

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

FORM 10-Q

(Mark One)

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

For the quarterly period ended March 31, 2019

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 No. 001-38258

MERCHANTS BANCORP

(Exact name of registrant as specified in its charter)

Indiana
(State or other jurisdiction of
incorporation or organization)

20-5747400
(I.R.S. Employer
Identification Number)

11555 North Meridian Street, Suite 400 Carmel, Indiana
(Address of principal
executive office)

46032
(Zip Code)

(317) 569-7420

(Registrant's telephone number, including area code)

N/A

(Former name or former address, if changed since last report)

Indicate by check mark whether the registrant: (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports) and (2) has been subject to such filing requirements for the past 90 days.

Yes No

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

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

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

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

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act).

Yes No

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

Title of each class	Trading Symbol(s)	Name of each exchange on which registered
Common Stock, without par value	MBIN	NASDAQ
Series A Preferred Stock, without par value	MBINP	NASDAQ

As of May 6, 2019, the latest practicable date, 28,704,163 shares of the registrant's common stock, without par value, were issued and outstanding.

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Merchants Bancorp

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Part I – Financial Information

Item 1. Financial Statements

Merchants Bancorp
Condensed Consolidated Balance Sheets
March 31, 2019 (Unaudited) and December 31, 2018
(In thousands, except share data)

	March 31, 2019	December 31, 2018
Assets		
Cash and due from banks	\$ 19,554	\$ 25,855
Interest-earning demand accounts	293,897	310,669
Cash and cash equivalents	313,451	336,524
Securities purchased under agreements to resell	6,838	6,875
Trading securities	129,914	163,419
Available for sale securities	296,669	331,071
Federal Home Loan Bank (FHLB) stock	18,880	7,974
Loans held for sale (includes \$6,307 and \$11,886, respectively at fair value)	882,071	832,455
Loans receivable, net of allowance for loan losses of \$13,356 and \$12,704, respectively	2,168,256	2,045,423
Premises and equipment, net	21,078	15,136
Mortgage servicing rights	76,249	77,844
Interest receivable	14,365	13,827
Goodwill	17,144	17,477
Intangible assets, net	3,381	3,542
Other assets and receivables	28,429	32,596
Total assets	<u>\$ 3,976,725</u>	<u>\$ 3,884,163</u>
Liabilities and Shareholders' Equity		
Liabilities		
Deposits		
Noninterest-bearing	\$ 128,029	\$ 182,879
Interest-bearing	2,992,998	3,048,207
Total deposits	3,121,027	3,231,086
Borrowings	338,031	195,453
Deferred and current tax liabilities, net	18,274	15,444
Other liabilities	21,562	20,943
Total liabilities	<u>3,498,894</u>	<u>3,462,926</u>
Commitments and Contingencies		
Shareholders' Equity		
Common stock, without par value		
Authorized - 50,000,000 shares		
Issued and outstanding - 28,704,163 shares at March 31, 2019 and 28,694,036 shares at December 31, 2018		
	135,190	135,057
Preferred stock, without par value - 5,000,000 total shares authorized		
8% Preferred stock - \$1,000 per share liquidation preference		
Authorized - 50,000 shares		
Issued and outstanding - 41,625 shares		
	41,581	41,581
7% Series A Preferred stock - \$25 per share liquidation preference		
Authorized - 3,500,000 shares		
Issued and outstanding - 2,000,000 shares		
	48,269	—
Retained earnings	252,637	244,909
Accumulated other comprehensive income (loss)	154	(310)
Total shareholders' equity	<u>477,831</u>	<u>421,237</u>
Total liabilities and shareholders' equity	<u>\$ 3,976,725</u>	<u>\$ 3,884,163</u>

See notes to condensed consolidated financial statements.

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Merchants Bancorp
Condensed Consolidated Statements of Income (Unaudited)
For the Three Months Ended March 31, 2019 and 2018
(In thousands, except share data)

	Three Months Ended March 31,	
	2019	2018
Interest Income		
Loans	\$ 34,455	\$ 24,612
Investment securities:		
Trading	1,045	989
Available for sale - taxable	1,551	1,542
Available for sale - tax exempt	96	—
Federal Home Loan Bank stock	223	129
Other	2,304	1,766
Total interest income	<u>39,674</u>	<u>29,038</u>
Interest Expense		
Deposits	14,227	7,016
Borrowed funds	1,316	1,914
Total interest expense	<u>15,543</u>	<u>8,930</u>
Net Interest Income	24,131	20,108
Provision for loan losses	649	1,406
Net Interest Income After Provision for Loan Losses	<u>23,482</u>	<u>18,702</u>
Noninterest Income		
Gain on sale of loans	2,643	10,892
Loan servicing fees, net	(347)	(322)
Mortgage warehouse fees	753	486
Gains on sale of investments available for sale (includes \$127 and \$0, respectively, related to accumulated other comprehensive earnings reclassifications)	127	—
Other income	488	257
Total noninterest income	<u>3,664</u>	<u>11,313</u>
Noninterest Expense		
Salaries and employee benefits	8,567	6,487
Loan expenses	934	956
Occupancy and equipment	876	565
Professional fees	539	488
Deposit insurance expense	277	246
Technology expense	472	291
Other expense	1,370	1,237
Total noninterest expense	<u>13,035</u>	<u>10,270</u>
Income Before Income Taxes	14,111	19,745
Provision for income taxes (includes \$32 and \$0, respectively, related to income tax expense for reclassification items)	3,541	4,684
Net Income	<u>\$ 10,570</u>	<u>\$ 15,061</u>
Dividends on preferred stock	(833)	(833)
Net Income Allocated to Common Shareholders	<u>9,737</u>	<u>14,228</u>
Basic Earnings Per Share	<u>\$ 0.34</u>	<u>\$ 0.50</u>
Diluted Earnings Per Share	<u>\$ 0.34</u>	<u>\$ 0.50</u>
Weighted-Average Shares Outstanding		
Basic	<u>28,702,250</u>	<u>28,690,876</u>
Diluted	<u>28,737,439</u>	<u>28,710,480</u>

See notes to condensed consolidated financial statements.

