

**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 **September 30, 2020**

or

Transition Report Pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934

For the transition period from ____ to
Commission File Number **001-38084**

FARMERS & MERCHANTS BANCORP, INC.

(Exact name of registrant as specified in its charter)

OHIO

(State or other jurisdiction of
incorporation or organization)

307 North Defiance Street, Archbold, Ohio

(Address of principal executive offices)

34-1469491

(IRS Employer
Identification No.)

43502

(Zip Code)

(419) 446-2501

Registrant's telephone number, including area code
(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
Common Stock, No Par Value	FMAO	NASDAQ Capital Market

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or Section 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	<input type="checkbox"/>	Accelerated filer	<input checked="" type="checkbox"/>
Non-accelerated filer	<input type="checkbox"/>	Smaller reporting company	<input checked="" type="checkbox"/>
Emerging growth company	<input type="checkbox"/>		

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 of each of the issuers' classes of common stock, as of the latest practicable date:

Common Stock, No Par Value
Class

11,158,701
Outstanding as of October 23, 2020

FARMERS & MERCHANTS BANCORP, INC.
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101.INS	Inline XBRL Instance Document - The instance document does not appear in the Interactive Data File because its XBRL tags are embedded within the Inline XBRL document. (1)	
101.SCH	Inline XBRL Taxonomy Extension Schema Document (1)	
101.CAL	Inline XBRL Taxonomy Extension Calculation Linkbase Document (1)	
101.DEF	Inline XBRL Taxonomy Extension Definition Linkbase Document (1)	
101.LAB	Inline XBRL Taxonomy Extension Label Linkbase Document (1)	
101.PRE	Inline XBRL Taxonomy Extension Presentation Linkbase Document (1)	

(1) Pursuant to Rule 406T of Regulation S-T, the interactive Data Files in Exhibit 101 hereto are deemed not filed or part of a registration statement or prospectus for purposes of Sections 11 or 12 of the Securities act of 1933, as amended, are deemed not filed for purposes of Section 18 of the Exchange Act of 1934, as amended, and otherwise are not subject to liability under those sections.

	(in thousands of dollars)	
	September 30, 2020	December 31, 2019
	(Unaudited)	
Assets		
Cash and due from banks	\$ 46,395	\$ 50,137
Federal funds sold	41,358	1,159
Total cash and cash equivalents	87,753	51,296
Interest-bearing time deposits	4,657	4,309
Securities - available-for-sale	259,041	222,293
Other securities, at cost	5,827	5,810
Loans held for sale	7,621	4,248
Loans, net	1,351,979	1,211,771
Premises and equipment	26,776	26,283
Construction in progress	-	68
Goodwill	47,340	47,340
Mortgage servicing rights	3,027	2,629
Other real estate owned	206	214
Bank owned life insurance	15,501	15,235
Other assets	16,872	15,834
Total Assets	\$ 1,826,600	\$ 1,607,330

Liabilities and Stockholders' Equity

Liabilities		
Deposits		
Noninterest-bearing	\$ 330,845	\$ 265,156
Interest-bearing		
NOW accounts	534,792	423,655
Savings	392,059	322,973
Time	261,177	276,563
Total deposits	1,518,873	1,288,347
Federal funds purchased and securities sold under agreements to repurchase	29,859	48,073
Federal Home Loan Bank (FHLB) advances	17,724	24,806
Dividend payable	1,882	1,768
Accrued expenses and other liabilities	14,841	14,078
Total liabilities	1,583,179	1,377,072

Commitments and Contingencies

Stockholders' Equity		
Common stock - No par value 20,000,000 shares authorized; issued and outstanding 12,230,000 shares 9/30/20 and 12/31/19	81,577	81,535
Treasury stock - 1,071,299 shares 9/30/20, 1,093,065 shares 12/31/19	(12,397)	(12,456)
Retained earnings	168,381	160,081
Accumulated other comprehensive income	5,860	1,098
Total stockholders' equity	243,421	230,258
Total Liabilities and Stockholders' Equity	\$ 1,826,600	\$ 1,607,330

See Notes to Condensed Consolidated Unaudited Financial Statements.

Note: The December 31, 2019, Condensed Consolidated Balance Sheet has been derived from the audited Consolidated Balance Sheet as of that date.

FARMERS & MERCHANTS BANCORP, INC. AND SUBSIDIARIES
CONDENSED CONSOLIDATED STATEMENTS OF INCOME
(Unaudited)

	(in thousands of dollars, except per share data)		(in thousands of dollars, except per share data)	
	Three Months Ended		Nine Months Ended	
	September 30, 2020	September 30, 2019	September 30, 2020	September 30, 2019
Interest Income				
Loans, including fees	\$ 16,181	\$ 15,202	\$ 48,256	\$ 46,605
Debt securities:				
U.S. Treasury and government agencies	761	972	2,674	2,501
Municipalities	279	190	784	612
Dividends	36	69	107	233
Federal funds sold	4	120	15	319
Other	32	459	194	887
Total interest income	17,293	17,012	52,030	51,157
Interest Expense				
Deposits	1,864	3,654	7,019	9,606
Federal funds purchased and securities sold under agreements to repurchase	174	201	605	527
Borrowed funds	231	257	754	813
Total interest expense	2,269	4,112	8,378	10,946
Net Interest Income - Before Provision for Loan Losses	15,024	12,900	43,652	40,211
Provision for Loan Losses	1,987	247	4,986	410
Net Interest Income After Provision for Loan Losses	13,037	12,653	38,666	39,801
Noninterest Income				
Customer service fees	2,299	1,722	6,143	4,994
Other service charges and fees	879	1,179	2,622	3,311
Net gain on sale of loans	1,537	260	2,128	558
Net gain (loss) on sale of available-for-sale securities	-	-	270	(26)
Total noninterest income	4,715	3,161	11,163	8,837
Noninterest Expense				
Salaries and wages	5,102	4,158	13,420	12,300
Employee benefits	1,566	1,331	4,461	4,148
Net occupancy expense	558	630	1,686	1,911
Furniture and equipment	875	720	2,383	2,179
Data processing	490	482	1,340	2,157
Franchise taxes	368	248	1,105	735
ATM expense	444	416	1,234	1,281
Advertising	411	587	979	1,229
Net (gain) loss on sale of other assets owned	(7)	22	(13)	65
FDIC assessment	194	-	410	194
Mortgage servicing rights amortization	296	149	784	329
Consulting fees	205	196	561	404
Other general and administrative	1,786	1,667	5,027	4,897
Total noninterest expense	12,288	10,606	33,377	31,829
Income Before Income Taxes	5,464	5,208	16,452	16,809
Income Taxes	1,054	933	3,133	3,130
Net Income	\$ 4,410	\$ 4,275	\$ 13,319	\$ 13,679
Basic and Diluted Earnings Per Share	\$ 0.40	\$ 0.38	\$ 1.20	\$ 1.23
Dividends Declared	\$ 0.17	\$ 0.15	\$ 0.49	\$ 0.45

See Notes to Condensed Consolidated Unaudited Financial Statements

FARMERS & MERCHANTS BANCORP, INC. AND SUBSIDIARIES
CONDENSED CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME
(Unaudited)

	(in thousands of dollars) Three Months Ended		(in thousands of dollars) Nine Months Ended	
	September 30, 2020	September 30, 2019	September 30, 2020	September 30, 2019
Net Income	\$ 4,410	\$ 4,275	\$ 13,319	\$ 13,679
Other Comprehensive Income (Net of Tax):				
Net unrealized gain on available-for-sale securities	639	841	6,298	5,651
Reclassification adjustment for realized (gain) loss on sale of available-for-sale securities	-	-	(270)	26
Net unrealized gain on available-for-sale securities	639	841	6,028	5,677
Tax expense	134	176	1,266	1,192
Other comprehensive income	505	665	4,762	4,485
Comprehensive Income	<u>\$ 4,915</u>	<u>\$ 4,940</u>	<u>\$ 18,081</u>	<u>\$ 18,164</u>

See Notes to Condensed Consolidated Unaudited Financial Statements

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FARMERS & MERCHANTS BANCORP, INC. AND SUBSIDIARIES
CONDENSED CONSOLIDATED STATEMENTS OF CHANGES TO STOCKHOLDERS' EQUITY
FOR THE THREE AND NINE MONTHS ENDED SEPTEMBER 30, 2020
(000'S OMITTED, EXCEPT PER SHARE DATA)
(Unaudited)

	Shares of Common Stock	Common Stock	Treasury Stock	Retained Earnings	Accumulated Other Comprehensive Income	Total Stockholders' Equity
Balance - January 1, 2020	11,136,935	\$ 81,535	\$ (12,456)	\$ 160,081	\$ 1,098	\$ 230,258
Net income				4,105		4,105
Other comprehensive income					3,735	3,735
Purchase of treasury stock	(7,064)		(170)			(170)
Forfeiture of 450 shares of restricted stock	(450)	11	(10)	(2)		(1)
Stock-based compensation expense		298				298
Cash dividends declared - \$0.16 per share				(1,768)		(1,768)
Balance - March 31, 2020	11,129,421	81,844	(12,636)	162,416	4,833	236,457
Net income				4,804		4,804
Other comprehensive income					522	522
Purchase of treasury stock	(2,508)		(56)			(56)
Stock-based compensation expense		290				290
Director stock award	2,112		24	24		48
Cash dividends declared - \$0.16 per share				(1,768)		(1,768)
Balance - June 30, 2020	11,129,025	82,134	(12,668)	165,476	5,355	240,297
Net income				4,410		4,410
Other comprehensive income					505	505
Purchase of treasury stock	(6,875)		(150)			(150)
Issuance of 36,551 shares of restricted stock	36,551	(796)	421	377		2
Stock-based compensation expense		239				239
Cash dividends declared - \$0.17 per share				(1,882)		(1,882)
Balance - September 30, 2020	<u>11,158,701</u>	<u>\$ 81,577</u>	<u>\$ (12,397)</u>	<u>\$ 168,381</u>	<u>\$ 5,860</u>	<u>\$ 243,421</u>

See Notes to Condensed Consolidated Unaudited Financial Statements

FARMERS & MERCHANTS BANCORP, INC. AND SUBSIDIARIES
CONDENSED CONSOLIDATED STATEMENTS OF CHANGES TO STOCKHOLDERS' EQUITY
FOR THE THREE AND NINE MONTHS ENDED SEPTEMBER 30, 2019
(000'S OMITTED, EXCEPT PER SHARE DATA)
(Unaudited)

	Shares of Common Stock	Common Stock	Treasury Stock	Retained Earnings	Accumulated Other Comprehensive Income (Loss)	Total Stockholders' Equity
Balance - January 1, 2019	9,285,261	\$ 10,823	\$ (12,409)	\$ 147,887	\$ (3,014)	\$ 143,287
Net income				3,224		3,224
Other comprehensive income					1,402	1,402
Issuance of 1,830,000 shares of common stock in acquisition	1,830,000	70,437				70,437
Purchase of treasury stock	(6,558)		(213)			(213)
Issuance of 400 shares of restricted stock (Net of forfeitures - 2,040)	(1,640)	66	(58)	9		17
Stock-based compensation expense		434				434
Cash dividends declared - \$0.15 per share				(1,654)		(1,654)
Balance - March 31, 2019	11,107,063	81,760	(12,680)	149,466	(1,612)	216,934
Net income				6,180		6,180
Other comprehensive income					2,418	2,418
Forfeiture of 880 shares of restricted stock	(880)	38	(27)	2		13
Stock-based compensation expense		157				157
Cash dividends declared - \$0.15 per share				(1,655)		(1,655)
Balance - June 30, 2019	11,106,183	81,955	(12,707)	153,993	806	224,047
Net income				4,275		4,275
Other comprehensive income					665	665
Purchase of treasury stock	(6,569)		(165)			(165)
Issuance of 37,700 shares of restricted stock (Net of forfeitures - 300)	37,400	(925)	419	515		9
Stock-based compensation expense		234				234
Cash dividends declared - \$0.15 per share				(1,657)		(1,657)
Balance - September 30, 2019	11,137,014	\$ 81,264	\$ (12,453)	\$ 157,126	\$ 1,471	\$ 227,408

See Notes to Condensed Consolidated Unaudited Financial Statements

FARMERS & MERCHANTS BANCORP, INC. AND SUBSIDIARIES
CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS (Unaudited)

(in thousands of dollars)
Nine Months Ended

	September 30, 2020	September 30, 2019
Cash Flows from Operating Activities		
Net income	\$ 13,319	\$ 13,679
Adjustments to reconcile net income to net cash from operating activities:		
Depreciation	1,993	1,980
Amortization of premiums on available-for-sale securities, net	900	579
Amortization of servicing rights	784	329
Amortization of core deposit intangible	546	546
Net amortization (accretion) of fair value adjustments	382	(1,530)
Stock-based compensation expense	827	825
Director stock award	48	-
Deferred income taxes	(3)	(200)
Provision for loan loss	4,986	410
Gain on sale of loans held for sale	(2,128)	(558)
Originations of loans held for sale	(151,477)	(50,428)
Proceeds from sale of loans held for sale	150,130	48,543
(Gain) loss on sale of other assets owned	(13)	65
(Gain) loss on sales of securities available-for-sale	(270)	26
Change in other assets and other liabilities, net	(3,531)	5,750
Net cash provided by operating activities	<u>16,493</u>	<u>20,016</u>
Cash Flows from Investing Activities		
Activity in available-for-sale securities:		
Maturities, prepayments and calls	67,137	34,384
Sales	11,843	11,100
Purchases	(110,330)	(44,936)
Activity in other securities, at cost:		
Sales	-	237
Purchases	(17)	-
Change in interest-bearing time deposits	(348)	(535)
Proceeds from sale of other assets owned	92	371
Additions to premises and equipment	(2,407)	(2,805)
Loan originations and principal collections, net	(144,978)	(51,240)
Acquisition of Limberlost, net of cash received	-	(2,089)
Net cash used in investing activities	<u>(179,008)</u>	<u>(55,513)</u>
Cash Flows from Financing Activities		
Net change in deposits	230,359	142,853
Net change in federal funds purchased and securities sold under agreements to repurchase	(18,214)	(2,125)
Repayment of FHLB advances	(7,493)	(23,938)
Purchase of treasury stock	(376)	(378)
Cash dividends paid on common stock	(5,304)	(4,688)
Net cash provided by financing activities	<u>198,972</u>	<u>111,724</u>
Net Increase in Cash and Cash Equivalents	<u>36,457</u>	<u>76,227</u>
Cash and Cash Equivalents - Beginning of year	<u>51,296</u>	<u>38,365</u>
Cash and Cash Equivalents - End of period	<u>\$ 87,753</u>	<u>\$ 114,592</u>

(continued)

FARMERS & MERCHANTS BANCORP, INC. AND SUBSIDIARIES
 CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS (Unaudited) (Continued)

(in thousands of dollars)

Nine Months Ended

	September 30, 2020	September 30, 2019
Supplemental Information		
Cash paid during the period for:		
Interest	\$ 7,970	\$ 9,962
Income taxes	\$ 4,700	\$ 2,345
Noncash investing activities:		
Transfer of loans to other real estate owned	\$ 71	\$ 187
The Company purchased all of the capital stock of Limberlost for \$78,902 on January 1, 2019. In conjunction with the acquisition, liabilities were assumed as follows:		
Fair value of assets acquired	\$ -	\$ 336,380
Less: common stock issued	-	70,437
Cash paid for the capital stock	-	8,465
Liabilities assumed	\$ -	\$ 257,478

See Notes to Condensed Consolidated Unaudited Financial Statements.

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NOTE 1 BASIS OF PRESENTATION AND OTHER

The accompanying unaudited condensed consolidated financial statements have been prepared in accordance with generally accepted accounting principles for interim financial information and with the instructions for Form 10Q and Rule 10-01 of Regulation S-X; accordingly, they do not include all of the information and footnotes required by generally accepted accounting principles for complete financial statements. In the opinion of management, all adjustments, consisting of normal recurring accruals, considered necessary for a fair presentation have been included. Operating results for the three and nine months ended September 30, 2020 are not necessarily indicative of the results that are expected for the year ended December 31, 2020. The condensed consolidated balance sheet of the Company as of December 31, 2019, has been derived from the audited consolidated balance sheet of the Company as of that date. These condensed consolidated financial statements should be read in conjunction with the consolidated financial statements and footnotes thereto included in the Company's Annual Report on Form 10-K for the year ended December 31, 2019.

The Company recognizes revenues as they are earned based on contractual terms, as transactions occur, or as services are provided and collectability is reasonably assured. The Company's principal source of revenue is interest income from loans and investment securities. The Company also earns noninterest income from various banking and financial services offered primarily through Farmers & Merchants State Bank. Interest income is primarily recognized on an accrual basis according to nondiscretionary formulas written in contracts, such as loan agreements or investment security contracts. The Company also earns noninterest income from various banking and financial services provided to business and consumer clients such as deposit account, debit card, and mortgage banking services. Revenue is recorded for noninterest income based on the contractual terms for the service or transaction performed.

NOTE 2 BUSINESS COMBINATION AND ASSET PURCHASE

On January 1, 2019, the Company acquired Limberlost Bancshares, Inc. ("Limberlost"), the bank holding company for Bank of Geneva, a community bank based in Geneva, Indiana. Bank of Geneva operated six full-service offices in the northeast Indiana communities of Geneva, Berne, Decatur, Monroe, Portland and Monroeville. Shareholders of Limberlost received 1,830 shares of FMAO common stock and \$8,465.00 in cash for each share. Limberlost had 1,000 shares outstanding on January 1, 2019. The share price of Farmers & Merchants Bancorp, Inc. (FMAO) stock on January 1, 2019 was \$38.49. Total consideration for the acquisition was approximately \$78.9 million consisting of \$8.5 million in cash and \$70.4 million in stock. As a result of the acquisition, the Company has had an opportunity to increase its deposit base and reduce transaction costs. The Company also expects to reduce costs through economies of scale.

Under the acquisition method of accounting, the total purchase was allocated to net tangible and intangible assets based on their current estimated fair values on the date of acquisition. Of the total purchase price of \$78.9 million, \$3.9 million has been allocated to core deposit intangible included in other assets and is being amortized over seven years on a straight line basis. Goodwill of \$43.3 million resulting from the acquisition consists largely of the synergies and economies of scale expected from combining the operations of the Company and Bank of Geneva. Of that total amount, none of the purchase price is deductible for tax purposes. The following table summarizes the consideration paid for Bank of Geneva and the amounts of the assets acquired and liabilities assumed recognized at the acquisition date.

Fair Value of Consideration Transferred

	(In Thousands)
Cash	\$ 8,465
Common Shares (1,830,000 shares)	70,437
Total	\$ 78,902

Recognized amounts of identifiable assets acquired and liabilities assumed

Assets	
Cash and cash equivalents	\$ 6,376
Securities - available-for-sale	17,494
Other securities, at cost	2,347
Loans, net	257,183
Premises and equipment	2,538
Goodwill	43,266
Other assets	7,176
Total Assets Purchased	\$ 336,380

Liabilities	
Deposits	
Noninterest bearing	\$ 37,822
Interest bearing	168,312
Total deposits	206,134
Federal Home Loan Bank (FHLB) advances	48,196
Accrued expenses and other liabilities	3,148
Total Liabilities Assumed	\$ 257,478

The Company acquired loans in the acquisition that had evidence of deterioration of credit quality since origination and it was probable, at acquisition, that all contractually required payments would not be collected.

Loans purchased with evidence of credit deterioration since origination and for which it is probable that all contractually required payments will not be collected are considered to be credit impaired. Evidence of credit quality deterioration as of the purchase date may include information such as past-due and nonaccrual status, borrower credit scores and recent loan to value percentages. Purchased credit-impaired loans are accounted for under the accounting guidance for loans and debt securities acquired with deteriorated credit quality (ASC 310-30) and initially measured at fair value, which includes estimated future credit losses expected to be incurred over the life of the loan. Accordingly, an allowance for credit losses related to these loans is not carried over and recorded at the acquisition date. Management estimated the cash flows expected to be collected at acquisition using our internal risk models, which incorporate the estimate of current key assumptions, such as default rates, severity and prepayment speeds.

The carrying amount of those loans is included in loans, net on the balance sheet as of December 31, 2019 and September 30, 2020. The amounts of loans at December 31, 2019 and September 30, 2020 are as follows:

	2019 (In Thousands)	
Balance - January 1, 2019		
Commercial	\$	4,094
Consumer RE		231
Consumer		71
Carrying amount, net of fair value adjustment of \$2,118	\$	<u>2,278</u>
Balance - December 31, 2019		
Commercial	\$	106
Consumer RE		-
Consumer		-
Carrying amount, net of fair value adjustment of \$62	\$	<u>44</u>
Balance - September 30, 2020		
Commercial	\$	-
Consumer RE		-
Consumer		-
Carrying amount, net of fair value adjustment of \$0	\$	<u>-</u>

Loans acquired during 2019 for which it was probable at acquisition that all contractually required payments would not be collected are as follows:

	(In Thousands)	
Contractually required payments receivable at acquisition		
Commercial	\$	4,215
Consumer RE		261
Consumer		94
Total required payments receivable	\$	<u>4,570</u>
Cash flows expected to be collected at acquisition	\$	2,788
Basis in acquired loans at acquisition	\$	4,396

The balance of the fair value adjustment for loans acquired and accounted for under this guidance (ASC 310-30) was \$62 thousand at December 31, 2019, zero at September 30, 2020 and \$2.118 million on January 1, 2019.

Changes in accretable yield, or income expected to be collected, are as follows:

	Three Months Ended September 30, 2020 (In Thousands)	Three Months Ended September 30, 2019 (In Thousands)	Nine Months Ended September 30, 2020 (In Thousands)	Nine Months Ended September 30, 2019 (In Thousands)
Beginning Balance	\$ 1,871	\$ 2,329	\$ 2,021	\$ 2,544
Additions	-	-	2	6
Accretion	(107)	(112)	(321)	(2,316)
Reclassification from nonaccretable difference	-	34	62	2,019
Disposals	(5)	(6)	(5)	(8)
Ending Balance	<u>\$ 1,759</u>	<u>\$ 2,245</u>	<u>\$ 1,759</u>	<u>\$ 2,245</u>

The Company purchased an office on December 13, 2013 in Custar, Ohio. Core deposit intangible assets of \$1.17 million were recognized and are being amortized over its remaining economic useful life of the deposits of 7 years on a straight line basis.

