



**FINANCIAL
GROUP**

2017 Annual Report



Dear Shareholders

We are pleased to announce our financial results for the past year. Net income increased by 15.9% to \$2,345,110, the seventh consecutive year of double digit earnings increases. For the second consecutive year, we grew the balance sheet of the bank, growing just a shade under \$10 million dollars or 3.7%. The exciting aspect of our growth came in our loan portfolio as it grew \$14 million dollars or 8.6%. We also originated and sold an additional \$25.4 million dollars in mortgage loans. (We keep all the servicing on sold loans with the exception of a couple specialized mortgage products.) Our new Morganton loan production office contributed approximately 17% of our portfolio loan production, giving us more than modest growth in this area. Also, for the second year in a row, our non-interest income exceeded our net interest income. Non-interest income grew \$343 thousand dollars to \$7.6 million or 4.7%.

Our Insurance division had good growth in its property and casualty areas (13.5%), as well as net income, which increased to \$615,043 (15.5%). In March, we purchased Greystone Insurance in Boone. We completed the acquisition with only a quarter of the year remaining so; combined with good growth in our existing offices, we are anticipating positive increases from insurance again this year. We were also very pleased to have 5.0% growth in our deposits, with all of the growth coming in checking and savings accounts. Finally, we continue to reduce classified assets and saw them slip from \$8.3 million to \$6.4 million, or a reduction of 23.5%. In summary, we had solid trends in all the key metrics, in both banking services and insurance.

We added Dr. Harry Davis to our Board of Directors this year. Dr. Davis has a 40-year tenure at Appalachian State University, where he teaches a senior course for finance and banking majors on Commercial Bank Management. He has an endowed banking chair named for him in the Walker College of Business at ASU. He is also former Chair of the Department of Finance, Banking, and Insurance. His history with the North Carolina Bankers Association is almost as long. He has served as the Economist for the Association since 1980. In addition to that role, he is the Dean and Instructor for the North Carolina School of Banking. Dr. Davis is also an instructor for the Director's College, sponsored by the North Carolina Commissioner of Banks and the FDIC. We are very pleased to have Harry join our Board and share his deep knowledge of banking with us.

Located in the heart of the Blue Ridge Mountains, our communities saw an 11% increase in first-time visitors this past year. This region attracts many people from across the state for day trips to shop, tour a winery, explore hiking trails or take in long range vistas. Of course, many people come here to just sit back and do nothing. Tourism

A land of natural beauty, simple charm and a beckoning call that welcomes young and old to call this place home.

keeps our retail shops full, enables more and varied restaurants to thrive, and is the driver for our second home industry. Across North Carolina, approximately 4% of all housing is second homes; in the High Country, that figure exceeds 25%. If you look at new construction, the figure is higher still. We are also fortunate to have strong vibrant urban areas within a few hours' drive. While we regularly receive guests from all over the country, the piedmont of North Carolina provides the bulk of our visitors.

There was a time when we primarily saw tourists in the summer. The spring and summer bring many folks to travel down the Blue Ridge Parkway. We have nearly 100 miles of the Parkway running through our markets, and when tourists stop, they find some of the quaintest main streets in the country. In October, when the leaves turn shades of red, yellow, and orange, those same visitors often return. On weekends in November, not many cars head down the mountain without a Christmas tree tied on top. Ashe County produces more Christmas trees than any other county in the United States, and in the winter trees are traded in for skis and snowboards.

Our rural communities do face challenges, including population growth, limited employment opportunities, an aging workforce and transportation concerns. However, few places in the United States offer our unique combination of natural beauty and commitment to community. We will work hard, along with other community leaders, to make sure a healthy economy exists. We're pleased to be a part of the community and provide businesses with insurance, banking, and financial services.

Throughout this book, you'll see beautiful images from our back door and some facts we're proud to share, like how the oldest river in North America is, ironically named the New River. The headwaters of its two main tributaries are located in Watauga County, then merge in Ashe, travel through Alleghany and head north into Virginia. For more information about our area, check out the "Our Communities" section of our website at www.golifestore.com/communities. Thank you for your support as we continue to develop the best customer experience for our customers and communities.



Robert Washburn
President and Chief Executive Officer



Robert Washburn, President and Chief Executive Officer



Brett Miller, LifeStore Employee and Bike Enthusiast

Fitness, Passion and Community

Many LifeStore employees are involved in their community by lending a hand with organized events. They live in our communities and allow their passions to direct them to serve and give back. LifeStore employee Brett Miller is a great example of taking a passion and turning it into a community project.