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Merchants Bancorp
Condensed Consolidated Statements of Comprehensive Income (Unaudited)
For the Three Months Ended March 31, 2019 and 2018
(In thousands)

	Three Months Ended	
	March 31,	
	2019	2018
Net Income	\$ 10,570	\$ 15,061
Other Comprehensive Income (Loss):		
Net change in unrealized losses on investment securities available for sale, net of (taxes) benefits of \$(192) and \$97, respectively	559	(318)
Less: Reclassification adjustment for gains included in net income, net of \$32 tax expense in 2019	95	—
Other comprehensive income (loss) for the period	464	(318)
Comprehensive Income	<u>\$ 11,034</u>	<u>\$ 14,743</u>

See notes to condensed consolidated financial statements.

Merchants Bancorp
Condensed Consolidated Statement of Shareholders' Equity (Unaudited)
For the Three Months Ended March 31, 2019
(In thousands, except share data)

	Common Stock		8% Preferred Stock		7% Preferred Stock		Retained Earnings	Accumulated Other Comprehensive Income (Loss)	Total
	Shares	Amount	Shares	Amount	Shares	Amount			
Balance, January 1, 2019	28,694,036	\$ 135,057	41,625	\$ 41,581	—	\$ —	\$ 244,909	\$ (310)	\$ 421,237
Net income	—	—	—	—	—	—	10,570	—	10,570
Shares issued for stock compensation plans	10,127	133	—	—	—	—	—	—	133
Issuance of 7% preferred stock, net of offering expenses of \$1,731	—	—	—	—	2,000,000	48,269	—	—	48,269
Dividends on 8% preferred stock, \$5.00 per share	—	—	—	—	—	—	(833)	—	(833)
Dividends on common stock, \$0.07 per share	—	—	—	—	—	—	(2,009)	—	(2,009)
Other comprehensive income	—	—	—	—	—	—	—	464	464
Balance, March 31, 2019	28,704,163	\$ 135,190	41,625	\$ 41,581	2,000,000	\$ 48,269	\$ 252,637	\$ 154	\$ 477,831

For the Three Months Ended March 31, 2018
(In thousands, except share data)

	Common Stock		8% Preferred Stock		7% Preferred Stock		Retained Earnings	Accumulated Other Comprehensive Income (Loss)	Total
	Shares	Amount	Shares	Amount	Shares	Amount			
Balance, January 1, 2018	28,685,167	\$ 134,891	41,625	\$ 41,581	—	\$ —	\$ 192,008	\$ (1,006)	\$ 367,474
Net income	—	—	—	—	—	—	15,061	—	15,061
Shares issued for stock compensation plans	7,039	50	—	—	—	—	—	—	50
Dividends on 8% preferred stock, \$5.00 per share	—	—	—	—	—	—	(833)	—	(833)
Dividends on common stock, \$0.06 per share	—	—	—	—	—	—	(1,721)	—	(1,721)
Reclassification of deferred tax asset due to tax reform	—	—	—	—	—	—	243	(243)	—
Other comprehensive loss	—	—	—	—	—	—	—	(318)	(318)
Balance, March 31, 2018	28,692,206	\$ 134,941	41,625	\$ 41,581	—	\$ —	\$ 204,758	\$ (1,567)	\$ 379,713

See notes to condensed consolidated financial statements.

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Merchants Bancorp
Condensed Consolidated Statements of Cash Flows (Unaudited)
Three Months Ended March 31, 2019 and 2018
(In thousands)

	Three Months Ended March 31,	
	2019	2018
Operating activities:		
Net income	\$ 10,570	\$ 15,061
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation	137	103
Provision for loan losses	649	1,406
Gain on sale of securities	(127)	—
Gain on sale of loans	(2,643)	(10,892)
Proceeds from sales of loans	3,729,430	4,020,784
Loans and participations originated and purchased for sale	(3,776,827)	(4,098,115)
Change in mortgage servicing rights for paydowns and fair value adjustments	2,615	2,263
Net change in:		
Trading securities	33,505	(59,193)
Other assets and receivables	2,699	(3,407)
Other liabilities	1,933	7,918
Other	798	309
Net cash provided by (used in) operating activities	<u>2,739</u>	<u>(123,763)</u>
Investing activities:		
Net change in securities purchased under agreements to resell	37	41
Purchases of available-for-sale securities	(45,000)	(28,224)
Proceeds from the sale of available-for-sale securities	31,086	—
Proceeds from calls, maturities and paydowns of available-for-sale securities	49,055	25,360
Purchases of loans	(14,233)	(34,273)
Net change in loans receivable	(109,620)	(137,092)
Purchase of Federal Home Loan Bank stock	(11,860)	(118)
Proceeds from sale of Federal Home Loan Bank stock	1,190	—
Purchases of premises and equipment	(4,206)	(1,055)
Purchases of mortgage servicing rights	—	(327)
Purchase of limited partnership interests	—	(13)
Cash (paid) received in acquisition of subsidiary	—	6,505
Net cash used in investing activities	<u>(103,551)</u>	<u>(169,196)</u>
Financing activities:		
Net change in deposits	(110,031)	82,106
Proceeds from Federal Home Loan Bank borrowings	2,348,720	284,189
Repayment of Federal Home Loan Bank borrowings	(2,209,281)	(142,568)
Proceeds from issuance of preferred stock	48,269	—
Proceeds from notes payable	4,404	—
Payments on notes payable	(1,500)	—
Dividends	(2,842)	(2,554)
Net cash provided by financing activities	<u>77,739</u>	<u>221,173</u>
Net Change in Cash and Cash Equivalents	<u>(23,073)</u>	<u>(71,786)</u>
Cash and Cash Equivalents, Beginning of Period	<u>336,524</u>	<u>359,519</u>
Cash and Cash Equivalents, End of Period	<u>\$ 313,451</u>	<u>\$ 287,733</u>
Additional Cash Flows Information:		
Interest paid	\$ 14,745	\$ 7,751
Income taxes paid	64	—
The Company purchased all of the capital stock of FMBI on January 2, 2018. In conjunction with the acquisitions, liabilities were assumed as follows:		
Fair value of assets acquired	\$ —	\$ 44,217
Cash paid for the capital stock/fair value common stock issued	—	5,472
Fair value of liabilities assumed	—	38,745

See notes to condensed consolidated financial statements.