As mentioned previously, the acquisition of Bank of Geneva resulted in the recognition of \$3.9 million in core deposit intangible assets which are being amortized over its remaining life of 7 years on a straight line basis.

The amortization expense for the nine months ended September 30, 2019 was \$546 thousand. Of the \$721 thousand to be expensed in 2020, \$546 thousand has been expensed for the nine months ended September 30, 2020. Annual amortization of core deposit intangible assets is as follows:

	<u>(In Thousands)</u>	<u>(In Thousands)</u>	<u>(In Thousands)</u>
	Custar	Geneva	Total
2020	\$ 161	\$ 560	\$ 721
2021	-	560	560
2022	-	560	560
2023	-	560	560
2024	-	560	560
2025	-	560	560
	<u>\$ 161</u>	<u>\$ 3,360</u>	<u>\$ 3,521</u>

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NOTE 3 SECURITIES

Mortgage-backed securities, as shown in the following tables, are all government sponsored enterprises. The amortized cost and fair value of securities, with gross unrealized gains and losses at September 30, 2020 and December 31, 2019, are as follows:

	(In Thousands)			
	September 30, 2020			
	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
Available-for-Sale:				
U.S. Treasury	\$ 3,000	\$ 4	\$ -	\$ 3,004
U.S. Government agencies	88,120	1,952	(10)	90,062
Mortgage-backed securities	100,858	2,153	(31)	102,980
State and local governments	59,646	3,355	(6)	62,995
Total available-for-sale securities	<u>\$ 251,624</u>	<u>\$ 7,464</u>	<u>\$ (47)</u>	<u>\$ 259,041</u>

	(In Thousands)			
	December 31, 2019			
	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
Available-for-Sale:				
U.S. Treasury	\$ 10,023	\$ 10	\$ (12)	\$ 10,021
U.S. Government agencies	61,882	584	(21)	62,445
Mortgage-backed securities	94,998	426	(227)	95,197
State and local governments	54,001	749	(120)	54,630
Total available-for-sale securities	<u>\$ 220,904</u>	<u>\$ 1,769</u>	<u>\$ (380)</u>	<u>\$ 222,293</u>

Investment securities will at times depreciate to an unrealized loss position. The Company utilizes the following criteria to assess whether impairment is other than temporary. No one item by itself will necessarily signal that a security should be recognized as an other than temporary impairment.

1. The fair value of the security has significantly declined from book value.
2. A downgrade has occurred that lowered the credit rating to below investment grade (below Baa3 by Moody and BBB – by Standard and Poors.)
3. Dividends have been reduced or eliminated or scheduled interest payments have not been made.
4. The underwater security has longer than 10 years to maturity and the loss position had existed for more than 3 years.
5. Management does not possess both the intent and ability to hold the security for a period of time sufficient to allow for any anticipated recovery in fair value.

If the impairment is judged to be other than temporary, the cost basis of the individual security shall be written down to fair value, thereby establishing a new cost basis. The new cost basis shall not be changed for subsequent recoveries in fair value. The amount of the write down shall be included in current earnings as a realized loss. The recovery in fair value, if any, shall be recognized in earnings when the security is sold. The table below is presented by category of security and length of time in a continuous loss position. The Company currently does not hold any securities with other than temporary impairment.

Information pertaining to securities with gross unrealized losses at September 30, 2020 and December 31, 2019, aggregated by investment category and length of time that individual securities have been in a continuous loss position follows:

	(In Thousands)					
	September 30, 2020					
	Less Than Twelve Months		Twelve Months & Over		Total	
	Gross Unrealized Losses	Fair Value	Gross Unrealized Losses	Fair Value	Gross Unrealized Losses	Fair Value
U.S. Treasury	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -
U.S. Government agencies	(10)	14,010	-	-	(10)	14,010
Mortgage-backed securities	(31)	11,298	-	-	(31)	11,298
State and local governments	(6)	1,061	-	-	(6)	1,061
Total available-for-sale securities	\$ (47)	\$ 26,369	\$ -	\$ -	\$ (47)	\$ 26,369

	(In Thousands)					
	December 31, 2019					
	Less Than Twelve Months		Twelve Months & Over		Total	
	Gross Unrealized Losses	Fair Value	Gross Unrealized Losses	Fair Value	Gross Unrealized Losses	Fair Value
U.S. Treasury	\$ -	\$ -	\$ (12)	\$ 5,030	\$ (12)	\$ 5,030
U.S. Government agencies	(16)	10,549	(5)	10,745	(21)	21,294
Mortgage-backed securities	(102)	27,696	(125)	11,332	(227)	39,028
State and local governments	(120)	16,845	-	-	(120)	16,845
Total available-for-sale securities	\$ (238)	\$ 55,090	\$ (142)	\$ 27,107	\$ (380)	\$ 82,197

Unrealized losses on securities have not been recognized into income because the issuers' bonds are of high credit quality, values have only been impacted by rate changes, and the Company has the intent and ability to hold the securities for the foreseeable future. Additionally, the decline in value is primarily due to changes in interest rates since the securities were purchased. The fair value is expected to recover as the bonds approach the maturity date.

Below are the gross realized gains and losses for the three and nine months ended September 30, 2020 and September 30, 2019.

	Three Months (In Thousands)		Nine Months (In Thousands)	
	2020	2019	2020	2019
	Gross realized gains	\$ -	\$ -	\$ 270
Gross realized losses	-	-	-	(42)
Net realized gains (losses)	\$ -	\$ -	\$ 270	\$ (26)
Tax expense (benefit) related to net realized gains (losses)	\$ -	\$ -	\$ 57	\$ (5)

The net realized gains (losses) on sales and related tax expense is a reclassification out of accumulated other comprehensive income (loss). The net realized gains (losses) is included in net gains (losses) on sale of available-for-sale securities and the related tax expense (benefit) is included in income taxes in the condensed consolidated statements of income and comprehensive income.

The amortized cost and fair value of debt securities at September 30, 2020, by contractual maturity, are shown below. Expected maturities will differ from contractual maturities because borrowers may have the right to call or prepay obligations with or without call or prepayment penalties.

	(In Thousands)	
	Amortized Cost	Fair Value
One year or less	\$ 9,390	\$ 9,410
After one year through five years	49,534	50,784
After five years through ten years	84,035	87,646
After ten years	7,807	8,221
Total	\$ 150,766	\$ 156,061
Mortgage-backed securities	100,858	102,980
Total	\$ 251,624	\$ 259,041

Investments with a carrying value of \$87.1 million and \$88.8 million at September 30, 2020 and December 31, 2019, respectively, were pledged to secure public deposits and securities sold under repurchase agreements.

Other securities include Federal Home Loan Bank of Cincinnati and Indianapolis stock in the amount of \$5.8 million as of September 30, 2020 and December 31, 2019, in addition to Ohio Equity Fund for Housing Limited Partnership of \$38 thousand and \$21 thousand as of September 30, 2020 and December 31, 2019.

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NOTE 4 LOANS

Loan balances as of September 30, 2020 and December 31, 2019 are summarized below:

<u>Loans:</u>	(In Thousands)	
	September 30, 2020	December 31, 2019
Consumer Real Estate	\$ 175,963	\$ 165,349
Agricultural Real Estate	192,883	199,105
Agricultural	103,330	111,820
Commercial Real Estate	595,146	551,309
Commercial and Industrial	238,175	135,631
Consumer	53,320	49,237
Other	9,030	8,314
	<u>1,367,847</u>	<u>1,220,765</u>
Less: Net deferred loan fees and costs	<u>(3,985)</u>	<u>(1,766)</u>
	<u>1,363,862</u>	<u>1,218,999</u>
Less: Allowance for loan losses	<u>(11,883)</u>	<u>(7,228)</u>
Loans - Net	<u>\$ 1,351,979</u>	<u>\$ 1,211,771</u>

Other loans primarily fund public improvement in the Bank's service area.

The distribution of fixed rate loans and variable rate loans by major loan category is as follows as of September 30, 2020:

	(In Thousands)	
	Fixed Rate	Variable Rate
Consumer Real Estate	\$ 128,976	\$ 46,987
Agricultural Real Estate	101,191	91,692
Agricultural	89,810	13,520
Commercial Real Estate	446,886	148,260
Commercial and Industrial	210,588	27,587
Consumer	49,050	4,270
Other	8,976	54

As of September 30, 2020 and December 31, 2019 one to four family residential mortgage loans amounting to \$40.5 million and \$42.1 million, respectively, have been pledged as security for future loans and existing loans the Bank has received from the Federal Home Loan Bank.

Unless listed separately, Other loans are included in the Commercial and Industrial category for the remainder of the tables in this Note 4.

The following table represents the contractual aging of the recorded investment (in thousands) in past due loans by portfolio classification of loans as of September 30, 2020 and December 31, 2019, net of deferred loan fees and costs:

	30-59 Days Past Due	60-89 Days Past Due	Greater Than 90 Days	Total Past Due	Current	Total Financing Receivables	Recorded Investment > 90 Days and Accruing
September 30, 2020							
Consumer Real Estate	\$ 80	\$ 33	\$ -	\$ 113	\$ 175,482	\$ 175,595	\$ -
Agricultural Real Estate	-	-	-	-	192,577	192,577	-
Agricultural	-	-	-	-	103,476	103,476	-
Commercial Real Estate	169	-	-	169	593,767	593,936	-
Commercial and Industrial	-	-	-	-	244,823	244,823	-
Consumer	34	8	-	42	53,413	53,455	-
Total	\$ 283	\$ 41	\$ -	\$ 324	\$ 1,363,538	\$ 1,363,862	\$ -

	30-59 Days Past Due	60-89 Days Past Due	Greater Than 90 Days	Total Past Due	Current	Total Financing Receivables	Recorded Investment > 90 Days and Accruing
December 31, 2019							
Consumer Real Estate	\$ 355	\$ 70	\$ -	\$ 425	\$ 164,266	\$ 164,691	\$ -
Agricultural Real Estate	-	107	-	107	198,752	198,859	-
Agricultural	78	7	-	85	111,864	111,949	-
Commercial Real Estate	-	-	-	-	550,082	550,082	-
Commercial and Industrial	201	267	-	468	143,541	144,009	-
Consumer	54	-	-	54	49,355	49,409	-
Total	\$ 688	\$ 451	\$ -	\$ 1,139	\$ 1,217,860	\$ 1,218,999	\$ -

The following table presents the recorded investment in nonaccrual loans by class of loans as of September 30, 2020 and December 31, 2019:

	(In Thousands)	
	September 30, 2020	December 31, 2019
Consumer Real Estate	\$ 1,523	\$ 1,209
Agricultural Real Estate	3,775	88
Agricultural	517	1,769
Commercial Real Estate	685	37
Commercial & Industrial	1,328	288
Consumer	42	9
Total	<u>\$ 7,870</u>	<u>\$ 3,400</u>

Following are the characteristics and underwriting criteria for each major type of loan the Bank offers:

Consumer Real Estate: Purchase, refinance, or equity financing of one to four family owner occupied dwelling. Success in repayment is subject to borrower's income, debt level, character in fulfilling payment obligations, employment, and others.

Agricultural Real Estate: Purchase of farm real estate or for permanent improvements to the farm real estate. Cash flow from the farm operation is the repayment source and is therefore subject to the financial success of the farm operation.

Agricultural: Loans for the production and housing of crops, fruits, vegetables, and livestock or to fund the purchase or re-finance of capital assets such as machinery and equipment and livestock. The production of crops and livestock is especially vulnerable to commodity prices and weather. The vulnerability to commodity prices is offset by the farmer's ability to hedge their position by the use of future contracts. The risk related to weather is often mitigated by requiring crop insurance.

Commercial Real Estate: Construction, purchase, and refinance of business purpose real estate. Risks include potential construction delays and overruns, vacancies, collateral value subject to market value fluctuations, interest rate, market demands, borrower's ability to repay in orderly fashion, and others. The Bank does employ stress testing on higher balance loans to mitigate risk by ensuring the customer's ability to repay in a changing rate environment before granting loan approval.

Commercial and Industrial: Loans to proprietorships, partnerships, or corporations to provide temporary working capital and seasonal loans as well as long term loans for capital asset acquisition. Risks include adequacy of cash flow, reasonableness of projections, financial leverage, economic trends, management ability and estimated capital expenditures during the fiscal year. The Bank does employ stress testing on higher balance loans to mitigate risk by ensuring the customer's ability to repay in a changing rate environment before granting loan approval.

Other: Primarily funds public improvements in the Bank's service area. Repayment ability is based on the continuance of the taxation revenue as the source of repayment.

Consumer: Funding for individual and family purposes. Success in repayment is subject to borrower's income, debt level, character in fulfilling payment obligations, employment, and others.

The Bank uses a nine tier risk rating system to grade its loans. The grade of a loan may change during the life of the loan.

The risk ratings are described as follows.

1. Zero (0) Unclassified. Any loan which has not been assigned a classification.
2. One (1) Excellent. Credit to premier customers having the highest credit rating based on an extremely strong financial condition, which compares favorably with industry standards (upper quartile of Risk Management Association ratios). Financial statements indicate a sound earnings and financial ratio trend for several years with satisfactory profit margins and excellent liquidity exhibited. Prime credits may also be borrowers with loans fully secured by highly liquid collateral such as traded stocks, bonds, certificates of deposit, savings account, etc. No credit or collateral exceptions exist and the loan adheres to the Bank's loan policy in every respect. Financing alternatives would be readily available and would qualify for unsecured credit. This grade is summarized by high liquidity, minimum risk, strong ratios, and low handling costs.

3. Two (2) Good. Desirable loans of somewhat less stature than Grade 1, but with strong financial statements. Loan supported by financial statements containing strong balance sheets, generally with a leverage position less than 1.50, and a history of profitability. Probability of serious financial deterioration is unlikely. Possessing a sound repayment source (and a secondary source), which would allow repayment in a reasonable period of time. Individual loans backed by liquid personal assets, established history and unquestionable character.
4. Three (3) Satisfactory. Satisfactory loans of average or slightly above average risk – having some deficiency or vulnerability to changing economic conditions, but still fully collectible. Projects should normally demonstrate acceptable debt service coverage. Generally, customers should have a leverage position less than 2.00. May be some weakness but with offsetting features of other support readily available. Loans that are meeting the terms of repayment. Loans may be graded 3 when there is no recent information on which to base a current risk evaluation and the following conditions apply:

At inception, the loan was properly underwritten and did not possess an unwarranted level of credit risk:

 - a. At inception, the loan was secured with collateral possessing a loan-to-value adequate to protect the Bank from loss;
 - b. The loan exhibited two or more years of satisfactory repayment with a reasonable reduction of the principal balance;
 - c. During the period that the loan has been outstanding, there has been no evidence of any credit weakness. Some examples of weakness include slow payment, lack of cooperation by the borrower, breach of loan covenants, or the business is in an industry which is known to be experiencing problems. If any of these credit weaknesses are observed, a lower risk grade is warranted.
5. Four (4) Satisfactory / Monitored. A “4” (Satisfactory/Monitored) risk grade may be established for a loan considered satisfactory but which is of average credit risk due to financial weakness or uncertainty. The loans warrant a higher than average level of monitoring to ensure that weaknesses do not advance. The level of risk in Satisfactory/Monitored classification is considered acceptable and within normal underwriting guidelines so long as the loan is given management supervision.
6. Five (5) Special Mention. Loans that possess some credit deficiency or potential weakness which deserve close attention but do not yet warrant substandard classification. Such loans pose unwarranted financial risk that if not corrected could weaken the loan and increase risk in the future. The key distinctions of a 5 (Special Mention) classification are that (1) it is indicative of an unwarranted level of risk, and (2) weaknesses are considered “potential” versus “defined” impairments to the primary source of loan repayment and collateral.
7. Six (6) Substandard. One or more of the following characteristics may be exhibited in loans classified substandard:
 - a. Loans which possess a defined credit weakness and the likelihood that a loan will be paid from the primary source and are uncertain. Financial deterioration is underway and very close attention is warranted to ensure that the loan is collected without loss.
 - b. Loans are inadequately protected by the current net worth and paying capacity of the borrower.
 - c. The primary source of repayment is weakened, and the Bank is forced to rely on a secondary source of repayment such as collateral liquidation or guarantees.
 - d. Loans are characterized by the distinct possibility that the Bank will sustain some loss if deficiencies are not corrected.
 - e. Unusual courses of action are needed to maintain a high probability of repayment.
 - f. The borrower is not generating enough cash flow to repay loan principal but continues to make interest payments.
 - g. The lender is forced into a subordinate position or unsecured collateral position due to flaws in documentation.
 - h. Loans have been restructured so that payment schedules, terms and collateral represent concessions to the borrower when compared to the normal loan terms.
 - i. The lender is seriously contemplating foreclosure or legal action due to the apparent deterioration in the loan.
 - j. There is significant deterioration in the market conditions and the borrower is highly vulnerable to these conditions.

8. Seven (7) Doubtful. One or more of the following characteristics may be exhibited in loans classified Doubtful:
 - a. Loans have all of the weaknesses of those classified as Substandard. Additionally, these weaknesses make collection or liquidation in full based on existing conditions improbable.
 - b. The primary source of repayment is gone, and there is considerable doubt as to the quality of the secondary source of repayment.
 - c. The possibility of loss is high, but because of certain important pending factors which may strengthen the loan, loss classification is deferred until its exact status is known. A Doubtful classification is established deferring the realization of the loss.
9. Eight (8) Loss. Loans are considered uncollectable and of such little value that continuing to carry them as assets on the institution's financial statements is not feasible. Loans will be classified Loss when it is neither practical nor desirable to defer writing off or reserving all or a portion of a basically worthless asset, even though partial recovery may be possible at some time in the future.

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The following table represents the risk category of loans by portfolio class, net of deferred fees and costs, based on the most recent analysis performed as of September 30, 2020 (Refer to the table in the COVID-19 section for deferrals impacted by the Coronavirus Aid, Relief and Economic Security Act (CARES Act.) and December 31, 2019:

		(In Thousands)				
		Agricultural Real Estate	Agricultural	Commercial Real Estate	Commercial and Industrial	Other
September 30, 2020						
1-2	\$	12,929	\$ 4,631	\$ 11,389	\$ 89,381	\$ -
3		38,127	26,818	164,410	26,846	4,716
4		112,786	69,383	402,362	110,393	4,314
5		10,387	1,991	10,631	4,143	-
6		18,348	653	5,144	4,131	-
7		-	-	-	899	-
8		-	-	-	-	-
Total	\$	<u>192,577</u>	<u>\$ 103,476</u>	<u>\$ 593,936</u>	<u>\$ 235,793</u>	<u>\$ 9,030</u>
		Agricultural Real Estate	Agricultural	Commercial Real Estate	Commercial and Industrial	Other
December 31, 2019						
1-2	\$	14,655	\$ 4,093	\$ 7,860	\$ 3,844	\$ -
3		33,951	36,913	131,780	19,790	3,168
4		116,834	65,414	401,404	103,527	5,146
5		14,836	2,300	3,699	2,465	-
6		18,583	3,229	5,339	4,983	-
7		-	-	-	1,086	-
8		-	-	-	-	-
Total	\$	<u>198,859</u>	<u>\$ 111,949</u>	<u>\$ 550,082</u>	<u>\$ 135,695</u>	<u>\$ 8,314</u>

For consumer residential real estate, and other, the Company also evaluates credit quality based on the aging status of the loan, as was previously stated, and by payment activity. The following tables present the recorded investment in those classes based on payment activity and assigned risk grading as of September 30, 2020 and December 31, 2019.

Grade	(In Thousands)	
	Consumer Real Estate	Consumer Real Estate
	September 30, 2020	December 31, 2019
Pass	\$ 172,132	\$ 160,930
Special Mention (5)	1,234	415
Substandard (6)	2,229	3,346
Doubtful (7)	-	-
Total	<u>\$ 175,595</u>	<u>\$ 164,691</u>

	(In Thousands)			
	Consumer - Credit		Consumer - Other	
	September 30, 2020	December 31, 2019	September 30, 2020	December 31, 2019
Performing	\$ 3,430	\$ 4,076	\$ 49,868	\$ 44,831
Nonperforming	-	15	157	487
Total	<u>\$ 3,430</u>	<u>\$ 4,091</u>	<u>\$ 50,025</u>	<u>\$ 45,318</u>

Information about impaired loans as of September 30, 2020, December 31, 2019 and September 30, 2019 are as follows:

	(In Thousands)		
	September 30, 2020	December 31, 2019	September 30, 2019
Impaired loans without a valuation allowance	\$ 5,134	\$ 2,420	\$ 1,914
Impaired loans with a valuation allowance	10,125	641	1,314
Total impaired loans	<u>\$ 15,259</u>	<u>\$ 3,061</u>	<u>\$ 3,228</u>
Valuation allowance related to impaired loans	\$ 1,198	\$ 197	\$ 187
Total non-accrual loans	<u>\$ 7,870</u>	<u>\$ 3,400</u>	<u>\$ 3,275</u>
Total loans past-due ninety days or more and still accruing	\$ 408	\$ -	\$ -
Quarter ended average investment in impaired loans	\$ 13,517	\$ 3,120	\$ 3,141
Year to date average investment in impaired loans	\$ 8,613	\$ 2,649	\$ 2,492

There were \$1.2 million additional funds available to be advanced in connection with impaired loans as of September 30, 2020.

The Bank had approximately \$6.4 million of its impaired loans classified as troubled debt restructured (TDR) as of September 30, 2020, \$1.0 million as of December 31, 2019 and \$1.1 million as of September 30, 2019.