Since he was a child, Brett has been passionate about bicycles. Not only is biking a great way to exercise, it's also a way to get outside, breathe some fresh air, and spend time with people you care about. "I've always been passionate about bicycles," Brett said. "That's all we used to do in the summer." Along with working for LifeStore as a part-time courier, Brett is also co-owner of The Recyclist Bike Shop in Lansing, NC.

The Recyclist sells higher end used bikes which Brett chose to stock because he wanted to get people on a bike. Brett explains that it is easy to get sticker shock when going into a bike shop and shopping for a new bike.

Brett enjoys riding and embodies all aspects of sharing his enthusiasm to make it possible for others to enjoy riding. He has volunteered to help finish the new 3.6 mile single track bike trail at the Lansing Creeper Trail Park in Lansing, NC. The park has now grown to 74 acres, making it larger than Ashe County Park, and the new trail will offer riders fun and challenges.

Brett's wife, Katrina teaches at Ashe County Middle School and he is keenly aware of the need for students to have more activities after school; so, he has started a Bike Club for the school. "I'm just trying to get the kids off their phones," Brett said about his new club. "That's really the goal." Since the club was announced to students, the response was even better than Brett expected, with about 30 students showing interest. As part of the new bike club, students will help create biking trails, learn how to repair bicycles, learn about bike parts, and eventually, take group rides on Saturdays.

This bike club is a unique idea for students. Cycling is a safe way for students to get exercise without playing sports, and it's been linked to increased cardiovascular fitness, increased strength and flexibility and decreased stress levels.

The biking club will foster a sense of community, and in a way, learning how to repair bikes even teaches engineering. More than that, it gives students an appreciation for volunteering in the community. Through the work that the bike club is going to do this year, the High Country will have even more beautiful bike trails, and a few more bikers to use them.

If you have a passion, let it grow and nurture its outcome.



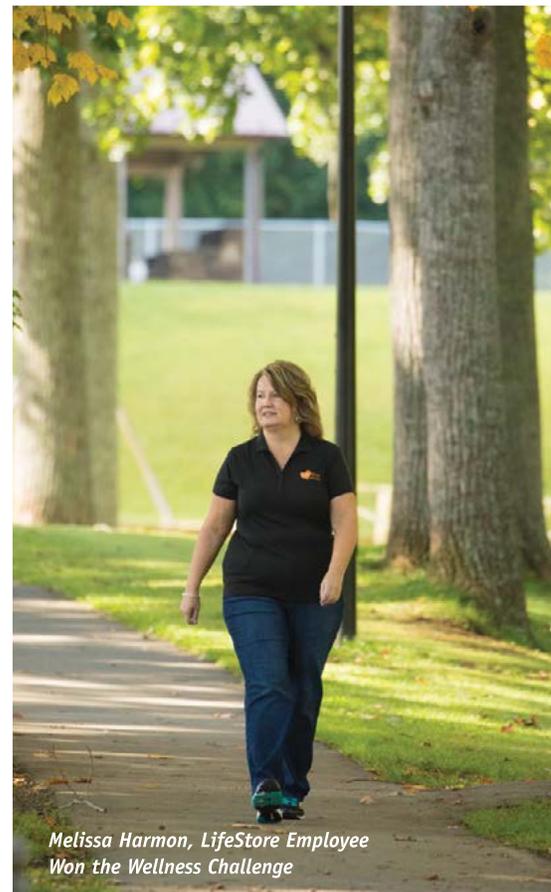
*LifeStore employees at Ashe County Heart Walk
From left to right: Dennis Winebarger, Chris Hill, Helen Bare, Miranda Wingler, Michelle Cox*



Committed to Wellness

The LifeStore Wellness program continues motivating employees to be healthier, make better choices and live a more active lifestyle. In the spring of 2017, a new challenge, "Walk To Williamsburg" was introduced. This walking challenge consisted of walking the distance to Williamsburg: 350 miles in 70 days or 10,000 steps per day. Tickets were awarded to walkers as they achieved certain milestones and employees were encouraged throughout the challenge with prize drawings and final prizes ranging from gift certificates to a Williamsburg, Virginia trip.