Merchants Bancorp
Notes to Condensed Consolidated Financial Statements
(Unaudited)

Note 1: Basis of Presentation

The accompanying consolidated financial statements include the accounts of Merchants Bancorp, a registered bank holding company (the “Company”) and its wholly owned subsidiaries, Merchants Bank of Indiana (“Merchants Bank”) and Farmers-Merchants Bank of Illinois (“FMBI”). Merchants Bank’s direct and indirect subsidiaries include Merchants Capital Corp. (“MCC”), Merchants Capital Servicing, LLC (“MCS”), Ash Realty Holdings, LLC (“Ash Realty”), MBI Midtown West, LLC (“MMW”), Natty Mac Funding, Inc. (“NMF”), and OneTrust Funding, Inc. The Company also acquired Farmers-Merchants National Bank of Paxton (“FMNBP”) on October 1, 2018 through a merger with FMBI, with FMBI as the surviving entity. All these entities are collectively referred to as the “Company”.

The accompanying unaudited condensed consolidated balance sheet of the Company as of December 31, 2018, which has been derived from audited financial statements, and unaudited condensed consolidated financial statements of the Company as of March 31, 2019 and for the three months ended March 31, 2019 and 2018, were prepared in accordance with the instructions for Form 10-Q and Article 10 of Regulation S-X and, therefore, do not include information or footnotes necessary for a complete presentation of financial position, results of operations and cash flows in conformity with accounting principles generally accepted in the United States of America. Accordingly, these condensed financial statements should be read in conjunction with the audited financial statements and notes thereto of the Company as of and for the year ended December 31, 2018 in its Annual Report on Form 10-K. Reference is made to the accounting policies of the Company described in the Notes to the Financial Statements contained in the Annual Report on Form 10-K.

In the opinion of management, all adjustments (consisting only of normal recurring adjustments) which are necessary for a fair presentation of the unaudited financial statements have been included to present fairly the financial position as of March 31, 2019 and the results of operations for the three months ended March 31, 2019 and 2018, and cash flows for the three months ended March 31, 2019 and 2018. All interim amounts have not been audited and the results of operations for the three months ended March 31, 2019, herein are not necessarily indicative of the results of operations to be expected for the entire year.

Principles of Consolidation

The consolidated financial statements as of and for the period ended March 31, 2019 include the Company, and its wholly owned subsidiaries, Merchants Bank, and FMBI. Also included are Merchants Bank’s wholly owned subsidiaries, MCC, MCC’s wholly owned subsidiary, MCS, Ash Realty, NMF, MMW, and OneTrust Funding, Inc. The consolidated financial statements as of and for the period ended March 31, 2018, include the Company and its wholly owned subsidiary, Merchants Bank, and Merchants Bank’s wholly owned subsidiaries, FMBI (after being acquired on January 2, 2018 and excluding results from FMNBP, which was acquired on October 1, 2018), MCC, MCC’s wholly owned subsidiary, MCS, Ash Realty, NMF, and MMW. All significant intercompany accounts and transactions have been eliminated in consolidation.

Use of Estimates

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

Material estimates that are particularly susceptible to significant change relate to the determination of the allowance for loan losses, loan servicing rights and fair values of financial instruments.

Merchants Bancorp
Notes to Condensed Consolidated Financial Statements
(Unaudited)

Public Offering of Preferred Stock

On March 28, 2019 the Company issued 2,000,000 shares of 7.00% Fixed-to-Floating Rate Series A Non-Cumulative Perpetual Preferred Stock, without par value (the “Series A Preferred Stock”), with a liquidation preference of \$25.00 per share. The aggregate gross offering proceeds for the shares issued by the Company was \$50.0 million, and after deducting underwriting discounts and commissions and offering expenses of approximately \$1.7 million paid to third parties, the Company received total net proceeds of \$48.3 million. On April 12, 2019, the Company issued an additional 81,800 shares of Series A Preferred Stock to the underwriters related to their exercise of an option to purchase additional shares under the associated underwriting agreement, resulting in an addition \$2.0 million in net proceeds, after deducting \$41,000 underwriting discounts. The Series A Preferred Stock have no voting rights with respect to matters that generally require the approval of our common shareholders. Dividends on the Series A Preferred Stock, to the extent declared by the Company’s board, are payable quarterly.

Recent Acquisitions

On May 8, 2017, the Company entered into a Stock Purchase Agreement to acquire FMBI (formerly Joy State Bank). The acquisition closed on January 2, 2018 at a total cost of approximately \$5.5 million. At December 31, 2017 Joy State Bank had \$43 million in assets. The Company recorded goodwill and intangible assets totaling \$988,000 and \$478,000, respectively, in connection with the acquisition. The intangible assets consisted of core deposit intangibles that are being amortized over 10 years on an accelerated basis. The acquired time deposits of \$16.7 million were recorded at a fair value of \$16.9 million. The fair value premium of \$185,000 is being accreted against interest expense over 20 months. The acquired loan portfolio of \$27.9 million was recorded at a fair value of \$27.5 million. The fair value discount of \$458,000 is being accreted to interest income on a straight-line basis over an average of 39 months in accordance with ASC 310-20. While there were some loans identified for potential classification under ASC 310-30, they were not material to the transaction. On October 22, 2018, the Company changed the name of Joy State Bank to Farmers-Merchants Bank of Illinois (“FMBI”). As a result of the acquisition, the Company increased its deposit base and benefited from economies of scale. The acquisition did not materially impact the Company’s financial position, results of operations or cash flows.