Modification programs focused on payment pattern changes and/or modified maturity dates with most receiving a combination of the two concessions. The modifications did not result in the contractual forgiveness of principal. In 2020, two loans resulted in payment changes from a monthly payment to principal and interest at maturity on June 19, 2020. One loan was paid off in May with the other loan past due and in the foreclosure process. In the second quarter of 2020, three loans had a rate concession along with the amortization extended. During the third quarter of 2020, one loan was modified with a rate concession. All interest was paid current at the time of the modifications. Consequently, the financial impact of the modifications was immaterial to the ALLL. During the year to date 2020, there were 6 new loans considered TDR with one of the loans subsequently paid off in May. There were 5 new loans considered TDR year to date 2019. The following tables represents three and nine months ended September 30, 2020 and 2019:

Three Months September 30, 2020	Number of Contracts Modified in	Pre- Modification Outstanding	Post- Modification Outstanding	Nine Months September 30, 2020	Number of Contracts Modified in	Pre- Modification Outstanding	Post- Modification Outstanding
(in thousands)	the	Recorded	Recorded	(in thousands)	the	Recorded	Recorded
<u>Troubled</u>	<u>Debt</u>	<u>Last Three</u>		<u>Troubled</u>	<u>Debt</u>	<u>Last Nine</u>	
<u>Restructurings</u>	<u>Months</u>	<u>Investment</u>	<u>Investment</u>	<u>Restructurings</u>	<u>Months</u>	<u>Investment</u>	<u>Investment</u>
Consumer Real Estate	-	\$ -	\$ -	Consumer Real Estate	-	\$ -	\$ -
Commercial Real Estate	-	-	-	Commercial Real Estate	2	981	981
Ag Real Estate	-	-	-	Ag Real Estate	2	5,380	5,380
Commercial and Industrial	1	50	50	Commercial and Industrial	1	50	50
Agricultural	-	-	-	Agricultural	1	164	164

Three Months September 30, 2019	Number of Contracts Modified in	Pre- Modification Outstanding	Post- Modification Outstanding	Nine Months September 30, 2019	Number of Contracts Modified in	Pre- Modification Outstanding	Post- Modification Outstanding
(in thousands)	the	Recorded	Recorded	(in thousands)	the	Recorded	Recorded
<u>Troubled</u>	<u>Debt</u>	<u>Last Three</u>		<u>Troubled</u>	<u>Debt</u>	<u>Last Nine</u>	
<u>Restructurings</u>	<u>Months</u>	<u>Investment</u>	<u>Investment</u>	<u>Restructurings</u>	<u>Months</u>	<u>Investment</u>	<u>Investment</u>
Consumer Real Estate	1	\$ 74	\$ 74	Consumer Real Estate	1	\$ 74	\$ 74
Commercial Real Estate	-	-	-	Commercial Real Estate	-	-	-
Ag Real Estate	-	-	-	Ag Real Estate	-	-	-
Commercial and Industrial	-	-	-	Commercial and Industrial	4	812	812
Agricultural	-	-	-	Agricultural	-	-	-

For the three and nine month periods ended September 30, 2020 and 2019, there were no TDRs that subsequently defaulted after modification.

For the nine month period ended September 30, 2020, there was one impaired commercial real estate loan of \$481 thousand that was classified as TDR paid off. There were no impaired loans classified as TDR paid off for the nine month period ended September 30, 2019.

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For the majority of the Bank's impaired loans, the Bank will apply the fair value of collateral or use a measurement incorporating the present value of expected future cash flows discounted at the loan's effective rate of interest. To determine fair value of collateral, collateral asset values securing an impaired loan are periodically evaluated. Maximum time of re-evaluation is every 12 months for chattels and titled vehicles and every two years for real estate. In this process, third party evaluations are obtained. Until such time that updated appraisals are received, the Bank may discount the collateral value used.

The Bank uses the following guidelines as stated in policy to determine when to realize a charge-off, whether a partial or full loan balance. A charge-off in whole or in part is realized when unsecured consumer loans, credit card credits and overdraft lines of credit reach 90 days delinquency. At 120 days delinquent, secured consumer loans are charged down to the value of the collateral, if repossession of the collateral is assured and/or in the process of repossession. Consumer mortgage loan deficiencies are charged down upon the sale of the collateral or sooner upon the recognition of collateral deficiency. Commercial and agricultural credits are charged down at 120 days delinquency, unless an established and approved work-out plan is in place or litigation of the credit will likely result in recovery of the loan balance. Upon notification of bankruptcy, unsecured debt is charged off. Additional charge-off may be realized as further unsecured positions are recognized.

The following tables present loans individually evaluated for impairment by class of loans for the three and nine months ended September 30, 2020 and September 30, 2019 and for the year ended December 31, 2019.

(In Thousands)						
Three Months Ended September 30, 2020	Recorded Investment	Unpaid Principal Balance	Related Allowance	QTD Average Recorded Investment	QTD Interest Income Recognized	QTD Interest Income Recognized Cash Basis
With no related allowance recorded:						
Consumer Real Estate	\$ 780	\$ 780	\$ -	\$ 791	\$ 41	\$ 5
Agricultural Real Estate	1,589	1,589	-	873	2	-
Agricultural	533	533	-	375	4	1
Commercial Real Estate	186	186	-	186	1	-
Commercial and Industrial	2,021	2,021	-	1,190	5	-
Consumer	25	25	-	26	21	-
With a specific allowance recorded:						
Consumer Real Estate	205	205	43	119	8	-
Agricultural Real Estate	5,425	5,425	432	5,450	2	-
Agricultural	188	188	28	342	3	-
Commercial Real Estate	3,033	3,033	44	3,046	-	-
Commercial and Industrial	1,274	1,274	651	1,119	3	-
Consumer	-	-	-	-	-	-
Totals:						
Consumer Real Estate	<u>\$ 985</u>	<u>\$ 985</u>	<u>\$ 43</u>	<u>\$ 910</u>	<u>\$ 49</u>	<u>\$ 5</u>
Agricultural Real Estate	<u>\$ 7,014</u>	<u>\$ 7,014</u>	<u>\$ 432</u>	<u>\$ 6,323</u>	<u>\$ 4</u>	<u>\$ -</u>
Agricultural	<u>\$ 721</u>	<u>\$ 721</u>	<u>\$ 28</u>	<u>\$ 717</u>	<u>\$ 7</u>	<u>\$ 1</u>
Commercial Real Estate	<u>\$ 3,219</u>	<u>\$ 3,219</u>	<u>\$ 44</u>	<u>\$ 3,232</u>	<u>\$ 1</u>	<u>\$ -</u>
Commercial and Industrial	<u>\$ 3,295</u>	<u>\$ 3,295</u>	<u>\$ 651</u>	<u>\$ 2,309</u>	<u>\$ 8</u>	<u>\$ -</u>
Consumer	<u>\$ 25</u>	<u>\$ 25</u>	<u>\$ -</u>	<u>\$ 26</u>	<u>\$ 21</u>	<u>\$ -</u>

(In Thousands)						
Year Ended December 31, 2019	Recorded Investment	Unpaid Principal Balance	Related Allowance	Average Recorded Investment	Interest Income Recognized	Interest Income Recognized Cash Basis
With no related allowance recorded:						
Consumer Real Estate	\$ 648	\$ 648	\$ -	\$ 626	\$ 32	\$ 9
Agricultural Real Estate	-	-	-	204	-	-
Agricultural	491	491	-	124	-	-
Commercial Real Estate	299	299	-	238	19	-
Commercial and Industrial	982	982	-	637	66	-
Consumer	-	-	-	-	-	-
With a specific allowance recorded:						
Consumer Real Estate	181	184	30	211	-	-
Agricultural Real Estate	-	-	-	22	1	-
Agricultural	200	200	21	29	-	-
Commercial Real Estate	-	-	-	-	-	-
Commercial and Industrial	227	377	142	555	-	-
Consumer	33	33	4	3	-	-
Totals:						
Consumer Real Estate	<u>\$ 829</u>	<u>\$ 832</u>	<u>\$ 30</u>	<u>\$ 837</u>	<u>\$ 32</u>	<u>\$ 9</u>
Agricultural Real Estate	<u>\$ -</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ 226</u>	<u>\$ 1</u>	<u>\$ -</u>
Agricultural	<u>\$ 691</u>	<u>\$ 691</u>	<u>\$ 21</u>	<u>\$ 153</u>	<u>\$ -</u>	<u>\$ -</u>
Commercial Real Estate	<u>\$ 299</u>	<u>\$ 299</u>	<u>\$ -</u>	<u>\$ 238</u>	<u>\$ 19</u>	<u>\$ -</u>
Commercial and Industrial	<u>\$ 1,209</u>	<u>\$ 1,359</u>	<u>\$ 142</u>	<u>\$ 1,192</u>	<u>\$ 66</u>	<u>\$ -</u>
Consumer	<u>\$ 33</u>	<u>\$ 33</u>	<u>\$ 4</u>	<u>\$ 3</u>	<u>\$ -</u>	<u>\$ -</u>

(In Thousands)

Three Months Ended September 30, 2019

	Recorded Investment	Unpaid Principal Balance	Related Allowance	QTD Average Recorded Investment	QTD Interest Income Recognized	QTD Interest Income Recognized Cash Basis
With no related allowance recorded:						
Consumer Real Estate	\$ 626	\$ 626	\$ -	\$ 628	\$ 9	\$ 3
Agricultural Real Estate	406	406	-	406	-	-
Agricultural	368	368	-	368	-	-
Commercial Real Estate	304	304	-	267	7	-
Commercial and Industrial	210	210	-	219	3	-
Consumer	-	-	-	-	-	-
With a specific allowance recorded:						
Consumer Real Estate	126	128	22	172	-	-
Agricultural Real Estate	-	-	-	-	-	-
Agricultural	-	-	-	-	-	-
Commercial Real Estate	-	-	-	-	14	-
Commercial and Industrial	1,188	1,188	165	1,081	-	-
Consumer	-	-	-	-	-	-
Totals:						
Consumer Real Estate	\$ 752	\$ 754	\$ 22	\$ 800	\$ 9	\$ 3
Agricultural Real Estate	\$ 406	\$ 406	\$ -	\$ 406	\$ -	\$ -
Agricultural	\$ 368	\$ 368	\$ -	\$ 368	\$ -	\$ -
Commercial Real Estate	\$ 304	\$ 304	\$ -	\$ 267	\$ 21	\$ -
Commercial and Industrial	\$ 1,398	\$ 1,398	\$ 165	\$ 1,300	\$ 3	\$ -
Consumer	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -

ITEM 1 NOTES TO CONDENSED CONSOLIDATED UNAUDITED FINANCIAL STATEMENTS (Continued)
NOTE 4 LOANS (Continued)

(In Thousands)

Nine Months Ended September 30, 2020

	Recorded Investment	Unpaid Principal Balance	Related Allowance	YTD Average Recorded Investment	YTD Interest Income Recognized	YTD Interest Income Recognized Cash Basis
With no related allowance recorded:						
Consumer Real Estate	\$ 780	\$ 780	\$ -	\$ 688	\$ 120	\$ 9
Agricultural Real Estate	1,589	1,589	-	451	6	-
Agricultural	533	533	-	367	9	1
Commercial Real Estate	186	186	-	199	3	-
Commercial and Industrial	2,021	2,021	-	819	18	-
Consumer	25	25	-	21	37	-
With a specific allowance recorded:						
Consumer Real Estate	205	205	43	60	10	-
Agricultural Real Estate	5,425	5,425	432	2,475	7	-
Agricultural	188	188	28	208	6	-
Commercial Real Estate	3,033	3,033	44	2,389	-	-
Commercial and Industrial	1,274	1,274	651	929	10	-
Consumer	-	-	-	7	-	-
Totals:						
Consumer Real Estate	\$ 985	\$ 985	\$ 43	\$ 748	\$ 130	\$ 9
Agricultural Real Estate	\$ 7,014	\$ 7,014	\$ 432	\$ 2,926	\$ 13	\$ -
Agricultural	\$ 721	\$ 721	\$ 28	\$ 575	\$ 15	\$ 1
Commercial Real Estate	\$ 3,219	\$ 3,219	\$ 44	\$ 2,588	\$ 3	\$ -
Commercial and Industrial	\$ 3,295	\$ 3,295	\$ 651	\$ 1,748	\$ 28	\$ -
Consumer	\$ 25	\$ 25	\$ -	\$ 28	\$ 37	\$ -

(In Thousands)						
Nine Months Ended September 30, 2019	Recorded Investment	Unpaid Principal Balance	Related Allowance	YTD Average Recorded Investment	YTD Interest Income Recognized	YTD Interest Income Recognized Cash Basis
With no related allowance recorded:						
Consumer Real Estate	\$ 626	\$ 626	\$ -	\$ 625	\$ 24	\$ 7
Agricultural Real Estate	406	406	-	135	-	-
Agricultural	368	368	-	123	-	-
Commercial Real Estate	304	304	-	217	14	-
Commercial and Industrial	210	210	-	697	9	-
Consumer	-	-	-	-	-	-
With a specific allowance recorded:						
Consumer Real Estate	126	128	22	220	-	-
Agricultural Real Estate	-	-	-	-	-	-
Agricultural	-	-	-	24	-	-
Commercial Real Estate	-	-	-	-	-	-
Commercial and Industrial	1,188	1,188	165	451	37	-
Consumer	-	-	-	-	-	-
Totals:						
Consumer Real Estate	<u>\$ 752</u>	<u>\$ 754</u>	<u>\$ 22</u>	<u>\$ 845</u>	<u>\$ 24</u>	<u>\$ 7</u>
Agricultural Real Estate	<u>\$ 406</u>	<u>\$ 406</u>	<u>\$ -</u>	<u>\$ 135</u>	<u>\$ -</u>	<u>\$ -</u>
Agricultural	<u>\$ 368</u>	<u>\$ 368</u>	<u>\$ -</u>	<u>\$ 147</u>	<u>\$ -</u>	<u>\$ -</u>
Commercial Real Estate	<u>\$ 304</u>	<u>\$ 304</u>	<u>\$ -</u>	<u>\$ 217</u>	<u>\$ 14</u>	<u>\$ -</u>
Commercial and Industrial	<u>\$ 1,398</u>	<u>\$ 1,398</u>	<u>\$ 165</u>	<u>\$ 1,148</u>	<u>\$ 46</u>	<u>\$ -</u>
Consumer	<u>\$ -</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ -</u>

As of September 30, 2020, the Company had \$71 thousand foreclosed residential real estate property obtained by physical possession and \$849 thousand of consumer mortgage loans secured by residential real estate properties for which foreclosure proceedings are in process according to local jurisdictions. As of September 30, 2019, the Company had \$187 thousand of foreclosed residential real estate property obtained by physical possession and \$379 thousand of consumer mortgage loans secured by residential real estate properties for which foreclosure proceedings were in process according to local jurisdictions.

The Allowance for Loan and Lease Losses (ALLL) has a direct impact on the provision expense. An increase in the ALLL is funded through recoveries and provision expense. The following tables summarize the activities in the allowance for credit losses.

	(In Thousands)	
	Nine Months Ended September 30, 2020	Twelve Months Ended December 31, 2019
Allowance for Loan & Lease Losses		
Balance at beginning of year	\$ 7,228	\$ 6,775
Provision for loan loss	4,986	1,138
Loans charged off	(480)	(841)
Recoveries	149	156
Allowance for Loan & Lease Losses	<u>\$ 11,883</u>	<u>\$ 7,228</u>
Allowance for Unfunded Loan Commitments & Letters of Credit	<u>\$ 633</u>	<u>\$ 479</u>
Total Allowance for Credit Losses	<u>\$ 12,516</u>	<u>\$ 7,707</u>

The Company segregates its ALLL into two reserves: The ALLL and the Allowance for Unfunded Loan Commitments and Letters of Credit (AULC). When combined, these reserves constitute the total Allowance for Credit Losses (ACL).

The ALLL does not include an accretible yield of \$1.7 million and \$2.0 million as September 30, 2020 and December 31, 2019 related to the acquisition of Bank of Geneva as previously discussed in Note 2.

The AULC is reported within other liabilities on the balance sheet while the ALLL is netted within the loans, net asset line. The ACL presented above represents the full amount of reserves available to absorb possible credit losses.

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The following table breaks down the activity within ACL for each loan portfolio classification and shows the contribution provided by both the recoveries and the provision along with the reduction of the allowance caused by charge-offs.

Additional analysis, presented in thousands, related to the allowance for credit losses for the three and nine months ended September 30, 2020 and September 30, 2019 in addition to the ending balances as of December 31, 2019 is as follows:

	Consumer Real Estate	Agricultural Real Estate	Agricultural	Commercial Real Estate	Commercial and Industrial	Consumer	Unfunded Loan Commitment & Letters of Credit	Unallocated	Total
Three Months Ended September 30, 2020 ALLOWANCE FOR CREDIT LOSSES:									
Beginning balance	\$ 570	\$ 813	\$ 1,036	\$ 4,458	\$ 2,423	\$ 561	\$ 605	\$ 72	\$ 10,538
Charge Offs	-	-	-	-	-	(79)	-	-	(79)
Recoveries	2	-	-	2	10	28	-	-	42
Provision (Credit)	(42)	(51)	(367)	1,275	839	94	-	239	1,987
Other Non-interest expense related to unfunded	-	-	-	-	-	-	28	-	28
Ending Balance	\$ 530	\$ 762	\$ 669	\$ 5,735	\$ 3,272	\$ 604	\$ 633	\$ 311	\$ 12,516
Ending balance: individually evaluated for impairment	\$ 43	\$ 432	\$ 28	\$ 44	\$ 651	\$ -	\$ -	\$ -	\$ 1,198
Ending balance: collectively evaluated for impairment	\$ 487	\$ 330	\$ 641	\$ 5,691	\$ 2,621	\$ 604	\$ 633	\$ 311	\$ 11,318
Ending balance: loans acquired with deteriorated credit quality	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -
FINANCING RECEIVABLES:									
Ending balance	\$ 175,595	\$ 192,577	\$ 103,476	\$ 593,936	\$ 244,823	\$ 53,455	\$ -	\$ -	\$ 1,363,862
Ending balance: individually evaluated for impairment	\$ 985	\$ 7,014	\$ 721	\$ 3,219	\$ 3,295	\$ 25	\$ -	\$ -	\$ 15,259
Ending balance: collectively evaluated for impairment	\$ 174,567	\$ 185,563	\$ 102,755	\$ 590,717	\$ 241,528	\$ 53,339	\$ -	\$ -	\$ 1,348,469
Ending balance: loans acquired with deteriorated credit quality	\$ 43	\$ -	\$ -	\$ -	\$ -	\$ 91	\$ -	\$ -	\$ 134

ITEM 1 NOTES TO CONDENSED CONSOLIDATED UNAUDITED FINANCIAL STATEMENTS (Continued)
 NOTE 4 LOANS (Continued)

December 31, 2019	Consumer Real Estate	Agricultural Real Estate	Agricultural	Commercial Real Estate	Commercial and Industrial	Consumer	Unfunded Loan Commitment & Letters of Credit	Unallocated	Total
ALLOWANCE FOR CREDIT LOSSES:									
Ending Balance	\$ 311	\$ 314	\$ 691	\$ 3,634	\$ 1,727	\$ 551	\$ 479	\$ -	\$ 7,707
Ending balance: individually evaluated for impairment	\$ 30	\$ -	\$ 21	\$ -	\$ 142	\$ 4	\$ -	\$ -	\$ 197
Ending balance: collectively evaluated for impairment	\$ 281	\$ 314	\$ 670	\$ 3,634	\$ 1,585	\$ 547	\$ 479	\$ -	\$ 7,510
Ending balance: loans acquired with deteriorated credit quality	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -
FINANCING RECEIVABLES:									
Ending balance	\$ 164,691	\$ 198,859	\$ 111,949	\$ 550,082	\$ 144,009	\$ 49,409	\$ -	\$ -	\$ 1,218,999
Ending balance: individually evaluated for impairment	\$ 829	\$ -	\$ 691	\$ 299	\$ 1,209	\$ 33	\$ -	\$ -	\$ 3,061
Ending balance: collectively evaluated for impairment	\$ 163,816	\$ 198,859	\$ 111,258	\$ 549,783	\$ 142,694	\$ 49,376	\$ -	\$ -	\$ 1,215,786
Ending balance: loans acquired with deteriorated credit quality	\$ 46	\$ -	\$ -	\$ -	\$ 106	\$ -	\$ -	\$ -	\$ 152

ITEM 1 NOTES TO CONDENSED CONSOLIDATED UNAUDITED FINANCIAL STATEMENTS (Continued)
NOTE 4 LOANS (Continued)

	Consumer Real Estate	Agricultural Real Estate	Agricultural	Commercial Real Estate	Commercial and Industrial	Consumer	Unfunded Loan Commitment & Letters of Credit	Unallocated	Total
Three Months Ended September 30, 2019									
ALLOWANCE FOR CREDIT LOSSES:									
Beginning balance	\$ 275	\$ 340	\$ 756	\$ 3,320	\$ 1,461	\$ 526	\$ 370	\$ 5	\$ 7,053
Charge Offs	(39)	-	(22)	-	(55)	(103)	-	-	(219)
Recoveries	-	-	1	2	13	32	-	-	48
Provision (Credit)	38	12	(2)	(17)	131	90	-	(5)	247
Other Non-interest expense related to unfunded	-	-	-	-	-	-	60	-	60
Ending Balance	\$ 274	\$ 352	\$ 733	\$ 3,305	\$ 1,550	\$ 545	\$ 430	\$ -	\$ 7,189
Ending balance: individually evaluated for impairment	\$ 22	\$ -	\$ -	\$ -	\$ 165	\$ -	\$ -	\$ -	\$ 187
Ending balance: collectively evaluated for impairment	\$ 252	\$ 352	\$ 733	\$ 3,305	\$ 1,385	\$ 545	\$ 430	\$ -	\$ 7,002
Ending balance: loans acquired with deteriorated credit quality	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -
FINANCING RECEIVABLES:									
Ending balance	\$ 158,458	\$ 200,625	\$ 110,405	\$ 501,095	\$ 138,395	\$ 49,718	\$ -	\$ -	\$ 1,158,696
Ending balance: individually evaluated for impairment	\$ 752	\$ 406	\$ 368	\$ 304	\$ 1,398	\$ -	\$ -	\$ -	\$ 3,228
Ending balance: collectively evaluated for impairment	\$ 157,659	\$ 200,219	\$ 110,037	\$ 500,791	\$ 136,997	\$ 49,718	\$ -	\$ -	\$ 1,155,421
Ending balance: loans acquired with deteriorated credit quality	\$ 47	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ 47