Melissa Harmon, Network Administrator/Software Support Specialist, took the challenge saying, "I got out of the routine to exercise and lost interest in watching my diet." The challenge was motivating and helped Melissa and others achieve personal fitness goals. During the challenge, she worked out at a nearby gym during lunch, walked after work and eliminated unhealthy choices such as soda from her diet. "The challenge motivated me to get back in shape. I wanted to look better, feel better and do more things with my son" said Melissa.



*Melissa Harmon, LifeStore Employee
Won the Wellness Challenge*

The pleasant temperatures and growing number of trails make walking outdoors a favorite activity.



*Carl Meyers
Co-owner, Appalachian Naturescapes*

At Home in the Mountains

Appalachian Naturescapes create landscapes and gardens to look as though they have been created by nature. Based in the mountains of western North Carolina, they are experts in natural landscape solutions for extreme slopes, drainage challenges and the special needs presented by micro-climates.

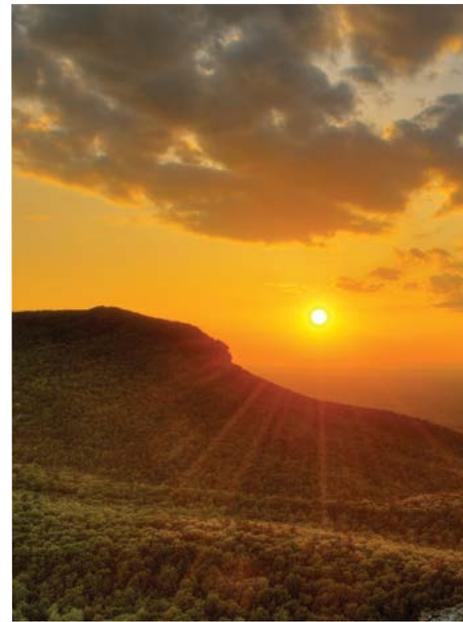
Appalachian Naturescapes recently won an Award of Distinction from the North Carolina Nursery and Landscape Association for their design work and install quality (project featured this page.) According to co-owner Carl Meyers, the beautiful mountains influenced his decision to return to Western North Carolina after studying at NC State.

Appalachian Naturescapes has a relationship with LifeStore dating back to Watauga Insurance. The owners of this business rely on Dina Boyd and Katy Fox to handle many of the details of the business including insurance. They appreciate the promptness and level of service LifeStore provides. Carl and partner Terrell Knutson place a lot of trust in their employees to guide them with vendor selection and purchases. Sandra Williams, Branch Manager of the Lenoir and Boone LifeStore Insurance offices,

understands the importance of delivering what you promise and exceeding the customer expectations whenever possible. “We are happy to take care of the needs of Appalachian Naturescapes and place a special emphasis on turning their requests around quickly. We understand our commercial clients are in a competitive business and time is money.”

One the specialties of this business is taking a problem and creating a solution to enrich the environment and leave the landscape looking natural and better than before. The project pictured began with the client wishing to replace a small concrete patio. Appalachian Naturescapes was concerned about just doing a simple replacement because there were several other problems negatively effecting the property. Water wasn’t draining around the existing patio, the basement was damp, and there was a canopy of large hardwoods making this area dark and damp. Carl explains, “This project became a drainage infrastructure, not just an aesthetic composition.” Projects typically evolve as we uncover possibilities and our designs are a joint effort between the client and our staff.

A restaurant where everybody eats regardless of means.



Renee Boughman
Executive Chef, F.A.R.M. Cafe

Feed All, Regardless of Means

The goal of alleviating hunger in the High Country has been taken on by many organizations, but none have done a better job than F.A.R.M. Cafe in Boone, NC.

F.A.R.M. Cafe is a non-profit, pay-what-you-can community kitchen that builds a healthy and inclusive community. They provide high-quality, delicious meals produced from local sources when available, served in a restaurant where everyone eats, regardless of means. F.A.R.M. stands for “Feed All, Regardless of Means.” The name also reflects the fact that F.A.R.M. Cafe uses ingredients from local sources when possible.

F.A.R.M. Cafe is part of a community cafe network, under an umbrella organization called One World Everybody Eats. The movement gives communities the chance to serve nutritious food to those in need, while in a restaurant setting. That makes it different from the “soup kitchen” model.

“The idea behind a pay-as-you-can cafe is that everybody can participate on some level,” said Renee Boughman, Executive Chef, who is responsible for the management and operation of the cafe. “If someone comes in and they’re in a position of food insecurity, or they’re low income, they can still be a part of our community by volunteering, by assisting, or by paying

what they can that day. Maybe next time when they have a little extra, they can help out their neighbor. That’s what makes this a unique setting, and makes it different than a soup kitchen.”