On October 1, 2018, the Company acquired FM Bancorp, Inc., a bank holding company, and its wholly owned subsidiary, Farmers-Merchants National Bank of Paxton (“FMNBP”). On that date, FM Bancorp, Inc. ultimately merged with and into the Company, with the Company as the surviving entity, and FMNBP merged with and into Joy State Bank, with Joy State Bank as the surviving bank. Effective October 22, 2018, Joy State Bank’s name changed to Farmers-Merchants Bank of Illinois (“FMBI”). Under the terms of the merger agreement, shareholders of the 27,537 outstanding shares of FM Bancorp, Inc. were compensated \$795.29 per share, for a total purchase price of \$21.9 million. As of September 30, 2018, FM Bancorp, Inc. and Farmers-Merchants National Bank of Paxton had total assets of approximately \$110.0 million, available for sale securities of \$66.3 million, deposits of approximately \$95.7 million, and net loan receivables of approximately \$35.0 million. As of March 31, 2019, the Company recorded goodwill and intangible assets totaling \$6.9 million and \$1.9 million. The intangible assets consisted of core deposit intangibles that are being amortized over 10 years on an accelerated basis. The acquired available for sale securities of \$66.3 million were recorded at fair value. A fair value discount associated with securities of \$1.0 million is being accreted into interest income, in accordance with ASC 310-20. While there were some loans identified for potential classification under ASC 310-30, they were not material to the transaction. The acquired gross loan portfolio of \$35.4 million was recorded at a fair value of \$34.8 million. The fair value discount of \$625,000 includes a discount related to interest assumptions for \$279,000 and to credit assumptions for \$346,000. The portion related to interest assumptions is being accreted into interest income on a straight-line basis over an average of 72 months in accordance with ASC 310-20. The discount portion related to credit assumptions is being accreted into interest income over the life of the loan. The acquired deposits of \$95.7 million were recorded at a fair value of \$95.7 million. As a result of the acquisition, the Company increased its deposit base and benefited from economies of scale. The acquisition did not materially impact the Company’s financial position, results of operations or cash flows.

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Merchants Bancorp Notes to Condensed Consolidated Financial Statements (Unaudited)

On December 31, 2018, the Company acquired the assets of NattyMac, LLC, a warehouse lender operating out of Clearwater, Florida, from Home Point Financial Corporation (“Home Point”). The Company also fully repaid Home Point the balance of, and all interest owed on, the \$30 million subordinated debt it had previously invested in the Company. Goodwill totaling \$5.0 million was recorded by the Company. Certain fair value measurements, intangibles, and the purchase price allocation are still being evaluated by management and are subject to change during the measurement period. As a result of the acquisition, the Company expects to increase its geographic footprint in the warehouse business, reduce its costs of borrowing, increase the earnings generated from its warehouse business, and benefit from its experienced talent pool. The acquisition did not materially impact the Company’s financial position, results of operations or cash flows.

Given the impact of the acquisitions was immaterial to the Company and its results of operations, pro forma information has not been included.

Reclassifications

Certain reclassifications have been made to the 2018 financial statements to conform to the financial statement presentation as of and for the three months ended March 31, 2019. These reclassifications had no effect net income.

Note 2: Securities

Trading Securities

Securities that are held principally for resale in the near term are recorded as trading securities at fair value with changes in fair value recorded in earnings. Trading securities include FHA and conventional Fannie Mae and Freddie Mac participation certificates. The unrealized gains included in trading securities totaled \$545,000 and \$1.5 million at March 31, 2019 and 2018, respectively.

Securities Available-For-Sale

The amortized cost and approximate fair values, together with gross unrealized gains and losses, of securities are as follows:

	March 31, 2019			Approximate Fair Value
	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	
(In thousands)				
Available-for-sale securities:				
Treasury notes	\$ 10,740	\$ 8	\$ 5	\$ 10,743
Federal agencies	235,621	2	423	235,200
Municipals	12,050	430	—	12,480
Mortgage-backed - Government-sponsored entity (GSE) - residential	38,092	155	1	38,246
Total available-for-sale securities	<u>\$ 296,503</u>	<u>\$ 595</u>	<u>\$ 429</u>	<u>\$ 296,669</u>

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Merchants Bancorp Notes to Condensed Consolidated Financial Statements (Unaudited)

	December 31, 2018			
	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Approximate Fair Value
(In thousands)				
Available-for-sale securities:				
Treasury notes	\$ 11,928	\$ 26	\$ 13	\$ 11,941
Federal agencies	237,894	8	972	236,930
Municipals	21,014	336	18	21,332
Mortgage-backed - Government-sponsored entity (GSE) - residential	60,693	254	79	60,868
Total available-for-sale securities	<u>\$ 331,529</u>	<u>\$ 624</u>	<u>\$ 1,082</u>	<u>\$ 331,071</u>

The amortized cost and fair value of available-for-sale securities at March 31, 2019 and December 31, 2018, by contractual maturity, are shown below. Expected maturities will differ from contractual maturities because issuers may have the right to call or prepay obligations with or without call or prepayment penalties. Securities not due at a single maturity date are shown separately.

Contractual Maturity	March 31, 2019		December 31, 2018	
	Amortized Cost	Fair Value	Amortized Cost	Fair Value
(In thousands)				
Within one year	\$ 149,649	\$ 149,318	\$ 179,323	\$ 178,581
After one through five years	98,685	98,643	72,470	72,282
After five through ten years	2,120	2,210	7,087	7,203
After ten years	7,957	8,252	11,956	12,137
	<u>258,411</u>	<u>258,423</u>	<u>270,836</u>	<u>270,203</u>
Mortgage-backed - Government-sponsored entity (GSE) - residential	38,092	38,246	60,693	60,868
	<u>\$ 296,503</u>	<u>\$ 296,669</u>	<u>\$ 331,529</u>	<u>\$ 331,071</u>

During the three months ended March 31, 2019, \$31.1 million of securities available-for-sale were sold, and a net gain of \$127,000 was recognized, consisting of \$361,000 in gains and \$234,000 of losses. During the three months ended March 31, 2018, no securities available-for-sale were sold.