ITEM 1 NOTES TO CONDENSED CONSOLIDATED UNAUDITED FINANCIAL STATEMENTS (Continued)
NOTE 4 LOANS (Continued)

	Consumer Real Estate	Agricultural Real Estate	Agricultural	Commercial Real Estate	Commercial and Industrial	Consumer	Unfunded Loan Commitment & Letters of Credit	Unallocated	Total
Nine Months Ended September 30, 2020									
ALLOWANCE FOR CREDIT LOSSES:									
Beginning balance	\$ 311	\$ 314	\$ 691	\$ 3,634	\$ 1,727	\$ 551	\$ 479	\$ -	\$ 7,707
Charge Offs	(35)	-	-	(8)	(165)	(272)	-	-	(480)
Recoveries	7	-	-	7	19	116	-	-	149
Provision (Credit)	247	448	(22)	2,102	1,691	209	-	311	4,986
Other Non-interest expense related to unfunded	-	-	-	-	-	-	154	-	154
Ending Balance	\$ 530	\$ 762	\$ 669	\$ 5,735	\$ 3,272	\$ 604	\$ 633	\$ 311	\$ 12,516
Ending balance: individually evaluated for impairment	\$ 43	\$ 432	\$ 28	\$ 44	\$ 651	\$ -	\$ -	\$ -	\$ 1,198
Ending balance: collectively evaluated for impairment	\$ 487	\$ 330	\$ 641	\$ 5,691	\$ 2,621	\$ 604	\$ 633	\$ 311	\$ 11,318
Ending balance: loans acquired with deteriorated credit quality	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -
FINANCING RECEIVABLES:									
Ending balance	\$ 175,595	\$ 192,577	\$ 103,476	\$ 593,936	\$ 244,823	\$ 53,455	\$ -	\$ -	\$ 1,363,862
Ending balance: individually evaluated for impairment	\$ 985	\$ 7,014	\$ 721	\$ 3,219	\$ 3,295	\$ 25	\$ -	\$ -	\$ 15,259
Ending balance: collectively evaluated for impairment	\$ 174,567	\$ 185,563	\$ 102,755	\$ 590,717	\$ 241,528	\$ 53,339	\$ -	\$ -	\$ 1,348,469
Ending balance: loans acquired with deteriorated credit quality	\$ 43	\$ -	\$ -	\$ -	\$ -	\$ 91	\$ -	\$ -	\$ 134

ITEM 1 NOTES TO CONDENSED CONSOLIDATED UNAUDITED FINANCIAL STATEMENTS (Continued)
NOTE 4 LOANS (Continued)

	Consumer Real Estate	Agricultural Real Estate	Agricultural	Commercial Real Estate	Commercial and Industrial	Consumer	Unfunded Loan Commitment & Letters of Credit	Unallocated	Total
Nine Months Ended September 30, 2019									
ALLOWANCE FOR CREDIT LOSSES:									
Beginning balance	\$ 247	\$ 250	\$ 768	\$ 3,217	\$ 1,305	\$ 484	\$ 274	\$ 504	\$ 7,049
Charge Offs	(95)	-	(22)	-	(55)	(382)	-	-	(554)
Recoveries	-	-	3	7	21	97	-	-	128
Provision (Credit)	122	102	(16)	81	279	346	-	(504)	410
Other Non-interest expense related to unfunded	-	-	-	-	-	-	156	-	156
Ending Balance	\$ 274	\$ 352	\$ 733	\$ 3,305	\$ 1,550	\$ 545	\$ 430	\$ -	\$ 7,189
Ending balance: individually evaluated for impairment	\$ 22	\$ -	\$ -	\$ -	\$ 165	\$ -	\$ -	\$ -	\$ 187
Ending balance: collectively evaluated for impairment	\$ 252	\$ 352	\$ 733	\$ 3,305	\$ 1,385	\$ 545	\$ 430	\$ -	\$ 7,002
Ending balance: loans acquired with deteriorated credit quality	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -
FINANCING RECEIVABLES:									
Ending balance	\$ 158,458	\$ 200,625	\$ 110,405	\$ 501,095	\$ 138,395	\$ 49,718	\$ -	\$ -	\$ 1,158,696
Ending balance: individually evaluated for impairment	\$ 752	\$ 406	\$ 368	\$ 304	\$ 1,398	\$ -	\$ -	\$ -	\$ 3,228
Ending balance: collectively evaluated for impairment	\$ 157,659	\$ 200,219	\$ 110,037	\$ 500,791	\$ 136,997	\$ 49,718	\$ -	\$ -	\$ 1,155,421
Ending balance: loans acquired with deteriorated credit quality	\$ 47	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ 47

NOTE 5 EARNINGS PER SHARE

Basic earnings per share are calculated using the two-class method. The two-class method is an earnings allocation formula under which earnings per share is calculated from common stock and participating securities according to dividends declared and participation rights in undistributed earnings. Under this method, all earnings distributed and undistributed, are allocated to participating securities and common shares based on their respective rights to receive dividends. Unvested share-based payment awards that contain non-forfeitable rights to dividends are considered participating securities (i.e. unvested restricted stock), not subject to performance based measures. Basic earnings per share is calculated by dividing net income available to common shareholders by the weighted average number of common shares outstanding. Application of the two-class method for participating securities results in a more dilutive basic earnings per share as the participating securities are allocated the same amount of income as if they are outstanding for purposes of basic earnings per share. There is no additional potential dilution in calculating diluted earnings per share, therefore basic and diluted earnings per share are the same amounts. Other than the restricted stock plan, the Company has no other employee stock based compensation plans.

The Compensation Committee of the Company has determined that it is appropriate to award shares of the common stock of the Company to Outside Directors and Employees that are officers of the Company or the Bank who also serve as Directors of the Company and the Bank as a portion of their retainer for services rendered as Directors of the Company and the Bank. The Committee believes that it is appropriate to award the Directors Shares equal to approximately \$4,000, rounded to the nearest whole Share on an annual basis commencing on June 5, 2020 and thereafter on the first Friday of June in each year. The value for the Shares to be based upon the closing price for Shares on June 4, 2020 and thereafter on the first Thursday in June in each year. On June 5, 2020, each Director received 176 shares. The use of stock for Directors' retainer, does not have an effect on diluted earnings per share as it is immediately vested.

	(in thousands of dollars)		(in thousands of dollars)	
	Three Months Ended		Nine Months Ended	
	September 30, 2020	September 30, 2019	September 30, 2020	September 30, 2019
Earnings per share				
Net income	\$ 4,410	\$ 4,275	\$ 13,319	\$ 13,679
Less: distributed earnings allocated to participating securities	(15)	(14)	(41)	(37)
Less: undistributed earnings allocated to participating securities	(19)	(18)	(59)	(63)
Net earnings available to common shareholders	<u>\$ 4,376</u>	<u>\$ 4,243</u>	<u>\$ 13,219</u>	<u>\$ 13,579</u>
Weighted average common shares outstanding including participating securities	11,142,797	11,121,426	11,135,695	11,105,993
Less: average unvested restricted shares	(83,257)	(79,335)	(83,445)	(81,569)
Weighted average common shares outstanding	<u>11,059,540</u>	<u>11,042,091</u>	<u>11,052,250</u>	<u>11,024,424</u>
Basic and diluted earnings per share	<u>\$ 0.40</u>	<u>\$ 0.38</u>	<u>\$ 1.20</u>	<u>\$ 1.23</u>

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NOTE 6 FAIR VALUE OF FINANCIAL INSTRUMENTS

Fair values of financial instruments are management's estimate of the values at which the instruments could be exchanged in a transaction between willing parties. These estimates are subjective and may vary significantly from amounts that would be realized in actual transactions. In addition, other significant assets are not considered financial assets including deferred tax assets, premises, equipment and intangibles. Further, the tax ramifications related to the realization of the unrealized gains and losses can have a significant effect on the fair value estimates and have not been considered in any of the estimates.

The following assumptions and methods were used in estimating the fair value for financial instruments:

Cash and Cash Equivalents

The carrying amounts reported in the balance sheet for cash, cash equivalents and federal funds sold approximate their fair values. Also included in this line item are the carrying amounts of interest-bearing deposits maturing within ninety days which approximate their fair values. Fair values of other interest-bearing deposits are estimated using discounted cash flow analyses based on current rates for similar types of deposits.

Interest Bearing Time Deposits

Fair values for fixed-rate certificates of deposit are estimated using a discounted cash flow analysis that applies interest rates currently being offered on certificates to a schedule of aggregated expected monthly maturities on time deposits.

Securities – Available-for-sale

Fair values for securities, excluding Federal Home Loan Bank stock are based on quoted market price, where available. If quoted market prices are not available, fair values are based on quoted market prices of comparable instruments.

Other Securities

The carrying value of Federal Home Loan Bank stock of Cincinnati and Indianapolis, approximates fair value based on the redemption provisions of the respective Federal Home Loan Bank.

Loans Held for Sale

The carrying amount approximates fair value due to insignificant amount of time between origination and date of sale.

Loans, net

The fair values of the loans are estimated using a credit mark adjustment along with discounted cash flow analysis, using interest rates currently being offered for loans with similar terms to borrowers with similar credit quality. The credit mark adjustment was estimated using merger and acquisition analysis of nationwide bank and thrift deals and/or the Bank's most recent acquisition experience.

Deposits

The fair values disclosed for deposits with no defined maturities are equal to their carrying amounts, which represent the amount payable on demand. The carrying amounts for variable-rate, fixed term money market accounts and certificates of deposit approximate their fair value at the reporting date. Fair value for fixed-rate certificates of deposit are estimated using a discounted cash flow analysis that applies interest rates currently being offered on certificates to a schedule of aggregated expected monthly maturities on time deposits.

Federal Funds Purchased and Securities Sold Under Agreements to Repurchase

The carrying value of federal funds purchased and securities sold under agreements to repurchase approximates fair values.

FHLB Advances

Fair values of FHLB advances are estimated using discounted cash flow analysis based on the Company's current incremental borrowing rates for similar types or borrowing arrangements.

Accrued Interest Receivable and Payable

The carrying amounts of accrued interest approximate their fair values.

Off Balance Sheet Financial Instruments

Fair values for off-balance sheet, credit related financial instruments are based on fees currently charged to enter into similar agreements, taking into account the remaining terms of the agreements and the counter-parties' credit standing.

The estimated fair values, and related carrying or notional amounts, for on and off-balance sheet financial instruments as of September 30, 2020 and December 31, 2019 are reflected below.

	(In Thousands)				
	September 30, 2020				
	Carrying Amount	Fair Value	Level 1	Level 2	Level 3
Financial Assets:					
Cash and cash equivalents	\$ 87,753	\$ 87,753	\$ 87,753	\$ -	\$ -
Interest-bearing time deposits	4,657	4,718	-	4,718	-
Securities - available-for-sale	259,041	259,041	3,004	254,452	1,585
Other securities	5,827	5,827	-	-	5,827
Loans held for sale	7,621	7,621	-	-	7,621
Loans, net	1,351,979	1,324,451	-	-	1,324,451
Interest receivable	6,879	6,879	-	-	6,879
Financial Liabilities:					
Interest bearing deposits	\$ 926,851	\$ 926,899	\$ -	\$ -	\$ 926,899
Non-interest bearing deposits	330,845	330,845	-	330,845	-
Time deposits	261,177	264,052	-	-	264,052
Total Deposits	1,518,873	1,521,796	-	330,845	1,190,951
Federal funds purchased and securities sold under agreement to repurchase	29,859	29,859	-	-	29,859
Federal Home Loan Bank advances	17,724	17,737	-	-	17,737
Interest payable	558	558	-	-	558

	(In Thousands)				
	December 31, 2019				
	Carrying Amount	Fair Value	Level 1	Level 2	Level 3
Financial Assets:					
Cash and cash equivalents	\$ 51,296	\$ 51,296	\$ 51,296	\$ -	\$ -
Interest-bearing time deposits	4,309	4,331	-	4,331	-
Securities - available-for-sale	222,293	222,293	10,021	210,782	1,490
Other securities	5,810	5,810	-	-	5,810
Loans held for sale	4,248	4,248	-	-	4,248
Loans, net	1,211,771	1,188,014	-	-	1,188,014
Interest receivable	6,769	6,769	-	-	6,769
Financial Liabilities:					
Interest bearing deposits	\$ 746,628	\$ 746,691	\$ -	\$ -	\$ 746,691
Non-interest bearing deposits	265,156	265,156	-	265,156	-
Time deposits	276,563	277,008	-	-	277,008
Total Deposits	1,288,347	1,288,855	-	265,156	1,023,699
Federal funds purchased and securities sold under agreement to repurchase	48,073	48,073	-	-	48,073
Federal Home Loan Bank advances	24,806	24,811	-	-	24,811
Interest payable	754	754	-	-	754

Fair Value Measurements

In general, fair values determined by Level 1 inputs use quoted prices in active markets for identical assets or liabilities in active markets that the Company has the ability to access.

Available-for-sale securities, when quoted prices are available in an active market, securities are valued using the quoted price and are classified as Level 1.

Fair values determined by Level 2 inputs use other inputs that are observable, either directly or indirectly. These Level 2 inputs include quoted prices for similar assets and liabilities in active markets, and other inputs such as interest rates and yield curves that are observable at commonly quoted intervals.

Available-for-sale securities classified as Level 2 are valued using the prices obtained from an independent pricing service. The prices are not adjusted. Securities of obligations of state and political subdivisions are valued using a type of matrix, or grid, pricing in which securities are benchmarked against the treasury rate based on credit rating. Substantially all assumptions used by the independent pricing service are observable in the marketplace, can be derived from observable data, or are supported by observable levels at which transactions are executed in the marketplace.

Level 3 inputs are unobservable inputs, including inputs that are available in situations where there is little, if any, market activity for the related asset or liability. The Bank holds some local municipals that the Bank evaluates based on the credit strength of the underlying project. The fair value is determined by valuing similar credit payment streams at similar rates.

In instances where inputs used to measure fair value fall into different levels in the above fair value hierarchy, fair value measurements in their entirety are categorized based on the lowest level input that is significant to the valuation. The Company's assessment of the significance of particular inputs to these fair value measurements requires judgment and considers factors specific to each asset.

The following summarizes financial assets measured at fair value on a recurring basis as of September 30, 2020 and December 31, 2019, segregated by level or the valuation inputs within the fair value hierarchy utilized to measure fair value:

Assets and Liabilities Measured at Fair Value on a Recurring Basis (In Thousands)			
	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
September 30, 2020			
Assets - (Securities Available-for-Sale)			
U.S. Treasury	\$ 3,004	\$ -	\$ -
U.S. Government agencies	-	90,062	-
Mortgage-backed securities	-	102,980	-
State and local governments	-	61,410	1,585
Total Securities Available-for-Sale	<u>\$ 3,004</u>	<u>\$ 254,452</u>	<u>\$ 1,585</u>
December 31, 2019			
Assets - (Securities Available-for-Sale)			
U.S. Treasury	\$ 10,021	\$ -	\$ -
U.S. Government agencies	-	62,445	-
Mortgage-backed securities	-	95,197	-
State and local governments	-	53,140	1,490
Total Securities Available-for-Sale	<u>\$ 10,021</u>	<u>\$ 210,782</u>	<u>\$ 1,490</u>

The following tables represent the changes in the Level 3 fair-value category of which unobservable inputs are relied upon as of the three and nine month periods ended September 30, 2020 and September 30, 2019.

(In Thousands)			
Fair Value Measurements Using Significant Unobservable Inputs (Level 3)			
	State and Local Governments Tax-Exempt	State and Local Governments Taxable	State and Local Governments Total
Balance at July 1, 2020	\$ -	\$ 1,550	\$ 1,550
Change in Market Value	-	35	35
Payments & Maturities	-	-	-
Balance at September 30, 2020	<u>\$ -</u>	<u>\$ 1,585</u>	<u>\$ 1,585</u>

	(In Thousands)		
	Fair Value Measurements Using Significant		
	Unobservable Inputs (Level 3)		
	State and Local Governments Tax-Exempt	State and Local Governments Taxable	State and Local Governments Total
Balance at January 1, 2020	\$ -	\$ 1,490	\$ 1,490
Change in Market Value	-	95	95
Payments & Maturities	-	-	-
Balance at September 30, 2020	\$ -	\$ 1,585	\$ 1,585

	(In Thousands)		
	Fair Value Measurements Using Significant		
	Unobservable Inputs (Level 3)		
	State and Local Governments Tax-Exempt	State and Local Governments Taxable	State and Local Governments Total
Balance at July 1, 2019	\$ -	\$ 1,505	\$ 1,505
Change in Market Value	-	4	4
Payments & Maturities	-	-	-
Balance at September 30, 2019	\$ -	\$ 1,509	\$ 1,509

	(In Thousands)		
	Fair Value Measurements Using Significant		
	Unobservable Inputs (Level 3)		
	State and Local Governments Tax-Exempt	State and Local Governments Taxable	State and Local Governments Total
Balance at January 1, 2019	\$ -	\$ 1,427	\$ 1,427
Change in Market Value	-	82	82
Payments & Maturities	-	-	-
Balance at September 30, 2019	\$ -	\$ 1,509	\$ 1,509

Most of the Company's available-for-sale securities, including any bonds issued by local municipalities, have CUSIP numbers or have similar characteristics of those in the municipal markets, making them marketable and comparable as Level 2.

The Company also has assets that, under certain conditions, are subject to measurement at fair value on a non-recurring basis. At September 30, 2020 and December 31, 2019, such assets consist primarily of collateral dependent impaired loans. Collateral dependent impaired loans categorized as Level 3 assets consist of non-homogeneous loans that are considered impaired. The Company estimates the fair value of the loans based on the present value of expected future cash flows using management's best estimate of key assumptions. These assumptions include future payment ability, timing of payment streams, and estimated realizable values of available collateral (typically based on outside appraisals.)

At September 30, 2020 and December 31, 2019, fair value of collateral dependent impaired loans categorized as Level 3 was \$8.1 million and \$444 thousand, respectively. The specific allocation for impaired loans was \$1.2 million and \$197 thousand as of September 30, 2020 and December 31, 2019, respectively, which are accounted for in the allowance for loan losses (see Note 4).

Other real estate is reported at either the lower of the fair value of the real estate minus the estimated costs to sell the asset or the cost of the asset. The determination of fair value of the real estate relies primarily on appraisals from third parties. If the fair value of the real estate, minus the estimated costs to sell the asset, is less than the asset's cost, the deficiency is recognized as a valuation allowance against the asset through a charge to expense. The valuation allowance is therefore increased or decreased, through charges or credits to expense, for changes in the asset's fair value or estimated selling costs.

The following table presents quantitative information about unobservable inputs used in recurring and nonrecurring Level 3 fair value measurements:

	(In Thousands) Fair Value at September 30, 2020	Valuation Technique	Unobservable Inputs	Range (Weighted Average)
State and local government	\$ 1,585	Discounted Cash Flow	Credit strength of underlying project or entity / Discount rate	0-5% (1.07%)
Collateral dependent impaired loans	8,144	Collateral based measurements	Discount to reflect current market conditions and ultimate collectability	0-50% (5.99%)
Other real estate owned - commercial	-	Appraisals	Discount to reflect current market	— % (—)

	(In Thousands) Fair Value at December 31, 2019	Valuation Technique	Unobservable Inputs	Range (Weighted Average)
State and local government	\$ 1,490	Discounted Cash Flow	Credit strength of underlying project or entity / Discount rate	0-5% (2.52%)
Collateral dependent impaired loans	444	Collateral based measurements	Discount to reflect current market conditions and ultimate collectability	0-50% (30.73%)
Other real estate owned - commercial	164	Appraisals	Discount to reflect current market	0-20% (23.31%)

The following table presents impaired loans and other real estate owned as recorded at fair value on September 30, 2020 and December 31, 2019:

	Assets Measured at Fair Value on a Nonrecurring Basis at September 30, 2020			
	(In Thousands)			
	Balance at September 30, 2020	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
Collateral dependent impaired loans	\$ 8,144	\$ -	\$ -	\$ 8,144
Other real estate owned - commercial	-	-	-	-

	Assets Measured at Fair Value on a Nonrecurring Basis at December 31, 2019			
	(In Thousands)			
	Balance at December 31, 2019	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
Collateral dependent impaired loans	\$ 444	\$ -	\$ -	\$ 444
Other real estate owned - commercial	164	-	-	164

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NOTE 7 FEDERAL FUNDS PURCHASED AND SECURITIES SOLD UNDER AGREEMENTS TO REPURCHASE

The Company had no Federal Funds purchased as of September 30, 2020 and \$17.8 million as of December 31, 2019, respectively. During the same time periods, the Company also had \$29.9 million and \$30.2 million in securities sold under agreement to repurchase.