With only a limited number of paid employees and a mix of students, retirees, people who need community service hours, and everyone in between, the model is working. They are constantly looking for ways to control their costs and the Non-Profit checking account from LifeStore does just that.

Renee explains they made the switch to LifeStore for a combination of reasons. “I had personal accounts with LifeStore because of Jan Noffsinger and the cafe was a Watauga Insurance customer. After we lost our bank downtown, we started researching banks. When LifeStore employees Cindy Gore and Brian Greer stopped by the cafe, I learned that LifeStore offered an interest bearing checking account for non-profits. It was a no brainer for us. Nobody is doing that. You’re local and your hours are so much more convenient. Staying open past 5 is so important for us.”

About 80 percent of diners can pay the suggested donation with 20 percent unable to regularly donate the suggested amount so they choose to volunteer. Boughman said as long as this 80/20 model stays intact, F.A.R.M. Cafe will thrive.

Financials

(In thousands)

Year Ended	2017	2016	2015	2014	2013
Selected Financial Condition Data:					
Total assets	\$ 275,831	\$ 266,049	\$ 254,349	\$ 254,961	\$ 267,743
Loans receivable, net ¹	176,660	162,654	176,007	182,036	191,854
Investment securities ²	50,065	50,697	25,377	32,033	32,933
Cash and cash equivalents	20,752	27,232	26,426	17,882	21,488
Deposits	198,183	188,757	179,654	175,741	189,176
Borrowings	49,577	51,628	51,676	57,721	57,763
Equity	23,028	21,810	19,014	17,906	16,941
Book value per share	22.60	21.40	18.66	17.57	16.62
Selected Operating Data:					
Interest income and dividends	\$ 9,608	\$ 9,417	\$ 10,347	\$ 10,693	\$ 11,351
Interest expense	2,155	2,199	2,316	2,407	2,786
Net interest income	7,453	7,219	8,032	8,286	8,565
Provision for loan losses	196	160	287	705	1,851
Net interest income after provision for loan losses	7,257	7,059	7,744	7,581	6,714
Non-interest income	7,600	7,257	6,576	5,330	5,841
Non-interest expense	11,874	11,665	12,345	11,872	11,899
Income before income tax expense	2,983	2,651	1,976	1,039	656
Income tax expense	638	627	472	160	-66
Net income	\$ 2,345	\$ 2,024	\$ 1,505	\$ 878	\$ 722
Year Ended June 30,	2017	2016	2015	2014	2013
Selected Ratios:					
Basic earnings per share of common stock	\$ 2.30	\$ 1.99	\$ 1.48	\$ 0.86	\$ 0.71
Return on average assets	0.87%	0.78%	0.58%	0.34%	0.27%
Return on average equity	10.63%	10.02%	8.05%	4.99%	4.17%
Net interest margin ³	3.10%	3.09%	3.52%	3.47%	3.50%
Efficiency ratio ⁴	78.88%	80.44%	84.50%	87.19%	82.60%
Nonperforming loans to total loans	1.96%	3.54%	2.75%	3.63%	3.80%
Allowance for loan losses to total loans	1.32%	1.43%	1.62%	1.54%	1.58%

¹ Loans receivable, net is comprised of total loans less allowance for loan losses, loans sold, undisbursed loan funds and deferred loan fees.

² Includes FHLB stock and investment securities.

³ The net interest margin represents net interest income as a percentage of average interest-earning assets.

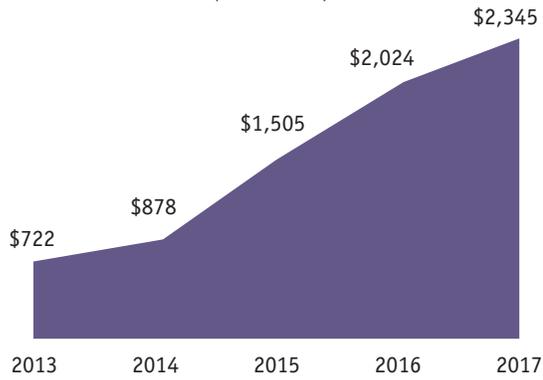
⁴ The efficiency ratio represents non-interest expense as a percentage of the sum of net interest income and non-interest income.



