HILLMAN](#)

Senior Vice President & Senior Relationship Manager

[ROSALINDA MEREDITH](#)

Senior Vice President & Compliance Officer

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Vice President & TellerConnect Manager

[BARRETT POWER](#)

Vice President & Branch Manager

[YOLANDA BELGARA](#)

Assistant Vice President & Consumer Credit Underwriter

[CATHY COPPLE](#)

Assistant Vice President & Loan Documentation Preparation

Department Manager

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[CALIB WILLIAMS](#)

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[CODY PETTY](#)

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[TAMI RANDOLPH](#)

Banking Officer & Mortgage Loan Originator

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