September 30, 2020					
Remaining Contractual Maturity of the Agreements (In Thousands)					
	Overnight & Continuous	Up to 30 days	30-90 days	Greater Than 90 days	Total
Federal funds purchased	\$ -	\$ -	\$ -	\$ -	\$ -
Repurchase agreements					
US Treasury & agency securities	1,540	-	-	28,319	29,859
	<u>\$ 1,540</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ 28,319</u>	<u>\$ 29,859</u>

December 31, 2019					
Remaining Contractual Maturity of the Agreements (In Thousands)					
	Overnight & Continuous	Up to 30 days	30-90 days	Greater Than 90 days	Total
Federal funds purchased	\$ 17,843	\$ -	\$ -	\$ -	\$ 17,843
Repurchase agreements					
US Treasury & agency securities	1,814	-	3,965	24,451	30,230
	<u>\$ 19,657</u>	<u>\$ -</u>	<u>\$ 3,965</u>	<u>\$ 24,451</u>	<u>\$ 48,073</u>

NOTE 8 RECENT ACCOUNTING PRONOUNCEMENTS

In June 2016, the Financial Accounting Standards Board (“FASB”) issued Accounting Standards Update (“ASU”) No. 2016-13 “*Financial Instruments - Credit Losses (Topic 326): Measurement of Credit Losses on Financial Instruments.*” This ASU requires the measurement of all expected credit losses for financial assets held at the reporting date based on historical experience, current conditions, and reasonable and supportable forecasts. Financial institutions and other organizations will now use forward-looking information to better inform their credit loss estimates. Many of the loss estimation techniques applied today will still be permitted, although the inputs to those techniques will change to reflect the full amount of expected credit losses. Organizations will continue to use judgment to determine which loss estimation method is appropriate for their circumstances. The ASU requires enhanced disclosures to help investors and other financial statement users better understand significant estimates and judgments used in estimating credit losses, as well as the credit quality and underwriting standards of an organization’s portfolio. These disclosures include qualitative and quantitative requirements that provide additional information about the amounts recorded in the financial statements. In addition, the ASU amends the accounting for credit losses on available-for-sale debt securities and purchased financial assets with credit deterioration.

The ASU is effective for SEC filers for fiscal years, and interim periods within those fiscal years, beginning after December 15, 2019 (i.e., January 1, 2020, for calendar year entities). FASB recently approved a delay in adoption for Smaller Reporting Companies. The Company has completed an analysis to determine that it qualifies as a Smaller Reporting Company. As such, adoption can be postponed until periods beginning after December 15, 2022 (i.e., January 1, 2023, for calendar year entities). Early application will be permitted for all organizations for fiscal years, and interim periods within those fiscal years, beginning after December 15, 2018.

The Company has contracted with an external advisor and has formed a committee to determine the methodology to be used. Most importantly, the Company is gathering as much data as possible to enable management to review scenarios and determine which calculations will produce the most reliable results. The Company began working with the third-party service provider to review parallel reports starting in June 2019. The Company will not adopt ASU 2016-13 in calendar year 2020 and management is currently evaluating when or if they would elect to early adopt ASU 2016-13.

In January 2017, the FASB issued ASU No. 2017-04 “*Intangibles – Goodwill and other (Topic 350) – Simplifying the Test for Goodwill Impairment.*” These amendments eliminate Step 2 from the goodwill impairment test. The amendments also eliminate the requirements for any reporting unit with a zero or negative carrying amount to perform a qualitative assessment and, if it fails that qualitative test, to perform Step 2 of the goodwill impairment test. An entity still has the option to perform the qualitative assessment for a reporting unit to determine if the quantitative impairment test is necessary. The guidance is effective for annual or any interim goodwill impairment tests in fiscal years beginning after December 15, 2019. Early adoption was permitted for interim or annual goodwill impairment tests performed on testing dates after January 1, 2017. ASU 2017-04 should be adopted on a prospective basis. The Company has adopted ASU 2017-04 effective January 1, 2020, as required, and does not expect the ASU to have a material impact on its financial statements. Goodwill testing is scheduled to be completed during the fourth quarter.

In August 2018, the FASB issued ASU No. 2018-13 “*Fair Value Measurement (Topic 820) - Disclosure Framework-Changes to the Disclosure Requirements for Fair Value Measurement.*” ASU 2018-13 modifies the disclosure requirements on fair value measurements in Topic 820. The amendments in this update remove disclosures that no longer are considered cost beneficial, modify/clarify the specific requirements of certain disclosures, and add disclosure requirements identified as relevant. ASU 2018-13 is effective for years beginning after December 15, 2019, with early adoption permitted. The Company adopted ASU 2018-13 effective January 1, 2020, as required, without material effect on its accounting disclosures.

In March 2020, in connection with the implementation of the CARES Act and related provisions, we have elected the temporary relief in the CARES Act not to apply the guidance in ASC 310-40 on accounting for troubled debt restructurings (TDRs) to loan modifications related to COVID-19 made between March 1, 2020 and the earlier of (1) December 31, 2020 or (2) 60 days after the end of the COVID-19 national emergency. The relief was only applied to modifications for borrowers that were not more than 30 days past due as of December 31, 2019. As of September 30, 2020, there were no loan modifications that would have been previously treated as TDRs under the guidance in ASC 310-40.

OVERVIEW

2020 started out to be the year of execution. After a good beginning in terms of loan growth and initiatives the first two months, March brought the year of unprecedented change. The Federal Reserve decreased its overnight rate by fifty basis points on March 3rd. As we were adjusting to that change, they again decreased the rate on March 15th by a before unseen 100 basis points. We began to see the disruption caused by COVID-19 and the focus of the Bank quickly changed. Execution took on a new meaning related to following the actions governed by the Bank's pandemic flu plan. The Bank took immediate measures to protect its customers and employees from risk of spread while continuing to provide financial services. Investigating solutions was our focus for the second quarter and will be for as long as it takes. **Please see section titled COVID-19 for additional information related to actions taken.**

During the third quarter, the Bank continued to grow, as loans increased by 17.71% or \$205.2 million over September 30, 2019 and 11.88% or \$144.9 million over December 31, 2019. Loan balances as of September 30, 2020 include approximately \$87 million in forgivable Paycheck Protection Program (PPP) loans made under the CARES Act. In comparison for the same time periods, deposits grew 18.85% or \$240.8 million over September 30, 2019 and 17.89% or \$230.5 million over December 31, 2019. Home loan activity continued to be robust, due to the refinance activity associated with interest rate reductions. The activity is expected to continue into fourth quarter as our home loan applications continue to grow. Deposit growth correlated to a flight to safety as the stock market experienced great volatility in addition to the depositing of funds from the PPP loans.

The growing season in our market area was variable with some areas receiving timely rains and others needing moisture. It is believed yields will be average when looking at our market area. Grain markets have increased thus giving producers an opportunity to lock in better prices. The profit potential appears better than believed earlier in the year. Fluctuations in markets and challenges in production are part of the inherent risk of agriculture that our producers have become used to managing. COVID-19 challenges seem to be decreasing. The agriculture portfolio remains healthy and concerns are manageable.

Row crop production accounts for the largest percentage of our agriculture portfolio. We remain very positive about the long term outlook of this sector. Our customers mitigate risk through the purchasing of crop insurance. F&M's exposure to customers that do not carry crop insurance is less than 5% of the total exposure in this sector of agriculture. The livestock sector, which equates to 25% of the agricultural portfolio, has 70% exposure to supportive roles and does not have direct ownership of the livestock. The Bank has limited exposure to any one producer and many loans are secured with buildings as collateral.

During the third quarter, most of the commercial sector in the Bank's markets returned to work in an increased capacity. Business volumes and profitability have returned for many commercial loan clients, but still lag for those industries most impacted by COVID-19. The current rate environment continues to drive acquisition and construction activity. These projects have seen some delays due to the higher restrictions in the second quarter. With these restrictions lessened in the third quarter, projects are moving forward and leases are being executed.

Loan Production Offices (LPO) in Muncie, Indiana, Oxford, Ohio and West Bloomfield, Michigan all have new loan activity and are helping extend the F&M footprint. The Bank was able to hire well known talented bankers from each area. The Bank is completing a new full-service office in Fort Wayne, Indiana which will open in the fourth quarter.

During the second quarter, the Bank accelerated investments in our digital infrastructure to support our employee's ability to work from home and to make it easier for our customers to engage with the Bank electronically. Due to retirement, the Bank also hired Shalini Singhal as our new Chief Information Officer. Shalini is a proven CIO who will lead our digital efforts.

The Company remains well capitalized and prepared to face the new challenges coming our way in 2020. Our history shows we weathered the 2008-2009 financial crisis and recession. We did so without taking Troubled Asset Relief Program (TARP) funds and our performance over the time frame was significantly higher than our peers. It is the character of the communities we serve that contributed to that success. It is not just what is done during the storm but how well prepared for the storm you are. F&M has prepared well with historically low troubled loans the last few years due to having strong credit quality controls in place. Additional loan loss provision was taken in the first three quarters in view of the unknown length and breadth of the declining economic situation and its potential effect on our loan portfolio.

F&M will continue to focus on serving our shareholders, communities, and customers while protecting our employees. Please see below for what we have accomplished so far in 2020 and our response to and impact of COVID-19.

COVID-19: What the Company knows and what steps have been taken

Shareholders

Dividend declaration

The Company expects to continue to maintain the payment of its quarterly dividend consistent with its past practices. We are sensitive to the needs of our long-time shareholders that utilize these funds to supplement their living expenses, especially in this low interest rate environment. Dividends declared during the quarter at \$0.17 per share increased by 6.25% over first and second quarters \$0.16 per share.

Annual Meeting

The Company held its Annual Meeting on April 16th; however, in light of the governmental restrictions the meeting was significantly different than in the past. There was no dinner, no presentation of 2019 or an outlook for 2020 and only a small group of directors and officers present. For the three items to be considered at the meeting, shareholders were asked to seriously consider not attending and vote by proxy. Over 80% of the shareholders voted by proxy.

Communities

Offices

With the health of our employees and customers being our top concern, as of March 20th, the Bank temporarily suspended branch lobby hours to the public for walk-in transactions. Appointments could be made at branches to complete all needed paperwork and transactions. Drive-thru services remained open as well as all ATM's and ITM's to complete needed transactions. To assure branches remained open, employees were divided into teams who rotated every three days to two weeks as a means to practice social distancing while limiting any possible exposure. During the month of May, the retail re-open team developed an employee handbook which focused on opening protocols, employee training, health and wellness and facility signage. Branch re-openings began on June 3rd with the last branches re-opening on June 15th. We continue to monitor and adjust lobby access as needed. Internal controls have not been significantly modified due to COVID-19.

Small Business

As a Small Business Administration (SBA) approved provider, the Bank was able to immediately participate in the SBA PPP established under the CARES Act, which was signed into law on March 27, 2020. The PPP provided much needed assistance to businesses in our communities. The Bank has been able to present applications for around 947 small businesses which provided approximately \$87 million in needed funding. Loan size varied from \$300 to \$2.3 million with only 2 loans over \$2 million. Net fee income from PPP loans to be recognized over 24 months will be \$3.2 million. The Bank began to take applications for PPP loan forgiveness in the third quarter.

Consumers

Home Loan

With the Federal Reserve rate drops of 150 basis points in March (100 basis points of which was directly related to the effects of the virus on the economy), a surge in home loan activity has occurred. Much of the activity is refinance related and the Bank has experienced the highest amount of applications in its history, both in number of and dollar amount. Given the nature of the programs, the results were recorded in the second and third quarters. The Bank sells most of its home loans into the secondary market through Freddie Mac.

Existing loans on our books for which the Bank has received inquiries into forbearance agreements, totaled over 100 as of September 30th. Of these inquiries, 95 customers entered into agreements totaling just under \$8.9 million. 30 loans were in-house making up \$2.2 million in principal balance and 65 were secondary market loans which we service with balances totaling \$6.7 million. Of the 30 in-house loans, 4 loans are in a repayment plan, 1 loan is in the payment deferral process and 3 loans are in forbearance as of September 30th. Of the 65 secondary market loans, 13 loans are in a repayment plan and 3 loans are in forbearance as of September 30th. Some inquiries were only for possible future requests. We remain ready to assist our customers through this difficult time in the best manner possible.

Retail Loans

The Bank is offering its “Skip-a-pay” program to consumers with installment loans, which allows the customer to skip the payment and extend the maturity of the contract for the payment period. We are allowing two payments to be skipped upon request with an additional one possible at the end of the initial request upon review. Normally, the Bank would charge a fee for this program – the fee has been waived. The Bank would also normally require the interest for the period to be collected and that requirement is currently waived. Interest is a part of the extended maturity payments. We have assisted 141 customers currently with loan balances totaling \$1.9 million. 129 of those customers have returned the extension documents representing approximately \$1.8 million and 247 extended months.

Waiving of late payment fees for our customers was introduced on March 16, 2020 and ceased on June 30, 2020. As of June 30th, the Bank had foregone fees of \$307 thousand on loans to help our customers. Of the \$307 thousand, \$131 thousand was related to two past due commercial loans. As a community bank, it is by definition what we should do.

Depositors

The Bank’s most popular checking account, which includes requirements to earn a reward, removed the requirement of debit card transactions to be completed during a cycle for the months of April and May. In the Bank’s geographical area, the states issued “stay at home” guidelines and many of our customers were concerned with being able to complete the requirement. This impacted almost 11.6 thousand accounts and represented just under \$101 million in average account balances. The product includes the option of attaching a savings account for which the same requirements were waived and impacted an additional almost 7 thousand accounts and \$113.1 million in average account balances, calculated as of June 30th. Overall, typically 80-85% of our customers meet all the requirements. The waiving of the debit card transactions allowed those customers to receive the reward and possibly an additional 77.5% of the previous non-qualifiers which represented the other 15-20% in total. With the removal of the “stay at home” guidelines, the debit card transaction requirement was reinstated beginning with the June cycle on May 29th. During the months of April and May, most individuals still met their debit card transaction requirement with the “stay at home” order in place. As of end of September, our customers are meeting the same percentage of qualifications as pre-COVID levels.

Employees

The Bank continued paying employees their full pay through March 31st. During this time period, accumulated PTO and vacation time were frozen and not required to be used to receive full pay. The Bank continues to promote social distancing by encouraging employees who can work remotely to do so and in other cases, departments have been dispersed to keep the team separated. As of April 1st, the Bank is following The Families First Coronavirus Response Act (FFCRA) which requires employers to provide their employees with paid sick leave and extended family and medical leave for specified reasons related to COVID-19. These provisions are in effect until December 31, 2020. Qualifying reasons for leave related to COVID-19 include the employee: (1) being subject to a quarantine order, (2) being advised by a healthcare provider to self-quarantine, (3) experiencing COVID-19 symptoms and is seeking a medical diagnosis, (4) caring for an individual subject to a quarantine order, (5) caring for his or her child whose school or place of care is closed or (6) experiencing any other substantially-similar condition specified by the U.S. Department of Health and Human Services. All time off related to the above reasons is being separately documented within our time and attendance system. The Bank will be able to reduce its employer tax for up to two weeks (80 hours, or a part-time employee’s two-week equivalent).

Financial – Exposures

Given the timing of the outbreak in the United States of the COVID-19 pandemic, management believes that the main impact on the Company’s first three quarters performance was a factor in the economic qualitative adjustment for the calculation of the allowance for loan loss. Subsequently the loan loss provision was increased which also included an increase due to loan growth. The COVID-19 pandemic represents an unprecedented challenge to the global economy in general and the financial services sector in particular. However, there is still significant uncertainty regarding the overall length of the pandemic and the aggregate impact that it will have on global and regional economies, including uncertainties regarding the potential positive effects of governmental actions taken in response to the pandemic during the remainder of 2020. With so much uncertainty, it is impossible for the Bank to accurately predict the impact that the pandemic will have on the Company’s primary markets and the overall extent to which it will affect the Company’s financial condition and results of operations during the remainder of the current fiscal year. At a minimum, the actions taken by the Company to assist its customers experiencing challenges from the pandemic, such as through the Bank’s “Skip-a-pay” program, the waiver of late payment fees, and the entry into loan forbearance agreements, did have an impact on the Company’s 2020 performance. Nonetheless, management believes that the Company’s current regulatory capital position is adequate to face the coming challenges.

The Company has a limited exposure to many sectors of the economy that will likely be impacted for an extended period such as the travel, restaurant, hospitality, energy and retail industries. The Bank does not have any direct exposure to the energy industry and hotels, entertainment and food related businesses are less than 10% of our overall loan portfolio as shown in the chart which follows. In addition, the Bank's hotel customers are financially strong business owners, operating brand name hotels in compelling locations. The Bank, along with many other financial institutions, has increased its provision for loan losses in the current year compared to 2019 by approximately \$4.6 million. The Bank is fully prepared to make additional provisions as warranted by the COVID-19 situation.

The Bank initially had loans of \$28 million in deferment and loans of \$137 million making interest only payments. As of September 30th, there is a total of \$8.5 million outstanding between deferrals and interest only payments within our commercial and agricultural portfolios. The \$8.5 million is comprised of \$1.4 million with one full month of deferment, \$641 thousand with three full months of deferment, \$5.5 million with three month interest only and \$900 thousand with six months interest only. At this point in time, existing loans outstanding in deferral or interest only payments are expected to be current as of December 31st.

Industry Segments (Dollars in Thousands)	Outstanding Loan Balance	Percent of Total Loan Portfolio	Payment Deferment	Percent of Total Loans Adjusted with Deferment	Interest Only Modifications	Percent of Total Loans Adjusted with Interest Only
Hospitality (Hotels)	\$ 74,426	5.44%	\$ -	0.00%	\$ 1,679	26.19%
Restaurants	21,726	1.59%	-	0.00%	2,000	31.20%
Retail Commercial						
Real Estate *	101,783	7.44%	-	0.00%	-	0.00%
Entertainment	24,568	1.80%	641	31.10%	1,302	20.32%
Car Dealers	32,094	2.35%	-	0.00%	-	0.00%
Gas Stations	17,586	1.29%	-	0.00%	-	0.00%
Other	770,197	56.31%	1,420	68.90%	1,429	22.29%
Total	<u>\$ 1,042,380</u>	<u>76.22%</u>	<u>\$ 2,061</u>	<u>100.00%</u>	<u>\$ 6,410</u>	<u>100.00%</u>
# of Customers			4		5	

*Includes Owner Occupied

Report on Adjusted Loans as of September 30, 2020

The other category in payment deferment as of September 30th is a loan for a livestock production facility. The other category for interest modifications as of September 30th is for construction of an agricultural implement facility and a manufacturer.

The restaurant portfolio, which represents 1.6% of the Bank's total loan portfolio, is 60% full-service restaurants with the remaining 40% quick-service restaurants. Of the \$87 million PPP loans originated, only \$6.1 million were to restaurants.

Entertainment loans, which total \$24.6 million or 1.8% of the Bank's total loan portfolio, has \$641 thousand on payment deferrals as of September 30th. The Bank has nearly 100 entertainment loans with an average loan amount of \$230 thousand. There is a diverse group of businesses that comprise this sector and have performed well throughout the pandemic. Businesses include sports, athletic and fitness facilities, camping and campgrounds, fireworks and pet kennels. Loans for sports and athletics total \$14.9 million while loans for campgrounds total \$2.7 million.

Our credit administration is closely monitoring and analyzing these higher risk segments within the loan portfolio, tracking loan payment deferrals, customer liquidity and providing timely reports to senior management and the board of directors. The Bank is in frequent contact with our borrowers during this time of uncertainty and has had only one COVID-19 related downgrade which was less than \$10 million. The Bank has stress tested our top five commercial concentrations which include retail commercial real estate, hotels, multi-family, industrial commercial real estate and assisted living. An outside third party has reviewed 55% of our commercial portfolio along with our internal credit department having recently reviewed 75% of our loan portfolio as a result of new money, renewals or annual reviews. Based on the Company's capital levels, prudent underwriting policies, loan concentration diversification and our geographic footprint, we expect to be able to manage the economic risks and uncertainties associated with the pandemic and remain adequately capitalized.

NATURE OF ACTIVITIES

Farmers & Merchants Bancorp, Inc. (the “Company”) is a financial holding company incorporated under the laws of Ohio in 1985. Our subsidiaries are The Farmers & Merchants State Bank (the “Bank”), a community bank operating in Northwest Ohio since 1897, and Farmers & Merchants Risk Management, Inc., a captive insurance company formed in December 2014 and located in Nevada. We report our financial condition and net income on a consolidated basis and we have only one segment.

Our executive offices are located at 307 North Defiance Street, Archbold, Ohio 43502, and our telephone number is (419) 446-2501. The Bank operates thirty full service banking offices throughout Northwest Ohio and Northeast Indiana.

On January 1, 2019, six offices of Bank of Geneva, located in the Indiana counties of Adams, Allen and Jay, were merged with and into The Farmers & Merchants State Bank. The Bank has continued its expansion strategy and the new offices have provided new growth opportunities.

The Farmers & Merchants State Bank engages in general commercial banking and savings business including commercial, agricultural and residential mortgage, consumer and credit card lending activities. The largest segment of the lending business relates to commercial, both real estate and non-real estate. The type of commercial business ranges from small business to multi-million dollar companies. The loans are a reflection of business located within the Banks’ market area. Because the Bank’s offices are located in Northwest Ohio and Northeast Indiana, a substantial amount of the loan portfolio is comprised of loans made to customers in the farming industry for such items as farm land, farm equipment, livestock and operating loans for seed, fertilizer, and feed. Other types of lending activities include loans for home improvements, and loans for the purchase of autos, trucks, recreational vehicles, motorcycles, and other consumer goods.

The Bank also provides checking account services, as well as savings and time deposit services such as certificates of deposits. In addition, Automated Teller Machines (ATMs) or Interactive Teller Machines (ITMs) are provided at most branch locations along with other independent locations in the market area. ITMs operate as an ATM with the addition of remote teller access to assist the user. The Bank has custodial services for Individual Retirement Accounts (IRAs) and Health Savings Accounts (HSAs). The Bank provides on-line banking access for consumer and business customers. For consumers, this includes bill-pay, on-line statement opportunities and mobile banking. For business customers, it provides the option of electronic transaction origination such as wire and Automated Clearing House (ACH) file transmittal. In addition, the Bank offers remote deposit capture or electronic deposit processing and merchant credit card services. Mobile banking was added in 2012 and has been widely accepted and used by consumers. Over the past couple of years, the Bank has updated its consumer offerings with “Secure” and “Pure” checking in 2014 and with KASASA Cash Back in 2015. During the second quarter 2017, new business checking products were announced and existing business accounts were converted to one of three new products, Business Essential, Edge or Elite. The new products provided customers with new options to bundle services and for the Bank to utilize the full relationship to determine pricing. This was the next step of implementation for the Bank’s “earn to free” strategic initiative. During second quarter 2019, “Smart 25” checking and Business Money Market savings products were launched. Upgrades to our digital products and services continue to occur in both retail and business lines. During the fourth quarter of 2020, new checking products will be rolled out which will replace KASASA.