Travel to the NC Mountains is the heaviest in summer and fall.

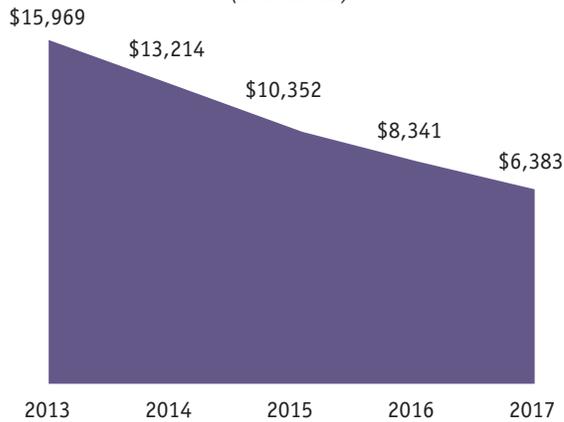
LifeStore Financial Group Net Income

(in thousands)

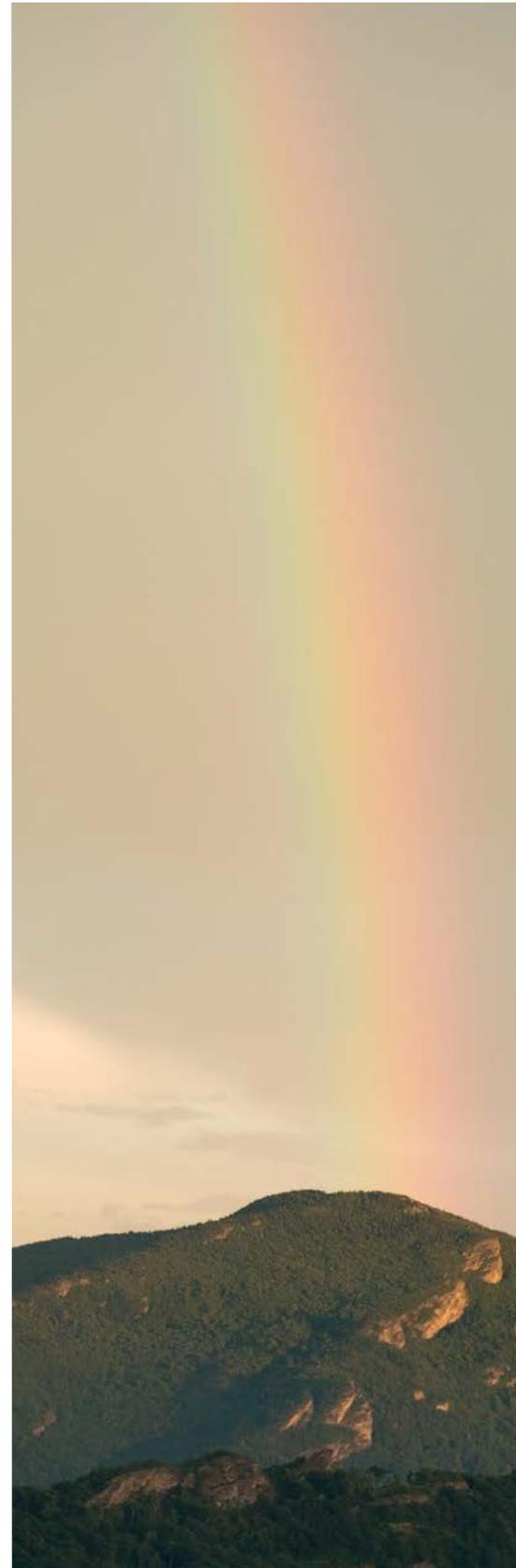
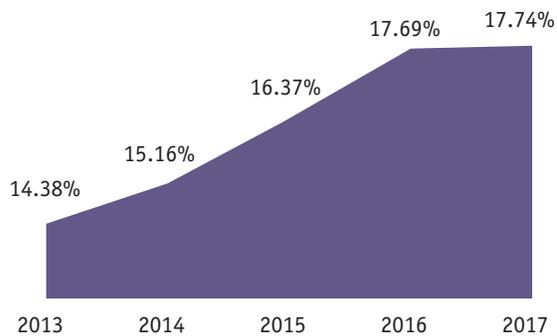


LifeStore Bank Classified Assets

(in thousands)



LifeStore Bank Total Risk - Weighted Capital Ratio





Jody Brown
President, LifeStore Insurance



Insurance

What a great year for LifeStore Insurance! Financially, we had our best year ever and put ourselves in a great position to continue to prosper into the future. We enjoyed a fifth consecutive year of increases in gross revenue and net income. Our gross revenue was \$4.6 million, which is an increase of 5% over YE 2016. Our net income for YE 2017 was \$615,043, an increase of more than 15% from YE 2016. We anticipated a decrease in revenue from individual health insurance, shifted our focus, and more than overcame the shortfall. Our Commercial Insurance saw a 13% increase over 2016 and Personal Insurance increased by 15% over 2016.