The following tables show the Company's investments' gross unrealized losses and fair value of the Company's investments with unrealized losses that are not deemed to be other-than-temporarily impaired, aggregated by investment class and length of time that individual securities have been in a continuous unrealized loss position at March 31, 2019 and December 31, 2018:

	March 31, 2019					
	Less than 12 Months		12 Months or Longer		Total	
	Fair Value	Gross Unrealized Losses	Fair Value	Gross Unrealized Losses	Fair Value	Gross Unrealized Losses
(In thousands)						
Available-for-sale securities:						
Treasury notes	\$ —	\$ —	\$ 2,243	\$ 5	\$ 2,243	\$ 5
Federal agencies	—	—	180,198	423	180,198	423
Municipals	—	—	—	—	—	—
Mortgage-backed - Government-sponsored entity (GSE) - residential	914	1	—	—	914	1
	<u>\$ 914</u>	<u>\$ 1</u>	<u>\$ 182,441</u>	<u>\$ 428</u>	<u>\$ 183,355</u>	<u>\$ 429</u>

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	December 31, 2018					
	Less than 12 Months		12 Months or Longer		Total	
	Fair Value	Gross Unrealized Losses	Fair Value	Gross Unrealized Losses	Fair Value	Gross Unrealized Losses
	(In thousands)					
Available-for-sale securities:						
Treasury notes	\$ 1,990	\$ 8	\$ 995	\$ 5	\$ 2,985	\$ 13
Federal agencies	28,296	97	191,280	875	219,576	972
Municipals	2,051	18	—	—	2,051	18
Mortgage-backed - Government-sponsored entity (GSE) - residential	15,543	79	—	—	15,543	79
	<u>\$ 47,880</u>	<u>\$ 202</u>	<u>\$ 192,275</u>	<u>\$ 880</u>	<u>\$ 240,155</u>	<u>\$ 1,082</u>

Other-than-temporary Impairment

Unrealized losses on securities have not been recognized to income because the Company has the intent and ability to hold the securities for the foreseeable future, and the decline in fair value is primarily due to increased market interest rates. The fair value is expected to recover as the bonds approach the maturity date.

Note 3: Loans and Allowance for Loan Losses

Loans that management has the intent and ability to hold for the foreseeable future or until maturity or payoff are reported at their outstanding principal balances adjusted for unearned income, charge-offs, the allowance for loan losses, any unamortized deferred fees or costs on originated loans and unamortized premiums or discounts on purchased loans.

For loans amortized at cost, interest income is accrued based on the unpaid principal balance.

The accrual of interest on loans is discontinued at the time the loan is 90 days past due unless the credit is well-secured and in process of collection. Past-due status is based on contractual terms of the loan. In all cases, loans are placed on nonaccrual or charged off at an earlier date if collection of principal or interest is considered doubtful.

All interest accrued but not collected for loans that are placed on nonaccrual or charged off is reversed against interest income. The interest on these loans is applied to the principal balance until the loan can be returned to an accrual status. Loans are returned to accrual status when all the principal and interest amounts contractually due are brought current and future payments are reasonably assured.

For all loan portfolio segments, the Company promptly charges off loans, or portions thereof, when available information confirms that specific loans are uncollectable based on information that includes, but is not limited to, (1) the deteriorating financial condition of the borrower, (2) declining collateral values, and/or (3) legal action, including bankruptcy, that impairs the borrower's ability to adequately meet its obligations. For impaired loans that are considered to be solely collateral dependent, a partial charge-off is recorded when a loss has been confirmed by an updated appraisal or other appropriate valuation of the collateral.

When cash payments are received on impaired loans in each loan class, the Company records the payment as interest income unless collection of the remaining recorded principal amount is doubtful, at which time payments are used to reduce the principal balance of the loan. Troubled debt restructured loans recognize interest income on an accrual basis at the renegotiated rate if the loan is in compliance with the modified terms.

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Interest earned from the time of funding to the time of sale is recognized as interest income as accrued. Fees earned agreements are recognized when collected as noninterest income.

Loans receivable at March 31, 2019 and December 31, 2018 include:

	March 31, 2019	December 31, 2018
	(In thousands)	
Mortgage warehouse lines of credit	\$ 412,171	\$ 337,332
Residential real estate	409,172	410,871
Multi-family and healthcare financing	965,363	914,393
Commercial and commercial real estate	296,483	299,194
Agricultural production and real estate	81,063	79,255
Consumer and margin loans	17,360	17,082
	<u>2,181,612</u>	<u>2,058,127</u>
Less		
Allowance for loan losses	<u>13,356</u>	<u>12,704</u>
Loans Receivable	<u>\$ 2,168,256</u>	<u>\$ 2,045,423</u>

Risk characteristics applicable to each segment of the loan portfolio are described as follows.

Mortgage Warehouse Lines of Credit (MTG WHLOC): Under its warehouse program, the Company provides warehouse financing arrangements to approved mortgage companies for the origination and sale of residential mortgage loans and to a lesser extent multi-family loans. Agency eligible, governmental and jumbo residential mortgage loans that are secured by mortgages placed on existing one to four family dwellings may be originated or purchased and placed on each mortgage warehouse line.

As a secured line of credit, collateral pledged to the Company secures each individual mortgage until the lender sells the loan in the secondary market. A traditional secured warehouse line of credit typically carries a base interest rate of 30-day LIBOR, plus a margin, or mortgage note rate, less a margin.

Risk is evident if there is a change in the fair value of mortgage loans originated by mortgage bankers in warehouse, the sale of which is the expected source of repayment of the borrowings under a warehouse line of credit.

Residential Real Estate Loans (RES RE): Real estate loans are secured by owner-occupied 1-4 family residences. Repayment of residential real estate loans is primarily dependent on the personal income and credit rating of the borrowers. All-in-One mortgages included in this segment typically carry a base rate of 30-day LIBOR, plus a margin.

Multi-Family and Healthcare Financing (MF RE): The Company engages in multi-family and healthcare financing, including construction loans, specializing in originating and servicing loans for multi-family rental and senior living properties. In addition, the Company originates loans secured by an assignment of federal income tax credits by partnerships invested in multi-family real estate projects. Construction and land loans are generally based upon estimates of costs and estimated value of the completed project and include independent appraisal reviews and a financial analysis of the developers and property owners. Sources of repayment of these loans may include permanent loans, sales of developed property or an interim loan commitment from the Company until permanent agency-eligible financing is obtained. These loans are considered to be higher risk than other real estate loans due to their ultimate repayment being sensitive to interest rate changes, general economic conditions and the availability of long-term financing. Credit risk in these loans may be impacted by the creditworthiness of a borrower, property values and the local economy in the Company's market area. Repayment of these loans depends on the successful operation of a business or property and the borrower's cash flows.