The Bank has established underwriting policies and procedures which facilitate operating in a safe and sound manner in accordance with supervisory and regulatory guidance. Within this sphere of safety and soundness, the Bank’s practice has been to not promote innovative, unproven credit products which may not be in the best interest of the Bank or its customers. The Bank does offer a hybrid mortgage loan. Hybrid loans are loans that start out as a fixed rate mortgage but after a set number of years automatically adjust to an adjustable rate mortgage. The Bank offers a three year fixed rate mortgage after which the interest rate will adjust annually. The majority of the Bank’s adjustable rate mortgages are of this type. In order to offer longer term fixed rate mortgages, the Bank does participate in the Freddie Mac, Farmer Mac and Small Business Lending programs. The Bank also normally retains the servicing rights on these partially or 100% sold loans. In order for the customer to participate in these programs they must meet the requirements established by those agencies. In addition, the Bank does sell some of its longer term fixed rate agricultural mortgages into the secondary market with the aid of a broker.

The Bank does not have a program to fund sub-prime loans. Sub-prime loans are characterized as a lending program or strategy that targets borrowers who pose a significantly higher risk of default than traditional retail banking customers.

All loan requests are reviewed as to credit worthiness and are subject to the Bank’s underwriting guidelines as to secured versus unsecured credit. Secured loans are in turn subject to loan to value (LTV) requirements based on collateral types as set forth in the Bank’s Loan Policy and described more thoroughly below on the basis of general loan type. In addition, credit scores of those seeking consumer credit are reviewed and if they do not meet the Bank’s Loan Policy guidelines an additional officer approval is required.

Consumer Loans:

- Maximum loan to value (LTV) for cars, trucks and light trucks vary from 90% to 110% depending on whether direct or indirect.
- Loans above 100% are generally the result of additional charges for extended warranties and/or insurance coverage for wage or death.
- Boats, campers, motorcycles, RV's and Motor Coaches range from 80%-90% based on age of vehicle.
- 1st or 2nd mortgages on 1-4 family homes range from 75%-90% with "in-house" first real estate mortgages requiring private mortgage insurance on those exceeding 80% LTV.
- Raw land LTV maximum ranges from 65%-75% depending on whether or not the property has been improved.

Commercial/Agriculture/Real Estate:

- Maximum LTVs range from 70%-80% depending on type.
- Accounts Receivable: Up to 80% LTV less retainages and greater than 90 days.
- Maximum LTV on non-traditional loan up to 85%.

Inventory:

- Agriculture:
Livestock and grain up to 80% LTV, crops (insured) up to 75% and Warehouse Receipts up to 87%.
- Commercial:
Maximum LTV of 50% on raw and finished goods.
- Floor plan:
 - New/used vehicles to 100% of wholesale.
 - New/Used recreational vehicles and manufactured homes to 80% of wholesale.

Equipment:

- New not to exceed 80% of invoice, used NTE 50% of listed book or 75% of appraised value.
- Restaurant equipment up to 35% of market value.
- Heavy trucks, titled trailers up to NTE 75% LTV and aircraft up to 75% of appraised value.

F&M Investment Services, the brokerage department of the Bank, opened for business in April 1999. Securities are offered through Raymond James Financial Services, Inc.

In December of 2014, the Company became a financial holding company within the meaning of the Bank Holding Company Act of 1956 as amended (the "Act"), in order to provide the flexibility to take advantage of the expanded powers available to a financial holding company under the Act. Our subsidiary bank is in turn regulated and examined by the Ohio Division of Financial Institutions and the Federal Deposit Insurance Corporation. The activities of our bank subsidiary are also subject to other federal and state laws and regulations. The Company also formed a captive insurance company (the "captive") in December 2014 which is located in Nevada and regulated by the State of Nevada Division of Insurance.

The Bank's primary market includes communities located in the Ohio counties of Defiance, Fulton, Hancock, Henry, Lucas, Williams, Wood and in the Indiana counties of Adams, Allen, DeKalb, Jay and Steuben. In our banking activities, we compete directly with other commercial banks, credit unions, farm credit services, and savings and loan institutions in each of our operating localities. In a number of our locations, we compete against entities which are much larger than us. The primary factors in competing for loans and deposits are the rates charged as well as location and quality of the services provided.

At September 30, 2020, we had 374 full time equivalent employees. The employees are not represented by a collective bargaining unit. We provide our employees with a comprehensive benefit program, some of which is contributory. We consider our employee relations to be good.

RECENT REGULATORY DEVELOPMENTS

The Bank remains attentive to the current regulatory environment in light of the regulatory agencies' risk-based approach to examinations. Regulatory changes and the complexity of new and amended rules have resulted in challenges and uncertainties which could pose an increased risk of noncompliance. Various significant mortgage rules require monitoring by means of testing, validation of results, additional training, and further research or consultation to assist with ongoing compliance.

The global spread of the Coronavirus (COVID-19) and resulting declaration of a world-wide pandemic have impacted the financial services industry and banking operations in the United States (US) and world-wide. The financial services sector is

identified as a Critical Infrastructure Sector by the Department of Homeland Security during the COVID-19 response efforts. How basic business operations can be conducted has undergone a rapid and dramatic change. At the same time continuity of business operations involves promoting safety and security of customers and employees, providing a quality customer experience, and maintaining effective delivery systems and channels of communication. Regulatory guidance has been issued to manage and mitigate the unprecedented impact of the COVID-19 pandemic on business operations. Regulatory agencies promote prudent and practical efforts to assist customers and communities during this national emergency. Such assistance to alleviate the financial impact on affected customers can involve modification of loan terms for existing borrowers, waiver of certain fees and charges, providing small dollar loans, and offering forbearance and payment deferrals on mortgage loan obligations due to financial hardship. Legislation enacted in March 2020 has provided the Families First Coronavirus Response Act (FFCRA) and CARES Act. The FFCRA which is effective through December 31, 2020, provides for a paid leave for employees (of employers with fewer than 500 employees) who must quarantine due to the coronavirus, are caring for a sick family member, or caring for a child out of school. It significantly expands existing protections currently available to employees who take leave to care for a sick family member. The CARES Act, among other matters, resulted in expansion of SBA Lending Programs; provided for a financial election to suspend GAAP principles and regulatory determinations for COVID-19 related loan modifications that would otherwise be deemed Trouble Debt Restructuring; gave the FDIC authority to establish a temporary Debt Guarantee Program for bank liabilities; delayed Current Expected Credit Losses (CECL) compliance; reduced the Community Bank Leverage Ratio to 8% to eliminate risk-based capital compliance for banks under \$10 billion; required credit furnishers that agree to deferred loan payments, forbearance on a delinquent account, or any other relief during the national emergency to report accounts as current to Credit Reporting Agencies; and defined forbearance requirements and terms for single family and multi-family loans backed by federal government agencies or government sponsored entities due to COVID-19 financial hardship. Of immediate and significant importance has been the rollout of the SBA Paycheck Protection Program (PPP). The PPP authorized lending of up to \$350 billion in 100% guaranteed 7(a) loans to cover payroll costs, interest on mortgage payments, rent obligations, and utilities. The PPP provides a guaranteed loan for which a portion of the loan up to or equal to 8 weeks of covered payroll and specific operating expenses can be forgiven. The maximum loan size is capped at the lesser of 250% of the average monthly payroll costs or \$10 million.

In April, legislation known as the Paycheck Protection Program and Health Care Enhancement Act provided additional funding to replenish and supplement key programs under the CARES Act. Included in this legislation was the extension of the PPP with an additional \$320 billion in funding. At least \$60 billion of this funding was to be set aside for small and midsize banks and community lenders. Since April, the SBA has issued various Interim Final Rules to supplement and clarify matters involving the PPP. The Paycheck Protection Program Flexibility Act of 2020 (PPPFA) was enacted in early June 2020. This provided more flexibility to Borrowers regarding use of PPP loan funds. Certain provisions were retroactive to the date of the CARES Act and all PPP loans. Among these provisions were the extension of the covered period of the loan, extension of the forgiveness period, deferral of payments based on the loan forgiveness period, reduction in the minimum that must be spent for payroll costs, extended date by which employees must be rehired, and removal of restrictions on payroll tax deferral. The term for subsequent PPO loans made after enactment of the PPPFA was extended to five years from two. A primary focus is now directed to aiding PPP borrowers in navigating the loan forgiveness process. Further legislation and regulatory guidance may result depending on the duration of the COVID-19 spread and subsequent economic impact to customers, communities, businesses, and industry sectors.

With regard to all regulatory matters, the Bank remains committed in making good faith efforts to comply with technical requirements of the laws, rules, regulations, and guidance from both federal and state agencies which govern its activities.

CRITICAL ACCOUNTING POLICIES AND ESTIMATES

The Company's consolidated financial statements are prepared in accordance with accounting principles generally accepted in the United States of America, and the Company follows general practices within the financial services industry in which it operates. At times the application of these principles requires management to make assumptions, estimates and judgments that affect the amounts reported in the financial statements and accompanying notes.

These assumptions, estimates and judgments are based on information available as of the date of the financial statements. As this information changes, the financial statements could reflect different assumptions, estimates and judgments. Certain policies inherently have a greater reliance on assumptions, estimates and judgments and as such have a greater possibility of producing results that could be materially different than originally reported. Examples of critical assumptions, estimates and judgments are when assets and liabilities are required to be recorded at fair value, when a decline in the value of an asset not required to be recorded at fair value warrants an impairment write-down or valuation reserve to be established, or when an asset or liability must be recorded contingent upon a future event. These policies, along with the disclosures presented in the notes to the condensed consolidated financial statements and in the management discussion and analysis of the financial condition and results of operations, provide information on how significant assets and liabilities are valued and how those

values are determined for the financial statements. Based on the valuation techniques used and the sensitivity of financial statement amounts to assumptions, estimates, and judgments underlying those amounts, management has identified the determination of the ALLL, the valuation of its Mortgage Servicing Rights and the valuation of real estate acquired through or in lieu of loan foreclosures (“OREO Property”) as the accounting areas that require the most subjective or complex judgments, and as such could be the most subject to revision as new information becomes available.

OREO Property held for sale is initially recorded at fair value at the date of foreclosure. Subsequent to foreclosure, valuations are periodically performed by management and the assets are carried at the lower of cost or fair value minus estimated costs to sell.

Costs of holding foreclosed real estate are charged to expense in the current period, except for significant property improvements, which are capitalized. Valuations are periodically performed by management and a write-down is recorded by a charge to non-interest expense if the carrying value exceeds the fair value minus estimated costs to sell.

The net income from operations of foreclosed real estate held for sale is reported either in noninterest income or noninterest expense depending upon whether the property is in a gain or loss position overall. At September 30, 2020 OREO property holdings were \$206 thousand. OREO totaled \$214 thousand and \$351 thousand as of December 31, 2019 and September 30, 2019 respectively.

The ALLL and ACL represents management’s estimate of probable credit losses inherent in the Bank’s loan portfolio, unfunded loan commitments, and letters of credit at the report date. The ALLL methodology is regularly reviewed for its appropriateness and is approved annually by the Board of Directors. This written methodology is consistent with Generally Accepted Accounting Principles which provides for a consistently applied analysis.

The Bank’s methodology provides an estimate of the probable credit losses either by calculating a specific loss per credit or by applying a composite of historical factors over a relevant period of time with current internal and external factors which may affect credit collectability. Such factors which may influence estimated losses are the conditions of the local and national economy, local unemployment trends, and abilities of lending staff, valuation trends of fixed assets, and trends in credit delinquency, classified credits, and credit losses.

Inherent in most estimates is imprecision. The Bank’s ALLL may include a margin for imprecision with an unallocated portion. Bank regulatory agencies and external auditors periodically review the Bank’s methodology and adequacy of the ALLL. Any required changes in the ALLL or loan charge-offs by these agencies or auditors may have a material effect on the ALLL. For more information regarding the estimates and calculations used to establish the ALLL please see Note 4 to the consolidated financial statements provided herewith.

The Bank is also required to estimate the value of its mortgage servicing rights. The Bank’s mortgage servicing rights relating to fixed rate single-family mortgage loans that it has sold without recourse but services for others for a fee represent an asset on the Bank’s balance sheet. The valuation is completed by an independent third party.

The expected and actual rates of mortgage loan prepayments are the most significant factors driving the potential for the impairment of the value of mortgage servicing assets. Increases in mortgage loan prepayments reduce estimated future net servicing cash flows because the life of the underlying loan is reduced.

The Bank’s mortgage servicing rights relating to loans serviced for others represent an asset. This asset is initially capitalized and included in other assets on the Company's consolidated balance sheet. The mortgage servicing rights are then amortized as noninterest expense in proportion to, and over the period of the estimated future net servicing income of the underlying mortgage servicing rights. There are a number of factors, however, that can affect the ultimate value of the mortgage servicing rights to the Bank. The expected and actual rates of mortgage loan prepayments are the most significant factors driving the potential for the impairment of the value of mortgage servicing assets. Increases in mortgage loan prepayments reduce estimated future net servicing cash flows because the life of the underlying loan is reduced, meaning that the present value of the mortgage servicing rights is less than the carrying value of those rights on the Bank's balance sheet. Therefore, in an attempt to reflect an accurate expected value to the Bank of the mortgage servicing rights, the Bank receives a valuation of its mortgage servicing rights from an independent third party. The independent third party's valuation of the mortgage servicing rights is based on relevant characteristics of the Bank's loan servicing portfolio, such as loan terms, interest rates and recent national prepayment experience, as well as current national market interest rate levels, market forecasts and other economic conditions. For purposes of determining impairment, the mortgage servicing assets are stratified into like groups based on loan type, term, new versus seasoned and interest rate. Management, with the advice from its third-party valuation firm, reviewed the assumptions related to prepayment speeds, discount rates, and capitalized mortgage servicing income on a quarterly basis. Changes are reflected in the following quarter's analysis related to the mortgage servicing asset. In addition,

based upon the independent third party's valuation of the Bank's mortgage servicing rights, management then establishes a valuation allowance by each stratum, if necessary, to quantify the likely impairment of the value of the mortgage servicing rights to the Bank. The estimates of prepayment speeds and discount rates are inherently uncertain, and different estimates could have a material impact on the Bank's net income and results of operations. The valuation allowance is evaluated and adjusted quarterly by management to reflect changes in the fair value of the underlying mortgage servicing rights based on market conditions. The accuracy of these estimates and assumptions by management and its third party valuation specialist can be directly tied back to the fact that management has only been required to record minor valuation allowances through its income statement over time based upon the valuation of each stratum of servicing rights.

MATERIAL CHANGES IN FINANCIAL CONDITION, LIQUIDITY AND CAPITAL RESOURCES

In spite of the ongoing COVID-19 pandemic, the Company plans to continue in its growth mode in 2020 led by loan growth from within our newer markets. The Bank is focused on funding the loan growth with the least expensive source of deposits, sale of securities or borrowings. Growing deposits will also be a focus especially in our newer markets. The Bank offers the Insured Cash Sweep ("ICS") product accessed through the Promontory network of financial institutions which helps to reduce the amount of pledged securities. This has provided more availability for runoff of securities by the Bank if warranted to fund loan growth.

Liquidity in terms of cash and cash equivalents ended \$36.5 million higher as of September 30, 2020 than it was at yearend December 31, 2019. An increase in deposits helped to fund the \$140.2 million increase in net loans since yearend 2019. Commercial real estate, consumer real estate, commercial and industrial and consumer portfolios increased compared to December 31, 2019. The remaining two portfolios decreased compared to yearend.

In comparing to the same prior year period, the September 30, 2020 (net of deferred fees and cost) loan balances of \$1.4 billion accounted for \$205.2 million or 17.7% increase when compared to 2019's \$1.2 billion. The year over year improvement was made up of a combined increase of 99.6% in commercial and industrial related loans (comprised of 18.5% in commercial real estate loans and 81.1% in non-real estate commercial loans). PPP loans of approximately \$87.2 million are included in the non-real estate commercial portfolio. Consumer real estate loans increased by 10.8%, consumer loans by 7.5% and other loans by 10.6%. Agricultural related loans decreased 10.3% year over year (comprised of 4.0% in agricultural real estate and 6.3% in non-real estate agricultural loans). The Company credits the growth to the strong team of lenders focused on providing customers valuable localized services and thereby increasing our market share.

The chart below shows the breakdown of the loan portfolio category as of September 30, for the last three years, net of deferred fees and costs.

	(In Thousands)		
	September 30, 2020 Amount	September 30, 2019 Amount	September 30, 2018 Amount
Consumer Real Estate	\$ 175,595	\$ 158,458	\$ 82,629
Agricultural Real Estate	192,577	200,625	68,524
Agricultural	103,476	110,405	103,760
Commercial Real Estate	593,936	501,095	416,632
Commercial and Industrial	235,793	130,228	119,607
Consumer	53,455	49,718	41,541
Other	9,030	8,167	6,005
Total Loans, net	\$ 1,363,862	\$ 1,158,696	\$ 838,698

The following is a contractual maturity schedule by major category of loans excluding fair value adjustments as of September 30, 2020.

	(In Thousands)		
	Within	After One	After
	One Year	Year Within Five Years	Five Years
Consumer Real Estate	\$ 4,903	\$ 32,069	\$ 139,063
Agricultural Real Estate	7,148	5,663	180,864
Agricultural	58,767	31,897	12,665
Commercial Real Estate	39,227	310,028	246,035
Commercial and Industrial	67,085	149,522	21,623
Consumer	5,587	34,774	12,915
Other	2,250	173	6,602

While the security portfolio has been utilized to fund loan growth for the last three years, additional sources have been cultivated during 2018, 2019, and 2020. The security portfolio increased \$36.7 million in the first nine months of 2020 from yearend 2019. The amount of pledged investment securities decreased by \$1.7 million as compared to yearend and \$2.2 million as compared to September 30, 2019. Liquidity is improved with the additional option of selling unpledged investment securities if needed to fund loan growth or other initiatives. As of September 30, 2020, pledged investment securities totaled \$87.1 million. The current portfolio is in a net unrealized gain position of \$7.4 million.

For the Bank, an additional \$6.8 million is also available from the Federal Home Loan Bank based on current amounts of pledged collateral. At the present time, only 1-4 family and home equity portfolios are pledged. Additional borrowings would be available if additional portfolios (i.e. commercial real estate) were pledged.

With the exception of FHLB stocks, carried at cost, which is shown as other securities, all of the Company's security portfolio is categorized as "available-for-sale" and as such is recorded at fair value.

Management feels confident that liquidity needs for future growth can be met through additional maturities and/or sales from the security portfolio, increased deposits and additional borrowings. For short term needs, the Bank has \$148.1 million of unsecured borrowing capacity through its correspondent banks.

Overall total assets increased 13.6% since yearend 2019 and grew 16.0% since September 30, 2019. The largest growth in both periods was in the loan portfolios followed by securities. COVID-19 has not had an impact on Goodwill at this point but will be externally tested during fourth quarter 2020.

Deposits accounted for the largest growth within liabilities, up 17.9% or \$230.2 million since yearend and 18.8% or \$240.8 million over September 30, 2019 balances. As stated previously, the growth of deposits correlated to a flight to safety as the stock market experienced great volatility. Core deposits continue to drive the increase which provide the opportunity to generate additional noninterest income. This growth aided the increased liquidity position and funded the loan growth for the periods along with usage of purchased Federal Funds for daily borrowings.

Shareholders' equity increased by \$13.2 million as of the third quarter of 2020 compared to yearend 2019, as earnings exceeded dividend declarations during the nine months ended September 30, 2020. Accumulated other comprehensive income increased in unrealized gain position by \$4.8 million from December 2019 to an unrealized gain of \$5.9 million on September 30, 2020. Dividends declared increased to \$0.17 per share for third quarter 2020. Compared to September 30, 2019, shareholders' equity increased 7.0% or \$16 million. Profits were lower year-to-date September 2020 than year-to-date September 2019 by \$360 thousand.

Basel III regulatory capital requirements became effective in 2016. The Bank and Company include a capital conservation buffer as a part of the transition provision. For calendar year 2016, the applicable required capital conservation buffer percentage of 0.625% was the base above which institutions avoid limitations on distributions and certain discretionary bonus payments. For the calendar year 2017, the applicable required capital conservation buffer percentage was 1.25%. For 2018, the capital conservation buffer percentage increased to 1.875%. The total buffer requirement increased to 2.5% for calendar year 2019. As of September 30, 2020, the Company and the Bank are both positioned well above the 2019 requirement.

The Holding Company has sufficient liquidity to maintain its dividend policy without relying on the upstreaming of dividends from the Bank.

The Bank continues to be well-capitalized in accordance with Federal regulatory capital requirements as the capital ratios below show:

Tier I Leverage Ratio	9.26%
Risk Based Capital Tier I	11.04%
Total Risk Based Capital	11.90%
Stockholders' Equity/Total Assets	11.98%
Capital Conservation Buffer	3.90%

MATERIAL CHANGES IN RESULTS OF OPERATIONS

Comparison of Results of Interest Earnings and Expenses for three month periods ended September 30, 2020 and 2019

Interest Income

When comparing third quarter 2020 to third quarter 2019, average loan balances grew \$233 million with PPP loans accounting for \$87.2 million of the increase. This represented a 20.7% increase in a one-year time period. Interest income on loan balances experienced an increase of \$979 thousand as compared to the quarter ended September 30, 2019. Net fee income for the PPP loans is recognized on a straight line basis over 24 months and will be accelerated upon payoff. PPP loan income for the quarter included interest income of \$220 thousand and net fee income of \$417 thousand.