We made increasing our commercial and personal insurance revenue a focus for 2017. We write insurance for many different types of commercial clients and rely heavily on contractors; including trade contractors, Christmas tree farms and nurseries, wineries, restaurants, hotels and the lumber industry. Our Commercial Insurance grew from 39% to 42% of our overall revenue in 2017. These businesses reflect the region and its use of our natural resources, and we are proud to serve them. We recognize that without the culture, resources and natural beauty of our region, these industries would not exist as they do today; and we must continue to find solutions and products they can rely on. We also increased our personal insurance revenue in 2017; it now comprises almost 38% of our total revenue.

In March 2017, we announced the purchase of (the assets of) Greystone Insurance Associates, Inc. in Boone, NC. We are very pleased to bring such a fine agency into our organization. Having been in business in the High Country since 1989, their focus is on providing the highest level of personal service and professional expertise. The former president of Greystone, Linda Gilleland, joined LifeStore and will continue serving clients in the same capacity. We will continue operating Greystone Insurance as a Division of LifeStore Insurance and will work together to continue delivering the motto clients have become familiar with: "Experience the

Difference." Through the purchase of Greystone, we have two new important markets for our clients, and we can bring new opportunities to the Greystone clients.

In the past two years, we have purchased two agencies that will undoubtedly help position us for the future. Acquiring agencies, not only enlarges our footprint and increases our premium volume with our carriers, but it ensures that we can maintain strong relationships, create diversification in our portfolio, promote consistent growth and gain market share faster. The great majority of our agency purchases have been very successful and a win-win for us and the client. We feel particularly good about the immediate and future impact of Greystone to our success and the mutual benefit for us and the clients.

During 2017, we had two important members of our team retire after many years of service with our company. Ann Ashman, Sr. VP and Branch Manager of our Elkin team, retired on December 31, 2016, and Jan Noffsinger, VP of Health Operations, retired on June 30, 2017. We appreciate what these professionals did for their clients and our organization through their many years in the insurance industry.

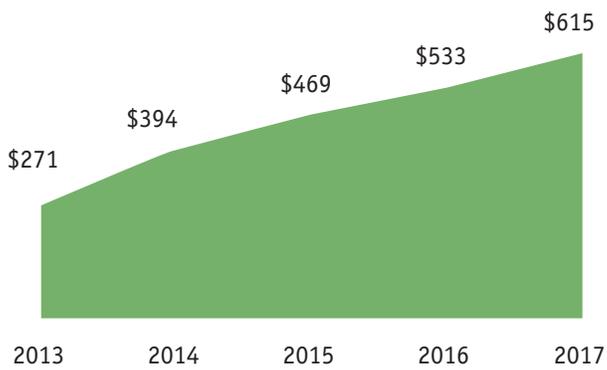
LifeStore Insurance is in a great position for future success, in 2018 and beyond. Our agency is one of the largest retail independent agencies in North Carolina, writing over \$23 million of property and casualty insurance, and generating over \$700,000 in the benefits area. Our challenge is streamlining our operation to deliver the best possible solutions, competitive pricing, and knowledge to our clients. Our 40 employees are risk advisors with an average time with our agency of 11 years and in the industry of 18 years. We take what we do very seriously and want to continue to achieve success for our clients, company, and industry.