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Commercial Lending and Commercial Real Estate Loans (CML & CRE): The commercial lending and commercial real estate portfolio includes loans to commercial customers for use in financing working capital needs, equipment purchases and expansions, as well as loans to commercial customers to finance land and improvements. It also includes loans collateralized by mortgage servicing rights of mortgage warehouse customers. The loans in this category are repaid primarily from the cash flow of a borrower's principal business operation. Credit risk in these loans is driven by creditworthiness of a borrower and the economic conditions that impact the cash flow stability from business operations.

Agricultural Production and Real Estate Loans (AG & AGRE): Agricultural production loans are generally comprised of seasonal operating lines of credit to grain farmers to plant and harvest corn and soybeans and term loans to fund the purchase of equipment. The Company also offers long term financing to purchase agricultural real estate. Specific underwriting standards have been established for agricultural-related loans including the establishment of projections for each operating year based on industry-developed estimates of farm input costs and expected commodity yields and prices. Operating lines are typically written for one year and secured by the crop and other farm assets as considered necessary. The Company is approved to sell agricultural loans in the secondary market through the Federal Agricultural Mortgage Corporation and uses this relationship to manage interest rate risk within the portfolio.

Consumer and Margin Loans (CON & MAR): Consumer loans are those loans secured by household assets. Margin loans are those loans secured by marketable securities. The term and maximum amount for these loans are determined by considering the purpose of the loan, the margin (advance percentage against value) in all collateral, the primary source of repayment, and the borrower's other related cash flow.

The allowance for loan losses is established as losses are estimated to have occurred through a provision for loan losses charged to net interest income. Loan losses are charged against the allowance when management believes the uncollectability of a loan balance is confirmed. Subsequent recoveries, if any, are credited to the allowance.

The allowance for loan losses is evaluated on a regular basis by management and is based upon management's periodic review of the collectability of the loans in light of historical experience, the nature and volume of the loan portfolio, adverse situations that may affect the borrower's ability to repay, estimated value of any underlying collateral and prevailing economic conditions. This evaluation is inherently subjective as it requires estimates that are susceptible to significant revision as more information becomes available.

The allowance consists of allocated and general components. The allocated component relates to loans that are classified as impaired. For those loans that are classified as impaired, an allowance is established when the discounted cash flows (or collateral value or observable market price) of the impaired loan is lower than the carrying value of that loan. The general component covers non-classified loans and is based on historical charge-off experience and expected loss given default derived from the Company's internal risk rating process. Other adjustments may be made to the allowance for pools of loans after an assessment of internal or external influences on credit quality that are not fully reflected in the historical loss or risk rating data.

A loan is considered impaired when, based on current information and events, it is probable that the Company will be unable to collect the scheduled payments of principal or interest when due according to the contractual terms of the loan agreement. Factors considered by management in determining impairment include payment status, collateral value and the probability of collecting scheduled principal and interest payments when due. Loans that experience insignificant payment delays and payment shortfalls generally are not classified as impaired. Management determines the significance of payment delays and payment shortfalls on a case-by-case basis, taking into consideration all of the circumstances surrounding the loan and the borrower, including the length of the delay, the reasons for the delay, the borrower's prior payment record and the amount of the shortfall in relation to the principal and interest owed. Impairment is measured on a loan-by-loan basis for commercial and construction loans by either the present value of expected future cash flows discounted at the loan's effective interest rate, the loan's obtainable market price or the fair value of the collateral if the loan is collateral dependent. For impaired loans where the Company utilizes discounted

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cash flows to determine the level of impairment, the Company includes the entire change in the present value of cash flows as bad debt expense.

Groups of loans with similar risk characteristics are collectively evaluated for impairment based on the group's historical loss experience adjusted for changes in trends, conditions and other relevant factors that affect repayment of the loans. Accordingly, the Company does not separately identify individual consumer and residential loans for impairment measurements, unless such loans are the subject of a restructuring agreement due to financial difficulties of the borrower.

In the course of working with borrowers, the Company may choose to restructure the contractual terms of certain loans. In restructuring the loan, the Company attempts to work out an alternative payment schedule with the borrower in order to optimize collectability of the loan. A troubled debt restructuring (TDR) occurs when, for economic or legal reasons related to a borrower's financial difficulties, the Company grants a concession to the borrower that it would not otherwise consider. Terms may be modified to fit the ability of the borrower to repay in line with its current financial status, and the restructuring of the loan may include the transfer of assets from the borrower to satisfy the debt, a modification of loan terms, or a combination of the two.

Nonaccrual loans, including TDRs that have not met the six-month minimum performance criterion, are reported as non-performing loans. For all loan classes, it is the Company's policy to have any restructured loans which are on nonaccrual status prior to being restructured remain on nonaccrual status until three months of satisfactory borrower performance, at which time management would consider its return to accrual status. A loan is generally classified as nonaccrual when the Company believes that receipt of principal and interest is questionable under the terms of the loan agreement. Most generally, this is at 90 or more days past due.

With regard to determination of the amount of the allowance for credit losses, restructured loans are considered to be impaired. As a result, the determination of the amount of impaired loans for each portfolio segment within troubled debt restructurings is the same as detailed previously above.

The following tables present, by portfolio segment, the activity in the allowance for loan losses for the three months ended March 31, 2019 and 2018 and the recorded investment in loans and impairment method as of March 31, 2019:

	At or For the Three Months Ended March 31, 2019							
	MTG WHLOC	RES RE	MF RE	CML & CRE	AG & AGRE	CON & MAR	TOTAL	
	(In thousands)							
Allowance for loan losses								
Balance, beginning of period	\$ 1,068	\$ 1,986	\$ 6,030	\$ 3,051	\$ 429	\$ 140	\$ 12,704	
Provision (credit) for loan losses	186	4	347	71	34	7	649	
Loans charged to the allowance	—	—	—	—	—	—	—	
Recoveries of loans previously charged off	—	—	—	—	3	—	3	
Balance, end of period	\$ 1,254	\$ 1,990	\$ 6,377	\$ 3,122	\$ 466	\$ 147	\$ 13,356	
Ending balance: individually evaluated for impairment	\$ 225	\$ —	\$ —	\$ 500	\$ 20	\$ —	\$ 745	
Ending balance: collectively evaluated for impairment	\$ 1,029	\$ 1,990	\$ 6,377	\$ 2,622	\$ 446	\$ 147	\$ 12,611	
Loans								
Ending balance	\$ 412,171	\$ 409,172	\$ 965,363	\$ 296,483	\$ 81,063	\$ 17,360	\$ 2,181,612	
Ending balance individually evaluated for impairment	\$ 572	\$ 4,255	\$ —	\$ 8,186	\$ 347	\$ 50	\$ 13,410	
Ending balance collectively evaluated for impairment	\$ 411,599	\$ 404,917	\$ 965,363	\$ 288,297	\$ 80,716	\$ 17,310	\$ 2,168,202	

