



*Larry J. Miller*  
*Vice Chairman, President and*  
*Chief Executive Officer*

May 7, 2014

Dear Shareholder,

We are pleased to report that Codorus Valley Bancorp, Inc. earned net income available to common shareholders (earnings) of \$2,941,000 or \$0.61 per share basic, \$0.59 per share diluted, for the quarter ended March 31, 2014, as compared to earnings of \$2,599,000 or \$0.55 per common share basic, \$0.54 per common share diluted, for the quarter ended March 31, 2013. Earnings for the current quarter increased \$342,000 or 13 percent above the first quarter of 2013, and \$422,000 or 17 percent above the fourth quarter of 2013.

#### **Review of operations**

Net interest income for the current quarter increased \$1,269,000 or 14 percent above the first quarter of 2013, and \$216,000 or 2 percent above the fourth quarter of 2013, primarily due to increased interest income and fees from a higher volume of commercial loans, and the realization of \$234,000 of nonrecurring loan income and fees from payoffs of two unrelated commercial loan relationships. Lower funding costs resulting from increased low-cost deposits, and lower rates generally paid on all deposit products, also contributed to the increase in net interest income.

The provision for loan losses for the current quarter increased \$290,000 or 112 percent compared to the first quarter of 2013. The increase in the provision was necessary to support growth in the loan portfolio and replenished the allowance for loan losses for net charge-offs during the quarter which totaled \$212,000, as compared to \$76,000 for the first quarter of 2013.

Noninterest income decreased \$277,000 or 14 percent for the current quarter as compared to the first quarter of 2013. Net gains from the sale of loans held for sales decreased reflecting a sharp decline in refinancing demand attributable to higher mortgage interest rates. Income from mutual fund, annuity and insurance sales also decreased due to lower sales volume and a loss of some accounts as a consequence of sales staff turnover in 2013.

Noninterest expense increased \$395,000 or 5 percent for the current quarter, compared to the first quarter of 2013. The increase was attributable primarily to increased marketing expenses as a result of nonrecurring costs to promote PeoplesBank's 150th year in business. Personnel expense for the quarter also increased \$136,000 or 3 percent compared to the same quarter in the prior year as a result of continued business growth and franchise expansion.

The \$34,000 or 3 percent decrease in the provision for income taxes for the current quarter was due to a nonrecurring \$171,000 favorable adjustment to the Corporation's net deferred tax asset reflecting the anticipated increase in the Corporation's federal statutory income tax rate from 34 percent to 35 percent. This adjustment more than offset the increase in the regular provision resulting from a higher level of pretax earnings.

## Review of financial condition

On March 31, 2014, total assets were approximately \$1.19 billion, representing a \$122 million or 11 percent increase, compared to March 31, 2013. Asset growth was primarily in the commercial loan portfolio and was funded by both increased core deposits and low-rate advances from the Federal Home Loan Bank of Pittsburgh.

Our nonperforming assets ratio of 1.98 percent as of March 31, 2014 reflected improvement from the 2.24 percent nonperforming assets ratio as of December 31, 2013, due to both payoffs of impaired loans, and sales of foreclosed real estate.

As previously announced, during the first quarter the Corporation completed a private placement with institutional and accredited investors by issuing 650,000 shares of common stock at a purchase price of \$20 per share. Gross proceeds from the transaction, totaling \$13 million, will be used to redeem \$13 million of the \$25 million in outstanding shares of preferred stock held by the United States Department of the Treasury under its Small Business Lending Fund Program.

## Other news

We continue to celebrate PeoplesBank's 150th anniversary with special activities and events planned throughout 2014 to commemorate this important milestone in our history and promote our anniversary theme - Proud of Our Past, Focused on Your Future.

We are pleased to announce that we continue to expand our franchise. During the current quarter, PeoplesBank concluded long-term lease negotiations related to constructing a full-service banking office in Shrewsbury, PA scheduled to open in November 2014.

As announced on April 8, 2014, the Corporation's Board of Directors declared a regular quarterly cash dividend of \$0.12 per common share, payable on May 13, 2014, to shareholders of record at the close of business on April 22, 2014. If you do not currently participate in the Company's Dividend Reinvestment and Stock Purchase Plan (DRSPP) but wish to enroll, you may contact the Company's plan administrator Wells Fargo Shareowner Services at 800-468-9716. The Board of Directors regularly reviews the dividend policy and can be expected to approve future changes to it as they deem necessary and appropriate.

On behalf of the Board of Directors, the Leadership Team, and all who serve our clients on a daily basis, thank you for your long-term investment in Codorus Valley Bancorp, Inc. and your continued confidence.

Sincerely,



Larry J. Miller  
Vice-Chairman, President, and CEO

**CODORUS VALLEY BANCORP, INC.**  
**CONSOLIDATED FINANCIAL HIGHLIGHTS**  
**Unaudited**

As of and for the three months ended  
March 31,

	<u>2014</u>	<u>2013</u>	<u>%chg</u>
<b>Selected financial information</b>			
(dollars in thousands)			
Assets	\$1,185,168	\$1,063,383	11.5
Shareholders' equity	\$123,362	\$103,185	19.6
Net income available to common shareholders	\$2,941	\$2,599	13.2
Common shares outstanding, as adjusted	5,470,955	4,712,249	16.1

**Ratios**

Return on average assets	1.04%	1.01%	3.0
Return on average equity	10.82%	10.39%	4.1
Capital leverage	11.34%	10.29%	10.2

**Per share information**

(adjusted for stock dividend)			
Net income per common share, basic	\$0.61	\$0.55	10.9
Net income per common share, diluted	\$0.59	\$0.54	9.3
Book value per common share	\$17.98	\$16.59	8.4

**Common stock & dividend information**

NASDAQ Global Market symbol: CVLY  
(Cash dividends and stock price are adjusted for common stock dividends.)

	<u>2014</u>			<u>2013</u>		
	<u>\$high</u>	<u>\$low</u>	<u>\$div</u>	<u>\$high</u>	<u>\$low</u>	<u>\$div</u>
First quarter	22.35	19.14	0.120	16.10	12.61	0.105
Second quarter				16.75	14.52	0.105
Third quarter				18.19	16.43	0.114
Fourth quarter				21.98	16.73	0.114

**Nasdaq market makers**

Boening & Scattergood, Inc.	800-842-8928 or 610-862-5368
Janney Montgomery Scott LLC	800-999-0503 or 717-779-2720
Sandler O'Neill & Partners, L.P. (institutional trades only)	800-635-6871 or 212-466-8000

**Stock transfer agent**

Wells Fargo Bank, N.A. 800-468-9716  
(www.wellsfargo.com/shareownerservices)

**Shareholder inquiries**

Shareholder contact line 717-747-1519 or 888-846-1970 ext. 519

Additional financial information is available via the Internet:

**www.peoplesbanknet.com**

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