Jody Brown
President, LifeStore Insurance

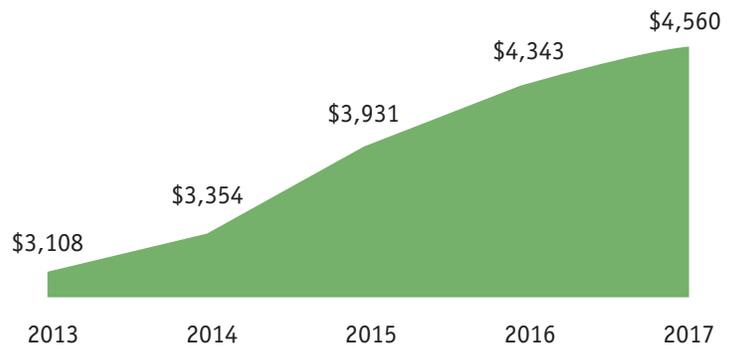


The North Carolina Fraser Fir Christmas Tree is the most popular Christmas Tree in North America. It is shipped to every state and many points around the world.

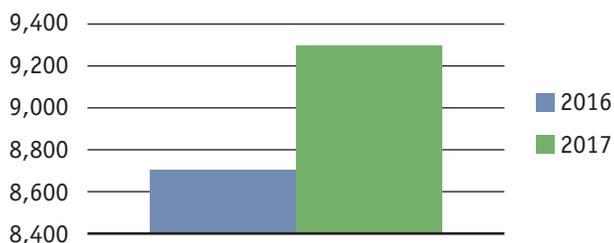
**LifeStore Insurance
Net Income**
(in thousands)



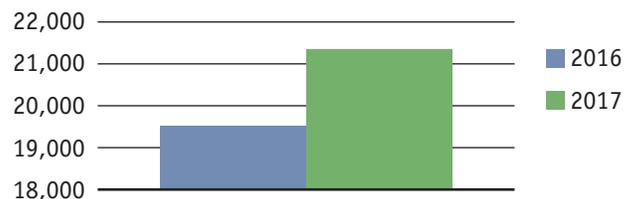
**LifeStore Insurance
Gross Revenue**
(in thousands)



**LifeStore Insurance
Client Growth**



**LifeStore Insurance
Policy Growth**





LifeStore's Brian Greer and Cindy Gore with F.A.R.M. Cafe Executive Chef Renee Boughman

Come Home to LifeStore

Since our bank was established in 1939, our goal has been simple: provide high-quality banking services to our community, with an emphasis on treating our customers like neighbors, not numbers.

We're happy to report that our customers feel like we've accomplished that goal. LifeStore recently conducted a customer survey, and one of many respondents characterized our philosophy by saying the following: "I'm not a number; it's a relationship that I am grateful to have." In fact, when asked what keeps people coming back to LifeStore, 63.5% of respondents answered: "The employees at LifeStore know me."

We believe our desire to please local customers is the main factor that has contributed to our recent increases in both loans and deposits. In the past year, our efforts have culminated in loan growth of 8.6% and checking account balance growth of 7.8%. Needless to say, these are strong results.

Our bankers are supported and encouraged to be innovative in providing financial solutions. They even team up to go to homes and businesses to conduct banking or obtain information necessary for a product or service. Bank loans are approved locally, not by an underwriting unit located in a distant major city. Mortgage lenders have the flexibility to place loans in the secondary market or originate portfolio loans. This option provides tremendous flexibility for applications

that may not exactly "fit" standard underwriting criteria.

Over the past year, new technology was introduced to expand the capabilities of online banking, and streamline the loan application process. This will be an ever-evolving process, as LifeStore will continue to introduce advancements that allow customers to conduct financial business anywhere, 24 hours a day.

These loan and deposit achievements have been and will continue to be predicated in an environment where our customers recognize they are known and appreciated. We realize it is imperative to constantly update technology offerings and have plans for a number of new offerings in the coming year.

"These elements have proven very effective for us; so as many banks become more impersonal, it is our intent to attract customers who yearn for both the personal touch and the convenience of ever changing technology," said Joedy Eller, Chief Banking Officer.

With our personal touch, drive to help the local community, and push to never refer to customers by a number, more and more people are choosing LifeStore. And our new motto "Come Home to LifeStore" is an invitation to bank where your name is known and employees take a personal interest in the customer and their financial goals.

Ashe County Christmas tree farms help drive the local economy, providing over 700 local jobs year round and over 2,000 jobs during the tree harvest season.



Scott Ballard
Owner, West End Wreaths

Friendship, Community and Opportunity

Friendship, community, and opportunity - according to LifeStore customer Scott Ballard, that's the secret of success for agricultural businesses in the High Country. Scott is the owner of West End Wreaths in Ashe County, NC. "Living in the epicenter of the Fraser Fir universe, it's kind of hard to avoid," Ballard said about getting in to the wreath business. "It pulled me in."