The available-for-sale securities portfolio increased in average balances by \$71.1 million when comparing to the previous year while the income decreased \$155 thousand over third quarter. Fed Funds sold and interest-bearing deposits decreased in average balances by \$29.2 million as compared to the same quarter in 2019 with decreased income of \$543 thousand for the current quarter due to much lower interest rates.

With the overall increase in the average balances of the Bank's earning assets, overall total interest income for the quarter comparisons was only higher for third quarter 2020 by 1.7% or \$281 thousand as compared to third quarter 2019. Decreases in the prime lending rate between the periods contributed to a decrease in rate yield.

Annualized yield, for the quarter ended September 30, 2020, was 4.04% as compared to 4.74% for the quarter ended September 30, 2019. The following charts demonstrate the value of increased loan balances in the balance sheet mix, as well as the impact on the changes in interest rates. The yields on tax-exempt securities and the portion of the tax-exempt IDB loans included in loans have been tax adjusted based on a 21% tax rate in the charts to follow.

	(In Thousands)		Annualized Yield/Rate	
	Quarter to Date Ended September 30, 2020		September 30,	September 30,
	Average Balance	Interest/Dividends	2020	2019
Interest Earning Assets:				
Loans	\$ 1,359,156	\$ 16,181	4.76%	5.40%
Taxable investment securities	245,274	968	1.58%	2.58%
Tax-exempt investment securities	26,032	108	2.10%	2.32%
Fed funds sold & other	83,760	36	0.17%	2.05%
Total Interest Earning Assets	\$ 1,714,222	\$ 17,293	4.04%	4.74%

Change in Interest Income Quarter to Date September 30, 2020 Compared to September 30, 2019

	(In Thousands)		
	Total Change	Change Due to Volume	Change Due to Rate
Interest Earning Assets:			
Loans	\$ 979	\$ 2,774	\$ (1,795)
Taxable investment securities	(114)	306	(420)
Tax-exempt investment securities	(41)	(34)	(7)
Fed funds sold & other	(543)	(13)	(530)
Total Interest Earning Assets	\$ 281	\$ 3,033	\$ (2,752)

Interest Expense

Offsetting the lower than expected increase in interest income for the quarter was the decrease in interest expense in 2020. Third quarter 2020 was lower by \$1.8 million or 44.8% compared to third quarter 2019. Since 2019, average interest-bearing deposit balances have increased \$163.3 million or 16.2% and the Company recognized approximately \$1.8 million less in interest expense for the most recent quarter. The prime rate has dropped 150 basis points to date in 2020. Management has adjusted deposit rates accordingly. Interest expense on FHLB borrowings was down \$26 thousand in the third quarter 2020 over the same time frame in 2019 due to borrowings taken on from the Limberlost acquisition being repaid.

Interest Bearing Liabilities:	(In Thousands)			
	Quarter to Date Ended September 30, 2020		Annualized Yield/Rate	
	Average Balance	Interest	September 30, 2020	September 30, 2019
Savings deposits	\$ 915,367	\$ 798	0.35%	1.11%
Other time deposits	258,809	1,066	1.65%	2.33%
Other borrowed money	18,920	231	4.88%	4.18%
Fed funds purchased & securities				
sold under agreement to repurchase	\$ 30,100	\$ 174	2.31%	2.78%
Total Interest Bearing Liabilities	\$ 1,223,196	\$ 2,269	0.74%	1.55%

Change in Interest Expense Quarter to Date September 30, 2020 Compared to September 30, 2019

	(In Thousands)		
	Total Change	Change Due to Volume	Change Due to Rate
Interest Bearing Liabilities:			
Savings deposits	\$ (1,246)	\$ 158	\$ (1,404)
Other time deposits	(544)	(74)	(470)
Other borrowed money	(26)	(69)	43
Fed funds purchased & securities			
sold under agreement to repurchase	(27)	7	(34)
Total Interest Bearing Liabilities	\$ (1,843)	\$ 22	\$ (1,865)

Overall, net interest spread for the third quarter 2020 was 11 basis points higher than last year. As the following chart indicates, the decline in yields on interest earning assets was less than the decline in the cost of funds when comparing to the same period a year ago.

	September 30, 2020	September 30, 2019	September 30, 2018
Interest/Dividend income/yield	4.04%	4.74%	4.52%
Interest Expense/cost	0.74%	1.55%	0.92%
Net Interest Spread	3.30%	3.19%	3.60%
Net Interest Margin	3.51%	3.60%	3.85%

Net Interest Income

Net interest income increased \$2.1 million for the third quarter 2020 over the same time frame in 2019 with the increase in interest income combined with the lower interest expense, as previously mentioned. As the new loans added in 2019 and 2020 generate more income, management expects the benefits of the Company's strategy of repositioning the balance sheet to continue to widen this margin as measured in dollars. In terms of net interest margin rate, the Bank recognizes competition for deposits may again increase and put pressure on the margin which may lead to a tightening.

Comparison of Noninterest Results of Operations - Third Quarter 2020 to Third Quarter 2019

Provision Expense

The ALLL has a direct impact on the provision expense. The increase in the ALLL is funded through recoveries and provision expense. The following tables both deal with the allowance for credit losses. The first table breaks down the activity within ALLL for each loan portfolio class and shows the contribution provided by both the recoveries and the provision along with the reduction of the allowance caused by charge-offs. The second table discloses how much of the ALLL is attributed to each class of the loan portfolio, as well as the percent that each particular class of the loan portfolio represents to the entire loan portfolio in the aggregate. The consumer loan portfolios accounted for the largest component of charge-offs and recoveries for third quarter of 2020 and 2019. The commercial real estate portfolio is currently creating a large impact on the ALLL due to the loan growth.

Total provision for loan losses was \$1.7 million higher for the third quarter 2020 as compared to the same quarter 2019. Provision for loan loss was increased due to the uncertainty related to COVID-19 and its effects on the ability of individuals, businesses and other entities to meet their financial obligations. Therefore, it is prudent to incorporate the impact of COVID-19 in the evaluation of the adequacy of Allowance for Loan and Lease Losses (ALLL). Due to the governors' prior closure of non-essential businesses in many states, including restaurants (except for carryout and delivery), hair salons, and retail establishments, the risk in those industries has increased. The restaurant and hospitality sectors have been hit especially hard. Risk in the Consumer and 1-4 Family Portfolio has increased but the full impact remains unknown. Increases to the Bank's ALLL for the third quarter of 2020, centered around current customers and businesses that are particularly vulnerable due to the stay at home order and qualitative factors, were adjusted accordingly. Management continues to monitor asset quality, making adjustments to the provision as necessary. Loan charge-offs were \$140 thousand lower in third quarter 2020 than the same quarter 2019. Recoveries were \$6 thousand lower in third quarter 2020 as compared to third quarter 2019. Combined net charge-offs were \$134 thousand lower in third quarter 2020 than the same time period 2019. Past due loans, which include no deferrals related to COVID-19, decreased \$2.2 million at September 30, 2020 as compared to September 30, 2019. The majority of the change is attributed to the decrease of past due balances in the consumer real estate, agricultural, agricultural real estate and commercial and industrial portfolios with an increase in the commercial real estate portfolio.

The following table breaks down the activity within the ALLL for each loan portfolio class and shows the contribution provided by both recoveries and the provision, along with the reduction of the allowance caused by charge-offs. The time period covered is for three months ended September 30, 2020, 2019, and 2018.

	(In Thousands)		
	Three Months Ended September 30, 2020	Three Months Ended September 30, 2019	Three Months Ended September 30, 2018
Loans, net	\$ 1,363,862	\$ 1,158,696	\$ 838,698
Daily average of outstanding loans	\$ 1,359,156	\$ 1,126,173	\$ 831,246
Allowance for Loan Losses - July 1,	\$ 9,933	\$ 6,683	\$ 6,789
Loans Charged off:			
Consumer Real Estate	-	39	29
Agriculture Real Estate	-	-	-
Agricultural	-	22	-
Commercial Real Estate	-	-	-
Commercial and Industrial	-	55	-
Consumer	79	103	94
	79	219	123
Loan Recoveries:			
Consumer Real Estate	2	-	18
Agriculture Real Estate	-	-	-
Agricultural	-	1	-
Commercial Real Estate	2	2	3
Commercial and Industrial	10	13	3
Consumer	28	32	18
	42	48	42
Net Charge Offs	37	171	81
Provision for loan loss	1,987	247	47
Acquisition provision for loan loss	-	-	-
Allowance for Loan & Lease Losses - September 30,	11,883	6,759	6,755
Allowance for Unfunded Loan Commitments & Letters of Credit - September 30,	633	430	333
Total Allowance for Credit Losses - September 30,	\$ 12,516	\$ 7,189	\$ 7,088
Ratio of net charge-offs to average Loans outstanding	0.00%	0.02%	0.01%
Ratio of the Allowance for Loan Loss to Nonperforming Loans*	151.01%	173.25%	1,399.98%

* Nonperforming loans are defined as all loans on nonaccrual, plus any loans 90 days past due not on nonaccrual.

The Bank uses the following guidelines as stated in policy to determine when to realize a charge-off of a loan, whether partial loan balance or full loan balance. The Bank is also following the guidelines established under the CARES Act. A charge down in whole or in part is realized when unsecured consumer loans, credit card credits and overdraft lines of credit reach 90 days delinquency. At 120 days delinquent, secured consumer loans are charged down to the value of the collateral, if repossession of the collateral is assured and/or in the process of repossession. Consumer mortgage loan deficiencies are charged down upon the sale of the collateral or sooner upon the recognition of collateral deficiency. Commercial and agricultural credits are charged down at 120 days delinquency, unless an established and approved work-out plan is in place or litigation of the credit will likely result in recovery of the loan balance. Upon notification of bankruptcy, unsecured debt is charged off. Additional charge-offs may be realized as further unsecured positions are recognized.

Loans classified as nonaccrual were higher as of September 30, 2020 at \$7.9 million as compared to \$3.3 million as of September 30, 2019. The agricultural real estate portfolio increased \$3.8 million while the commercial real estate, commercial and industrial and consumer real estate portfolios increased a combined \$2.2 million. The agricultural portfolio decreased by \$1.3 million as compared to September 2019.

In determining the allocation for impaired loans, the Bank applies the appraised market value of the collateral securing the asset, reduced by applying a discount for estimated costs of collateral liquidation. In some instances where the discounted market value is less than the loan amount, a specific impairment allocation is assigned, which may be reduced or eliminated by the write down of the credit's active principal outstanding balance.

For the majority of the Bank's impaired loans, including all collateral dependent loans, the Bank will apply the appraised market value methodology. However, the Bank may also utilize a measurement incorporating the present value of expected future cash flows discounted at the loan's effective rate of interest. To determine appraised market value, collateral asset values securing an impaired loan are periodically evaluated. Maximum time of re-evaluation is every 12 months for chattels and titled vehicles and every two years for real estate. In this process, third party evaluations are obtained and heavily relied upon. Until such time that updated appraisals are received, the Bank may discount the collateral value used.

The following table presents the balances for allowance for loan losses by loan type for nine months ended September 30, 2020 and September 30, 2019.

Balance at End of Period Applicable To:	(In Thousands)	% of Loan Category	(In Thousands)	% of Loan Category
	September 30, 2020		September 30, 2019	
	Amount		Amount	
Consumer Real Estate	\$ 530	12.87%	\$ 274	13.68%
Agricultural Real Estate	762	14.12%	352	17.31%
Agricultural	669	7.59%	733	9.53%
Commercial Real Estate	5,735	43.55%	3,305	43.25%
Commercial and Industrial	3,272	17.95%	1,550	11.94%
Consumer	604	3.92%	545	4.29%
Unallocated	311	0.00%	-	0.00%
Allowance for Loan & Lease Losses	11,883		6,759	
Off Balance Sheet Commitments	633		430	
Total Allowance for Credit Losses	<u>\$ 12,516</u>		<u>\$ 7,189</u>	

Noninterest Income

Noninterest income was up \$1.6 million for the third quarter 2020 over the same time frame in 2019. The Company has seen an increase in its mortgage production volume and the gain on the sale of these loans was \$1.3 million higher for the third quarter 2020 over the same period in 2019. Loan originations on loans held for sale for the third quarter 2020 were \$63.5 million with proceeds from sale at \$68.9 million for 2020 compared to 2019's third quarter activity of \$24.7 million in originations and \$24.8 million in sales. The increase in loan originations was driven by the refinance activity associated with the reduction in interest rates. The mortgages sold were both 1-4 family and agricultural real estate loans originated for sale.

Combined service fees increased by \$277 thousand as compared to third quarter 2019. Service fee income for 1-4 family and agricultural real estate loans increased by \$23 thousand, mortgage release fees increased \$45 thousand, servicing rights income increased \$334 thousand, credit card fees increased \$33 thousand and debit card income increased by \$163 thousand over the same quarter in 2019. The additional fee income was offset by a decrease in overdraft and returned check charges of \$283 thousand and service charge income of \$37 thousand.

The Bank may see an impact in some of the line items such as interchange fee income and overdraft fees going forward; however, we do see additional income being derived from home loan activity.

The impact of mortgage servicing rights, both to income and expense, is shown in the following table which reconciles the value of mortgage servicing rights. The capitalization runs through noninterest income while the amortization thereof is included in non-interest expense. For the third quarter of 2020 and 2019, mortgage servicing rights caused a net \$287 and \$91 thousand in income respectively. The higher capitalized additions for 2020 are attributed to a higher loan origination level of 1-4 families. A lower interest rate environment has helped to generate the mortgage refinance activity. For loans of 15 years and less, the value was 0.975% in the third quarter 2020 versus 1.055% in third quarter 2019. For loans over 15 years, the value was 1.109% versus 1.259% for the same periods respectively. The carrying value is well below the market value of \$3.6 million which indicates any large expense to fund the valuation allowance to be unlikely in 2020.

	Three Months (In Thousands)		Nine Months (In Thousands)	
	2020	2019	2020	2019
Beginning Balance	\$ 2,740	\$ 2,465	\$ 2,629	\$ 2,385
Capitalized Additions	583	240	1,182	500
Amortization	(296)	(149)	(784)	(329)
Ending Balance, September 30,	3,027	2,556	3,027	2,556
Valuation Allowance	-	-	-	-
Mortgage Servicing Rights net, September 30,	\$ 3,027	\$ 2,556	\$ 3,027	\$ 2,556

Noninterest Expense

For the third quarter 2020, noninterest expenses were \$1.7 million higher than for the same quarter in 2019. Salaries, wages, and employee benefits (includes normal merit increases, restricted stock expense, incentive payout and all employee benefits) increased \$1.2 million in total. This was comprised of increased salaries of \$944 thousand which includes a one-time true up of \$500 thousand to support our employees' annual incentive program and increased benefits of \$235 thousand. Furniture and equipment expenses increased \$155 thousand from the prior year primarily due to an increase in depreciation of \$54 thousand and an increase in maintenance contracts of \$94 thousand. Data processing charges only increased \$8 thousand for third quarter 2020. Building occupancy costs decreased \$72 thousand due to decreased building depreciation of \$39 thousand and decreased building repairs of \$28 thousand. Advertising decreased \$176 thousand for the quarter. Franchise taxes increased \$120 thousand over third quarter 2019 with the increase in equity due to the issuance of stock in the Bank of Geneva acquisition. FDIC assessment and other general and administrative expenses were up \$194 thousand and \$119 thousand respectfully as compared to third quarter 2019. In 2019, Small Bank Credits were applied to the FDIC assessment.

Income Taxes

Federal income tax expense was \$121 thousand higher for the third quarter 2020 compared to the same quarter in 2019. Effective tax rates were 19.29% and 17.91% for third quarter 2020 and 2019 respectively. The higher effective tax rate for third quarter 2020 equated to an increase in federal income tax expense of \$75 thousand with the remainder attributed to the increase in pre-tax income.

Net Income

Results overall, net income in the third quarter of 2020 was up \$135 thousand as compared to the same quarter last year. Third quarter 2020 included an additional \$1.7 million of loan loss provision as compared to third quarter 2019. As discussed previously, the long-term effects of COVID-19 and the ability of borrowers to make timely payments are unknown at this time. The Company has done an exceptional job of growing loans while keeping past dues low. The Company remains strong, stable, and well capitalized and has the capacity to continue to cover the increased costs of expansion.

Comparison of Results of Interest Earnings and Expenses for nine month periods ended September 30, 2020 and 2019

Interest Income

Higher loan balances created the improvement in the interest income for the first nine months of 2020 as compared to the first nine months of 2019. Interest income rose 1.7% or \$873 thousand while interest income from loans accounted for \$1.7 million of the increase. Contributing to the overall improvement was an increase in securities income of \$219 thousand offset by a decrease in income from Fed Funds sold and interest-bearing deposits of \$997 thousand over 2019. The asset yield decreased by 63 basis points to 4.30% for the first nine months of 2020 compared to the first nine months of 2019's 4.93%. The 2019 yield was favorably impacted by the \$2.0 million reversal of the estimated credit loss associated with the payoff of two purchased credit-impaired loans.

With each quarter of 2020, the loan growth has provided an offset to the overall decline in asset yield. PPP loan income for the year included interest income of \$390 thousand and net fee income of \$735 thousand. The growth factor contribution is shown in the charts which follow.

The average interest earning asset base was \$228.1 million higher in the first nine months 2020 than the first nine months of 2019, an increase of approximately 16.4%.

The yields on tax-exempt securities and the portion of the tax-exempt IDB loans included in loans have been tax adjusted based on a 21% tax rate in the charts to follow.

	(In Thousands)		Annualized Yield/Rate	
	Year to Date Ended September 30, 2020		September 30, 2020	September 30, 2019
	Average Balance	Interest/Dividends		
Interest Earning Assets:				
Loans	\$ 1,305,998	\$ 48,256	4.93%	5.58%
Taxable investment securities	208,499	3,220	2.06%	2.34%
Tax-exempt investment securities	25,564	345	2.28%	2.46%
Fed funds sold & other	75,917	209	0.37%	2.08%
Total Interest Earning Assets	\$ 1,615,978	\$ 52,030	4.30%	4.93%

Change in Interest Income Year to Date September 30, 2020 Compared to September 30, 2019

	(In Thousands)		
	Total Change	Change Due to Volume	Change Due to Rate
Interest Earning Assets:			
Loans	\$ 1,651	\$ 7,104	\$ (5,453)
Taxable investment securities	363	701	(338)
Tax-exempt investment securities	(144)	(136)	(8)
Fed funds sold & other	(997)	(4)	(993)
Total Interest Earning Assets	\$ 873	\$ 7,665	\$ (6,792)

Interest Expense

Interest expense was lower for the first nine months of 2020 compared to the first nine months of 2019. At \$8.4 million, the first nine months of 2020 was down \$2.6 million as compared to the same time period 2019 or 23.5%.

The average balance of interest-bearing liabilities was higher by \$148.7 million in 2020 than the first nine months of 2019. Interest bearing deposits increased \$148.6 million while Fed Funds purchased and securities sold under agreement to repurchase increased by a combined \$3.5 million. The higher balance coupled with the slight variation of the balance sheet mix, resulted in a 47 basis points decrease in the cost of funds at 0.95% for the first nine months of 2020 as compared to 2019's 1.42%.

The change chart below shows the decreased cost was driven more by rate than volume.

	(In Thousands)		Annualized Yield/Rate	
	Year to Date Ended September 30, 2020		September 30, 2020	September 30, 2019
	Average Balance	Interest		
Interest Bearing Liabilities:				
Savings deposits	\$ 849,748	\$ 3,237	0.51%	1.05%
Other time deposits	268,762	3,782	1.88%	2.05%
Other borrowed money	22,401	754	4.49%	4.20%
Fed funds purchased & securities sold under agreement to repurchase	33,118	605	2.44%	2.37%
Total Interest Bearing Liabilities	\$ 1,174,029	\$ 8,378	0.95%	1.42%

Change in Interest Expense Year to Date September 30, 2020 Compared to September 30, 2019

	(In Thousands)		
	Total Change	Change Due to Volume	Change Due to Rate
Interest Bearing Liabilities:			
Savings deposits	\$ (2,340)	\$ 539	\$ (2,879)
Other time deposits	(247)	101	(348)
Other borrowed money	(59)	(115)	56
Fed funds purchased & securities sold under agreement to repurchase	78	63	15
Total Interest Bearing Liabilities	<u>\$ (2,568)</u>	<u>\$ 588</u>	<u>\$ (3,156)</u>

Net Interest Income

Overall, net interest spread figures for the first nine months of 2020 were down from 2019 by 16 basis points and down 23 basis points from 2018. Net interest margin for the first nine months of 2020 was lower than the same periods of 2019 and 2018. As the chart below illustrates, lower yields on loan and investment income were only partially offset by lower interest expense resulting in total net interest margin down 27 basis points since the first nine months of 2019 and under the first nine months of 2018 by 19 basis points.

	September 30, 2020	September 30, 2019	September 30, 2018
Interest/Dividend income/yield	4.30%	4.93%	4.41%
Interest Expense/cost	0.95%	1.42%	0.83%
Net Interest Spread	<u>3.35%</u>	<u>3.51%</u>	<u>3.58%</u>
Net Interest Margin	<u>3.61%</u>	<u>3.88%</u>	<u>3.80%</u>

Net interest income was up \$3.4 million in the first nine months of 2020 over the same time frame in 2019 due to the increase in loan income and lower interest expense as previously mentioned. As the new loans added in 2019 and 2020 generate more income, management expects the benefits of the Company's strategy of repositioning the balance sheet to continue to widen this margin as measured in dollars. In terms of net interest margin rate, the Bank recognizes competition for deposits may again increase and put pressure on the margin which may lead to a tightening.