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	For the Three Months Ended March 31, 2018						
	MTG WHLOC	RES RE	MF RE	CML & CRE	AG & AGRE	CON & MAR	TOTAL
	(In thousands)						
Allowance for loan losses							
Balance, beginning of period	\$ 283	\$ 1,587	\$ 3,502	\$ 2,362	\$ 320	\$ 257	\$ 8,311
Provision (credit) for loan losses	223	76	748	323	13	23	1,406
Loans charged to the allowance	—	—	—	—	—	(17)	(17)
Recoveries of loans previously charged off	—	1	—	—	—	4	5
Balance, end of period	<u>\$ 506</u>	<u>\$ 1,664</u>	<u>\$ 4,250</u>	<u>\$ 2,685</u>	<u>\$ 333</u>	<u>\$ 267</u>	<u>\$ 9,705</u>

The following table presents the allowance for loan losses and the recorded investment in loans and impairment method as of December 31, 2018:

	December 31, 2018						
	MTG WHLOC	RES RE	MF RE	CML & CRE	AG & AGRE	CON & MAR	TOTAL
	(In thousands)						
Allowance for loan losses							
Balance, December 31, 2018	\$ 1,068	\$ 1,986	\$ 6,030	\$ 3,051	\$ 429	\$ 140	\$ 12,704
Ending balance: individually evaluated for impairment	\$ 225	\$ —	\$ —	\$ 400	\$ 20	\$ —	\$ 645
Ending balance: collectively evaluated for impairment	\$ 843	\$ 1,986	\$ 6,030	\$ 2,651	\$ 409	\$ 140	\$ 12,059
Loans							
Balance, December 31, 2018	\$ 337,332	\$ 410,871	\$ 914,393	\$ 299,194	\$ 79,255	\$ 17,082	\$ 2,058,127
Ending balance individually evaluated for impairment	\$ 575	\$ 1,606	\$ —	\$ 8,576	\$ 370	\$ 58	\$ 11,185
Ending balance collectively evaluated for impairment	<u>\$ 336,757</u>	<u>\$ 409,265</u>	<u>\$ 914,393</u>	<u>\$ 290,618</u>	<u>\$ 78,885</u>	<u>\$ 17,024</u>	<u>\$ 2,046,942</u>

Internal Risk Categories

In adherence with policy, the Company uses the following internal risk grading categories and definitions for loans:

Average or above – Loans to borrowers of satisfactory financial strength or better. Earnings performance is consistent with primary and secondary sources of repayment that are well defined and adequate to retire the debt in a timely and orderly fashion. These businesses would generally exhibit satisfactory asset quality and liquidity with moderate leverage, average performance to their peer group and experienced management in key positions. These loans are disclosed as “Acceptable and Above” in the following table.

Acceptable – Loans to borrowers involving more than average risk and which contain certain characteristics that require some supervision and attention by the lender. Asset quality is acceptable, but debt capacity is modest and little excess liquidity is available. The borrower may be fully leveraged and unable to sustain major setbacks. Covenants are structured to ensure adequate protection. Borrower’s management may have limited experience and depth. This category includes loans which are highly leveraged due to regulatory constraints, as well as loans involving reasonable exceptions to policy. These loans are disclosed as “Acceptable and Above” in the following table.

Special Mention (Watch) – This is a loan that is sound and collectable but contains considerable risk. Loans classified as special mention have a potential weakness that deserves management’s close attention. If left uncorrected, these potential weaknesses may result in deterioration of the repayment prospects for the loan or of the institution’s credit position at some future date.

Substandard - Loans classified as substandard are inadequately protected by the current net worth and paying capacity of the obligor or of the collateral pledged, if any. Loans so classified have a well-defined weakness or weaknesses that jeopardize the liquidation of the debt. They are characterized by the distinct possibility that the institution will sustain some loss if the deficiencies are not corrected.

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Doubtful - Loans classified as doubtful have all the weaknesses inherent in those classified as substandard, with the added characteristic that the weaknesses make collection or liquidation in full, on the basis of currently existing facts, conditions, and values, highly questionable and improbable.

The following tables present the credit risk profile of the Company's loan portfolio based on internal rating category and payment activity as of March 31, 2019 and December 31, 2018:

	March 31, 2019						
	MTG WHLOC	RES RE	MF RE	CML & CRE	AG & AGRE	CON & MAR	TOTAL
	(In thousands)						
Special Mention (Watch)	\$ —	\$ 590	\$ 56,962	\$ 12,451	\$ 2,791	\$ 381	\$ 73,175
Substandard	572	4,255	—	8,186	347	50	13,410
Doubtful	—	—	—	—	—	—	—
Acceptable and Above	411,599	404,327	908,401	275,846	77,925	16,929	2,095,027
Total	<u>\$ 412,171</u>	<u>\$ 409,172</u>	<u>\$ 965,363</u>	<u>\$ 296,483</u>	<u>\$ 81,063</u>	<u>\$ 17,360</u>	<u>\$ 2,181,612</u>

	December 31, 2018						
	MTG WHLOC	RES RE	MF RE	CML & CRE	AG & AGRE	CON & MAR	TOTAL
	(In thousands)						
Special Mention (Watch)	\$ —	\$ 443	\$ 71,734	\$ 14,650	\$ 3,096	\$ 681	\$ 90,604
Substandard	575	1,606	—	8,576	370	58	11,185
Doubtful	—	—	—	—	—	—	—
Acceptable and Above	336,757	408,822	842,659	275,968	75,789	16,343	1,956,338
Total	<u>\$ 337,332</u>	<u>\$ 410,871</u>	<u>\$ 914,393</u>	<u>\$ 299,194</u>	<u>\$ 79,255</u>	<u>\$ 17,082</u>	<u>\$ 2,058,127</u>

The Company evaluates the loan risk grading system definitions and allowance for loan loss methodology on an ongoing basis. No significant changes were made to either during the past year.