West End Wreaths focuses specifically on making wreaths out of Fraser Fir Christmas trees and ships them across the country to garden centers, clubs using them as a fundraiser and individuals looking for a wreath ready to hang on the front door.

Ashe County is the leading Christmas tree producer in the United States, thanks to its unique climate and the work ethic of local farmers. In fact, several trees from the High Country have graced the White House. Every year, West Jefferson holds a festival to promote the local Christmas tree industry called "Christmas in July." There is a community wide push to promote Christmas trees, and it's a deep source of pride among locals. But according to Scott, it's the sense of community partnership in the Ashe County farming industry that's the real reason why local farmers have been so successful.

"The concept of harvest is something that we in our society have lost connection with - that's not true here. What harvest does, is it brings out the best in all of us because we understand that we have a short window of time to do what we need to do. If I have a problem, I know that I can call any number of farmers and get help; because they know if they ever need help, they can call me. That kind of cooperation and connection is lacking in our culture today."

Scott expresses the need for convenience and shares that banking at LifeStore adds an advantage. "I take full advantage of the extended hours LifeStore offers during harvest time." The accessibility, later hours, and Saturday hours is what sets LifeStore apart. We have, during harvest especially, such crazy schedules, and that kind of flexibility is crucial to our business. To have that availability to do banking, to do deposits, withdrawals and all those things, is a big-time factor for us," Scott said.

Scott's business is much like the wreaths he sells, embodying the circle of community, natural resources and love for your neighbor.



Harry M. Davis, Ph.D.

Professor of Banking and Dean for the North Carolina School of Banking, former Chair and current Professor for Department of Finance, Banking, and Insurance at Appalachian State University, Economist for the North Carolina Bankers Association, began serving in 2017.



Charles W. Jones, M.D.

General surgeon, joined Board in 2014. Operates private practice in Jefferson, NC as fourth generation surgeon



Claudia L. Kelley, Ph.D.

Professor of Accounting at Appalachian State University, joined Board in 2003



Donald R. Moore

Owner and manager of a McDonalds Restaurant in West Jefferson, NC, serving Board since 2001



Karen P. Powell

Public Relations Administrator for Skyline Membership Corporation in West Jefferson, NC, serving Board since 2006



Jerry L. Roten

Chairman of the Board of LifeStore, joined Board in 1992, former Clerk of Superior Court of Ashe County



Michael M. Sherman

Vice Chairman of the Board of LifeStore, joined Board in 2001, President and Chief Executive Officer of Zibra, LLC, a consumer products company based in Mooresville, NC



James C. Walker

BGen, USMC (Ret.), Deputy Director for International Projects including Operation Heal Our Patriots, Samaritans Purse Boone, NC, joined Board in 2016

Board of Directors

Last year ninety-one percent of overnight visitors came to the Mountain Region for leisure purposes, which included visiting friends and relatives, outdoor recreation and entertainment/sightseeing.



Left to right: Ruth Johnson, Joedy Eller, Robert Washburn, Joseph Brown

Executive Officers

Robert E. Washburn

Director, President & Chief Executive Officer

Melanie P. Miller

Executive Vice President & Chief Financial Officer

Joseph E. Eller

Executive Vice President & Chief Banking Officer

Ruth F. Johnson

Executive Vice President & Chief Credit Officer

Joseph T. Brown III

President of LifeStore Insurance Services, Inc.

LifeStore Bank Locations

1675 Blowing Rock Rd, Boone, NC 28607
840 E Main St, Jefferson, NC 28640
4951 NC Hwy 88 W, Warrentonville, NC 28693
205 S Jefferson Ave, West Jefferson, NC 28694
1441 Mt Jefferson Rd, West Jefferson, NC 28694

LifeStore Bank Loan Production Office

216 Collett St, Morganton, NC 28655

LifeStore Financial Group Support Center

21 E Ashe St, West Jefferson, NC 28694

LifeStore Insurance Locations

1675 Blowing Rock Rd, Boone, NC 28607
148 Hwy 105 Ext, Suite 204, Boone, NC 28607
925 N Bridge St, Elkin, NC 28621
840 E Main St, Jefferson, NC 28640
324 Morganton Blvd SW, Lenoir, NC 28645
315 Main St, North Wilkesboro, NC 28659
112 S Main St, Sparta, NC 28675
206 S Jefferson Ave, West Jefferson, NC 28694



www.GoLifeStore.com