Comparison of Results of Noninterest Earnings and Expenses for nine month periods ended September 30, 2020 and 2019

Provision Expense

Total provision for loan losses was \$4.6 million higher for the first nine months 2020 than for the first nine months 2019 attributable primarily to the uncertainties associated with COVID-19 and its effects on the ability of individuals, businesses and other entities to meet their financial obligations. Therefore, it is prudent to incorporate the impact of COVID-19 in the evaluation of the adequacy of Allowance for Loan and Lease Losses (ALLL). Due to the governors' prior closure of non-essential businesses in many states, including restaurants (except for carryout and delivery), hair salons, and retail establishments, the risk in those industries has increased. The restaurant and hospitality sectors have been hit especially hard. Risk in the Consumer and 1-4 Family Portfolio has increased but the full impact remains unknown. Increases to the Bank's ALLL for the first nine months of 2020, centered around current customers and businesses that are particularly vulnerable due to the stay at home order and qualitative factors, were adjusted accordingly. Management continues to monitor asset quality, making adjustments to the provision as necessary. Loan charge-offs were \$74 thousand lower in the first nine months of 2020 compared to the same period 2019. Recoveries were \$21 thousand higher in the first nine months of 2020 as compared to first nine months of 2019. Combined net charge-offs were \$95 thousand lower in the nine months ended September 2020 as compared to the same time period 2019. Management continues to evaluate the potential financial implications resulting from COVID-19 and adjusts ALLL qualitative factors as necessary.

The following table breaks down the activity within the ALLL for each loan portfolio class and shows the contribution provided by both recoveries and the provision, along with the reduction of the allowance caused by charge-offs. The time period covered is for nine months ended September 30, 2020, 2019, and 2018.

	(In Thousands)		
	Nine Months Ended September 30, 2020	Nine Months Ended September 30, 2019	Nine Months Ended September 30, 2018
Loans, net	\$ 1,363,862	\$ 1,158,696	\$ 838,698
Daily average of outstanding loans	\$ 1,305,998	\$ 1,113,892	\$ 830,118
Allowance for Loan Losses - January 1,	\$ 7,228	\$ 6,775	\$ 6,868
Loans Charged off:			
Consumer Real Estate	35	95	63
Agriculture Real Estate	-	-	-
Agricultural	-	22	-
Commercial Real Estate	8	-	15
Commercial and Industrial	165	55	100
Consumer	272	382	272
	<u>480</u>	<u>554</u>	<u>450</u>
Loan Recoveries:			
Consumer Real Estate	7	-	18
Agriculture Real Estate	-	-	-
Agricultural	-	3	6
Commercial Real Estate	7	7	7
Commercial and Industrial	19	21	8
Consumer	116	97	79
	<u>149</u>	<u>128</u>	<u>118</u>
Net Charge Offs	331	426	332
Provision for loan loss	4,986	410	219
Acquisition provision for loan loss	-	-	-
Allowance for Loan & Lease Losses - September 30,	11,883	6,759	6,755
Allowance for Unfunded Loan Commitments & Letters of Credit - September 30,	633	430	333
Total Allowance for Credit Losses - September 30,	\$ 12,516	\$ 7,189	\$ 7,088
Ratio of net charge-offs to average Loans outstanding	<u>0.03%</u>	<u>0.04%</u>	<u>0.04%</u>
Ratio of the Allowance for Loan Loss to Nonperforming Loans*	<u>151.01%</u>	<u>173.25%</u>	<u>1,399.98%</u>

* Nonperforming loans are defined as all loans on nonaccrual, plus any loans 90 days past due not on nonaccrual.

In comparing past due balances of loans 30+ days, September 30, 2020 balances were \$324 thousand as compared to September 30, 2019 balances of \$2.5 million. Net charge-offs were also slightly lower at \$331 thousand for the first nine months of 2020 compared to the first nine months of 2019's \$426 thousand.

Noninterest Income

Noninterest income for the first nine months of 2020 increased over the first nine months of 2019 by \$2.3 million. Gain on sale of loans showed an \$1.6 million increase over the first nine months of 2019 with the refinance activity due to interest rate reductions. Combined service fees increased by \$460 thousand with increased debit card income of \$358 thousand, servicing rights income of \$642 thousand and mortgage release fees of \$262 thousand. Overdraft and returned check income decreased \$636 thousand and miscellaneous service fees decreased \$196 thousand. The Company did sell some of its available-for-sale securities in first quarter 2020 and recognized a gain of \$270 thousand.

Noninterest Expense

Through the first nine months of 2020, noninterest expenses were \$1.5 million higher than in the first nine months of 2019. 2019 included \$1.3 million of third party acquisition related costs incurred with the Limberlost transaction. The nine months of 2020 included an increase of \$1.1 million in salaries and wages in addition to an increase of \$313 thousand in employee benefits. The addition of the acquired offices, normal merit increases, increased restricted stock expense, increased medical costs and increased employer taxes related to the vesting of restricted stock awards have impacted 2020. 2019 included acquisition costs in these categories of \$145 thousand.

Data processing fees were \$817 thousand lower than last year with \$868 thousand of the decrease acquisition related. A seven year contract extension was signed in the third quarter of 2016 which has helped reduce the expense while adding new products and services to better align with our customers' expectations in the coming years. We have already added additional products in 2020, mainly focused on mobile services and business deposit accounts. Furniture and equipment was \$204 thousand higher than 2019. Increased depreciation for new offices and office transformations, along with increased maintenance costs have led to this expense to increase over 2019.

General and administrative expenses were up \$130 thousand over the first nine months of 2019. Acquisition costs of \$182 thousand were included in this line for 2019. One of the largest increases was \$106 thousand for audit, accounting and exam fees. Overdraft related expenses were \$96 thousand more than 2019. The largest decrease for 2020 was in legal expenses. These two line items on the income statement were down by \$131 thousand over the first nine months of 2019. During the first nine months of 2019, legal acquisition expenses were \$96 thousand. Travel and convention expenses were down \$81 thousand as compared to 2019.

Income Taxes

Federal income tax expense was only \$3 thousand higher for the first nine months of 2020 compared to the first nine months of 2019. Effective tax rates were 19.04% and 18.62% for the first nine months of 2020 and 2019 respectively. The higher effective tax rate for the first nine months of 2020 equaled an increase in federal income tax expense of \$70 thousand with the remainder driven from decreased earnings.

Net Income

Overall, net income through the first nine months of 2020 was down \$360 thousand as compared to the first nine months of 2019. Provision for loan loss, which increased \$4.6 million for the first nine months of 2020 as compared to the first nine months of 2019, was the largest contributor to the decreased net income.

FORWARD LOOKING STATEMENTS

Statements contained in this portion of the Company's report may be forward-looking statements, as that term is defined in the Private Securities Litigation Reform Act of 1995. Forward-looking statements may be identified by the use of words such as "intend," "believe," "expect," "anticipate," "should," "planned," "estimated," and "potential." Such forward-looking statements are based on current expectations, but actual results may differ materially from those currently anticipated due to a number of factors, which include, but are not limited to, factors discussed in documents filed by the Company with the Securities and Exchange Commission from time to time. Other factors which could have a material adverse effect on the operations of the Company and its subsidiaries include, but are not limited to, changes in interest rates, general economic conditions, legislative and regulatory changes, monetary and fiscal policies of the U.S. Government, including policies of the U.S. Treasury and the Federal Reserve Board, the quality and composition of the loan or investment portfolios, demand for loan products, deposit flows, competition, demand for financial services in the Bank's market area, changes in relevant accounting principles and guidelines and other factors over which management has no control, including, but not limited to, the ongoing impact of the COVID-19 pandemic. The forward-looking statements are made as of the date of this report, and the Company assumes no obligation to update the forward-looking statements or to update the reasons why actual results differ from those projected in the forward-looking statements.

ITEM 3 QUALITATIVE AND QUANTITATIVE DISCLOSURES ABOUT MARKET RISK

Market risk is the exposure to loss resulting from changes in interest rates and equity prices. The primary market risk to which the Company is subject is interest rate risk. The majority of our interest rate risk arises from the instruments, positions and transactions entered into for purposes other than trading such as loans, available for sale securities, interest bearing deposits, short term borrowings and long term borrowings. Interest rate risk occurs when interest bearing assets and liabilities re-price at different times as market interest rates change. For example, if fixed rate assets are funded with variable rate debt, the spread between asset and liability rates will decline or turn negative if rates increase.

Interest rate risk is managed within an overall asset/liability framework. The principal objectives of asset/liability management are to manage sensitivity of net interest spreads and net income to potential changes in interest rates.

Funding positions are kept within predetermined limits designed to ensure that risk-taking is not excessive and that liquidity is properly managed. In the event that our asset/liabilities management strategies are unsuccessful, our profitability may be adversely affected. The Company employs a sensitivity analysis utilizing interest rate shocks to help in this analysis.

The shocks presented below assume an immediate change of rate in the percentages and directions shown covering a twelve month period:

<u>Interest Rate Shock</u> <u>on Net Interest Margin</u>			<u>Interest Rate Shock</u> <u>on Net Interest Income</u>			
Net Interest Margin (Ratio)	% Change to Flat Rate	Rate Direction	Rate Changes by	Cumulative Total (\$000)	% Change to Flat Rate	
3.65%	10.63%	Rising	3.00%	60,605	10.42%	
3.31%	0.43%	Rising	2.00%	55,997	2.03%	
3.27%	-0.67%	Rising	1.00%	55,062	0.32%	
3.29%	0.00%	Flat	0.00%	54,885	0.00%	
3.03%	-8.03%	Falling	-1.00%	51,308	-6.52%	
2.90%	-11.94%	Falling	-2.00%	49,450	-9.90%	
2.78%	-15.64%	Falling	-3.00%	47,713	-13.07%	

The net interest margin represents the forecasted twelve month margin. The Company also reviews shocks with a 4.0% fluctuation with a delayed time frame of 10 months and over a 24 month time frame. It also shows the effect rate changes will have on both the margin and net interest income. The goal of the Company is to lengthen the term of some of the Bank's fixed rate liabilities or sources of funds to decrease the exposure to a rising rate environment. Of course, customer desires also impact the Bank's ability to attract longer term deposits. Some movement into the longer term time deposits has occurred. Over the past year with the Limberlost acquisition, the Bank has experienced an increase in the time balances of our deposit portfolio, and therefore, an increase of term funding. Over the past two years, the Bank has also paid off term borrowings with the last \$5 million maturing December 2018; however, additional borrowings were a part of the Limberlost acquisition in 2019.

The shock chart currently shows a tightening in net interest margin over the next twelve months in a rising rate environment at 100 basis points and at all levels in a falling rate environment. At an increase of 100 basis points and the current low rate, there are not enough assets repricing above the floor for an expansion of net interest margin. Due to the existence of such a low rate environment, the model predicts expansion of net interest income at any level in a rising rate environment. Cost of funds are at 0.74% for the quarter and 0.95% for the year so the lowest shock of 100 basis points is where the Bank can take partial advantage and reprice some funds to match the level of shock. Once the shocks are falling over 100 basis points, the cost of funds cannot lower to match and the loss on net interest income continues to build. The average duration of the majority of the assets is outside the 12 month shock period. The majority of the newer loans added to the commercial real estate portfolio begin with an initial fixed rate period of three to five years whose variable adjustment is outside of the current shock time frame. The Bank continues to adjust its assumptions by including decay rates and key rate ties on certain deposit accounts and continues to review and modify those rates as the index rates change. All shocks are within risk exposure guidelines at all levels. The effect of the rate shocks may be mitigated to the extent that not all lines of business are directly tied to an external index and actual balance sheet composition may differ from prediction.

Overall, the Company must concentrate on increasing loan spreads on variable loans and extend the duration on cost of funds where possible.

ITEM 4 CONTROLS AND PROCEDURES

As of September 30, 2020, an evaluation was performed under the supervision and with the participation of the Company's management including the CEO and CFO, of the effectiveness of the design and operation of the Company's disclosure controls and procedures. Based on that evaluation, the Company's management, including the CEO and CFO, concluded that the Company's disclosure controls and procedures were effective as of September 30, 2020. There have been no changes in the Company's internal control over financial reporting that occurred during the quarter ended September 30, 2020 that have materially affected, or are reasonably likely to materially affect, the Company's internal control over financial reporting.

PART II OTHER INFORMATION

ITEM 1 LEGAL PROCEEDINGS

None

ITEM 1A RISK FACTORS

Except as otherwise provided below, there have been no material changes in the Company's risk factors from those disclosed in the Company's Annual Report on Form 10-K for the year ended December 31, 2019.

The ongoing COVID-19 pandemic and measures intended to prevent its spread could have a material adverse effect on our business, results of operations and financial condition, and such effects will depend on future developments, which are highly uncertain and are difficult to predict.

In December 2019, a novel coronavirus (COVID-19) was reported in China, and, in March 2020, the World Health Organization declared it a pandemic. On March 12, 2020, the President of the United States declared the COVID-19 outbreak in the United States a national emergency. The COVID-19 pandemic has caused significant economic dislocation in the United States as many state and local governments have ordered non-essential businesses to close and residents to shelter in place at home. This has resulted in an unprecedented slow-down in economic activity and a related increase in unemployment. Since the COVID-19 outbreak an unprecedented number of individuals have filed claims for unemployment, and stock markets have experienced significant volatility, with bank stocks suffering significant declines in value. In response to the COVID-19 outbreak, the Federal Reserve Board has reduced the benchmark fed funds rate to a target range of 0% to 0.25%, and the yields on 10 and 30-year treasury notes have declined to historic lows. The federal banking agencies have encouraged financial institutions to prudently work with affected borrowers and recently passed legislation to provide relief from reporting loan classifications due to modifications related to the COVID-19 outbreak.

Finally, the spread of the coronavirus has caused us to modify our business practices, including employee travel, employee work locations, and cancellation of physical participation in meetings, events and conferences. We may take further actions as may be required by government authorities or that we determine are in the best interests of our employees, customers and business partners. There is no certainty that such measures will be sufficient to mitigate the risks posed by the virus or will otherwise be satisfactory to government authorities. In addition, the success of our operations substantially depends on the management skills of our executive officers and directors, many of whom have held officer and director positions with us for many years. The unanticipated loss or unavailability of key employees due to the outbreak could harm our ability to operate our business or execute our business strategy.

Given the ongoing and dynamic nature of the circumstances, it is difficult to predict the full impact of the COVID-19 outbreak on our business. The United States government has taken steps to attempt to mitigate some of the more severe anticipated economic effects of the virus, including the passage of the CARES Act, but there can be no assurance that such steps will be effective or achieve their desired results in a timely fashion. The extent of such impact from the COVID-19 outbreak and related mitigation efforts will depend on future developments, which are highly uncertain, including but not limited to, the duration and spread of the outbreak, its severity, the actions to contain the virus or treat its impact, and how quickly and to what extent normal economic and operating conditions can resume. As the result, we could be subject to any of the following risks, any of which could have a material, adverse effect on our business, financial condition, liquidity, and results of operations:

- demand for our products and services may decline, making it difficult to grow assets and income;
- if the economy is unable to substantially reopen, and high levels of unemployment continue for an extended period of time, loan delinquencies, problem assets, and foreclosures may increase, resulting in increased charges and reduced income;

- collateral for loans, especially real estate, may decline in value, which could cause loan losses to increase;
- our allowance for loan losses may have to be increased if borrowers experience financial difficulties beyond forbearance periods, which will adversely affect our net income;
- the net worth and liquidity of loan guarantors may decline, impairing their ability to honor commitments to us;
- as the result of the decline in the Federal Reserve Board's target federal funds rate, the yield on our assets may decline to a greater extent than the decline in our cost of interest-bearing liabilities, reducing our net interest margin and spread and reducing net income;
- a material decrease in net income or a net loss over several quarters could result in a decrease in the rate of our quarterly cash dividend;
- we rely on third party vendors for certain services and the unavailability of a critical service due to the COVID-19 outbreak could have an adverse effect on us; and
- Federal Deposit Insurance Corporation premiums may increase if the agency experiences additional resolution costs.

Any one or a combination of the factors identified above could negatively impact our business, financial condition and results of operations and prospects. Even after the COVID-19 outbreak has subsided, we may continue to experience materially adverse impacts to our business as a result of the virus's global economic impact, including the availability of credit, adverse impacts on our liquidity and any recession that has occurred or may occur in the future.

ITEM 2 UNREGISTERED SALES OF EQUITY SECURITIES AND USE OF PROCEEDS

Treasury stock repurchased the quarter ended September 30, 2020.

Period	(a) Total Number of Shares Purchased	(b) Average Price Paid per Share	(c) Total Number of Shares Purchased as Part of Publicly Announced Plan or Programs (1)	(d) Maximum Number of Shares that may yet be purchased under the Plans or Programs
7/1/2020 to 7/31/2020	475 (2)	21.65 (2)	—	545,000
8/1/2020 to 8/31/2020	6,400 (2)	21.78 (2)	—	545,000
9/1/2020 to 9/30/2020	—	—	—	545,000
Total	6,875	21.77	—	545,000

(1) From time to time, the Company purchases shares in the market pursuant to a stock repurchase program publicly announced on January 17, 2020. On that date, the Board of Directors authorized the repurchase of 550,000 common shares between January 17, 2020 and December 31, 2020.

(2) Shares which were repurchased to account for tax payable on vested stock awards are outside of the Company's stock repurchase program.

ITEM 3 DEFAULTS UPON SENIOR SECURITIES

None

ITEM 4 MINE SAFETY DISCLOSURES

Not applicable

ITEM 5 OTHER INFORMATION

ITEM 6 EXHIBITS

3.1	<u>Amended Articles of Incorporation of the Registrant (incorporated by reference to Exhibit 3.1 to Registrant's Quarterly Report on Form 10-Q filed with the Commission on October 25, 2017).</u>
3.2	<u>Amended and Restated Code of Regulations of the Registrant (incorporated by reference to Exhibit 3.2 to Registrant's Quarterly Report on Form 10-Q filed with the Commission on July 26, 2017).</u>
4.1	<u>Description of Registrant's Common Stock (incorporated by reference to Exhibit 4.1 to Registrant's Annual Report on Form 10-K filed with the Commission on February 26, 2020).</u>
31.1	<u>Rule 13-a-14(a) Certification - CEO</u>
31.2	<u>Rule 13-a-14(a) Certification - CFO</u>
32.1	<u>Section 1350 Certification - CEO</u>
32.2	<u>Section 1350 Certification - CFO</u>
101.INS	Inline XBRL Instance Document - The instance document does not appear in the Interactive Data File because its XBRL tags are embedded within the Inline XBRL document. (1)
101.SCH	Inline XBRL Taxonomy Extension Schema Document (1)
101.CAL	Inline XBRL Taxonomy Extension Calculation Linkbase Document (1)
101.DEF	Inline XBRL Taxonomy Extension Definition Linkbase Document (1)
101.LAB	Inline XBRL Taxonomy Extension Label Linkbase Document (1)
101.PRE	Inline XBRL Taxonomy Extension Presentation Linkbase Document (1)
104	The cover page from the Company's Quarterly Report on Form 10-Q for the quarter ended September 30, 2020, has been formatted in Inline XBRL.

(1) Pursuant to Rule 406T of Regulation S-T, the interactive Data Files in Exhibit 101 hereto are deemed not filed or part of a registration statement or prospectus for purposes of Sections 11 or 12 of the Securities act of 1933, as amended, are deemed not filed for purposes of Section 18 of the Exchange Act of 1934, as amended, and otherwise are not subject to liability under those sections.

SIGNATURES

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.

Farmers & Merchants Bancorp, Inc.,

Date: October 28, 2020

By: /s/ Lars B. Eller
Lars B. Eller
President and Chief Executive Officer

Date: October 28, 2020

By: /s/ Barbara J. Britenriker
Barbara J. Britenriker
Executive Vice-President and
Chief Financial Officer

CERTIFICATIONS

I, Lars B. Eller, President and CEO of Farmers & Merchants Bancorp, Inc., certify that:

1. I have reviewed this quarterly report on Form 10-Q of Farmers & Merchants Bancorp, 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 quarterly 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 the Exchange Acts 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 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 controls 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: October 28, 2020

/s/ Lars B. Eller

Lars B. Eller

President and Chief Executive Officer

CERTIFICATIONS

I, Barbara J. Britenriker, Executive Vice President and CFO of Farmers & Merchants Bancorp, Inc., certify that:

1. I have reviewed this quarterly report on Form 10-Q of Farmers & Merchants Bancorp, 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 quarterly 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 the Exchange Acts 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 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 controls 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: October 28, 2020

/s/ Barbara J. Britenriker

Barbara J. Britenriker
Executive Vice President and
Chief Financial Officer

Exhibit 32.1

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

In connection with the Quarterly Report of Farmers & Merchants Bancorp, Inc. on Form 10-Q for the period ending September 30, 2020, as filed with the Securities and Exchange Commission ("the report"), I, Lars B. Eller, President and Chief Executive Officer, certify, pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, that:

1. The Report 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 the Report fairly presents, in all material respects, the financial condition and results of operations of Farmers & Merchants Bancorp, Inc. as of the dates and for the periods expressed in the Report.

Date: October 28, 2020

/s/ Lars B. Eller

Lars B. Eller

President and Chief Executive Officer

A signed original of this written statement required by Section 906 has been provided to Farmers & Merchants Bancorp, Inc. and will be retained by Farmers & Merchants Bancorp, Inc. and furnished to the Securities and Exchange Commission or its staff upon request.

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

In connection with the Quarterly Report of Farmers & Merchants Bancorp, Inc. on Form 10-Q for the period ending September 30, 2020, as filed with the Securities and Exchange Commission ("the report"), I, Barbara J. Britenriker, Executive Vice President and Chief Financial Officer, certify, pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, that:

1. The Report 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 the Report fairly presents, in all material respects, the financial condition and results of operations of Farmers & Merchants Bancorp, Inc. as of the dates and for the periods expressed in the Report.

Date: October 28, 2020

/s/ Barbara J. Britenriker

Barbara J. Britenriker
Executive Vice President and
Chief Financial Officer

A signed original of this written statement required by Section 906 has been provided to Farmers & Merchants Bancorp, Inc. and will be retained by Farmers & Merchants Bancorp, Inc. and furnished to the Securities and Exchange Commission or its staff upon request.