The following tables present the Company's loan portfolio aging analysis of the recorded investment in loans as of March 31, 2019 and December 31, 2018:

	March 31, 2019					
	30-59 Days Past Due	60-89 Days Past Due	Greater Than 90 Days	Total Past Due	Current	Total Loans
	(In thousands)					
MTG WHLOC	\$ —	\$ —	\$ 324	\$ 324	\$ 411,847	\$ 412,171
RES RE	3,431	237	998	4,666	404,506	409,172
MF RE	—	—	—	—	965,363	965,363
CML & CRE	191	306	175	672	295,811	296,483
AG & AGRE	53	—	577	630	80,433	81,063
CON & MAR	13	—	21	34	17,326	17,360
	<u>\$ 3,688</u>	<u>\$ 543</u>	<u>\$ 2,095</u>	<u>\$ 6,326</u>	<u>\$ 2,175,286</u>	<u>\$ 2,181,612</u>

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	December 31, 2018					
	30-59 Days Past Due	60-89 Days Past Due	Greater Than 90 Days	Total Past Due	Current	Total Loans
	(In thousands)					
MTG WHLOC	\$ —	\$ —	\$ 324	\$ 324	\$ 337,008	\$ 337,332
RES RE	579	178	825	1,582	409,289	410,871
MF RE	—	—	—	—	914,393	914,393
CML & CRE	245	52	253	550	298,644	299,194
AG & AGRE	91	—	588	679	78,576	79,255
CON & MAR	2	52	28	82	17,000	17,082
	<u>\$ 917</u>	<u>\$ 282</u>	<u>\$ 2,018</u>	<u>\$ 3,217</u>	<u>\$ 2,054,910</u>	<u>\$ 2,058,127</u>

A loan is considered impaired, in accordance with the impairment accounting guidance (ASC 310-10-35-16), when based on current information and events, it is probable the Company will be unable to collect all amounts due from the borrower in accordance with the contractual terms of the loan. Impaired loans include nonperforming commercial loans but also include loans modified in troubled debt restructurings.

The following tables present impaired loans and specific valuation allowance information based on class level as of March 31, 2019 and December 31, 2018:

	March 31, 2019						
	MTG WHLOC	RES RE	MF RE	CML & CRE	AG & AGRE	CON & MAR	TOTAL
	(In thousands)						
Impaired loans without a specific allowance:							
Recorded investment	\$ 248	\$ 4,255	\$ —	\$ 5,907	\$ 88	\$ 50	\$ 10,548
Unpaid principal balance	248	4,255	—	5,907	88	50	10,548
Impaired loans with a specific allowance:							
Recorded investment	324	—	—	2,279	259	—	2,862
Unpaid principal balance	324	—	—	2,279	259	—	2,862
Specific allowance	225	—	—	500	20	—	745
Total impaired loans:							
Recorded investment	572	4,255	—	8,186	347	50	13,410
Unpaid principal balance	572	4,255	—	8,186	347	50	13,410
Specific allowance	225	—	—	500	20	—	745

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	December 31, 2018						
	MTG WHLOC	RES RE	MF RE	CML & CRE	AG & AGRE	CON & MAR	TOTAL
	(In thousands)						
Impaired loans without a specific allowance:							
Recorded investment	\$ 251	\$ 1,606	\$ —	\$ 5,636	\$ 88	\$ 58	\$ 7,639
Unpaid principal balance	251	1,606	—	5,636	88	58	7,639
Impaired loans with a specific allowance:							
Recorded investment	324	—	—	2,940	282	—	3,546
Unpaid principal balance	324	—	—	2,940	282	—	3,546
Specific allowance	225	—	—	400	20	—	645
Total impaired loans:							
Recorded investment	575	1,606	—	8,576	370	58	11,185
Unpaid principal balance	575	1,606	—	8,576	370	58	11,185
Specific allowance	225	—	—	400	20	—	645

The following tables present by portfolio class, information related to the average recorded investment and interest income recognized on impaired loans for the three months ended March 31, 2019 and 2018:

	MTG WHLOC	RES RE	MF RE	CML & CRE	AG & AGRE	CON & MAR	TOTAL
	(In thousands)						
Three months ended March 31, 2019:							
Average recorded investment in impaired loans	\$ 574	\$ 2,806	\$ —	\$ 8,468	\$ 364	\$ 48	\$ 12,260
Interest income recognized	—	15	—	140	—	—	155
Three months ended March 31, 2018:							
Average recorded investment in impaired loans	\$ 1,352	\$ 729	\$ 117	\$ 6,587	\$ 635	\$ 146	\$ 9,566
Interest income recognized	19	3	3	46	—	—	71

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The following table presents the Company's nonaccrual loans and loans past due 90 days or more and still accruing at March 31, 2019 and December 31, 2018.

	March 31, 2019		December 31, 2018	
	Nonaccrual	Total Loans > 90 Days & Accruing	Nonaccrual	Total Loans > 90 Days & Accruing
	(In thousands)			
MTG WHLOC	\$ 572	\$ —	\$ 575	\$ —
RES RE	702	454	893	74
MF RE	—	—	—	—
CML & CRE	228	—	136	117
AG & AGRE	259	317	282	307
CON & MAR	13	8	18	9
	<u>\$ 1,774</u>	<u>\$ 779</u>	<u>\$ 1,904</u>	<u>\$ 507</u>

No troubled loans were restructured during the three months ended March 31, 2019 or 2018. No restructured loans defaulted during the three months ended March 31, 2019 or 2018. There were no residential loans in process of foreclosure at March 31, 2019 or December 31, 2018.

Note 4: Regulatory Matters

The Company, Merchants Bank, and FMBI are subject to various regulatory capital requirements administered by the federal banking agencies. Failure to meet minimum capital requirements can initiate certain mandatory, and possibly additional discretionary, actions by federal and state banking regulators that, if undertaken, could have a direct material effect on the Company's financial statements. Under capital adequacy guidelines and the regulatory framework for prompt corrective action, the Company, Merchants Bank, and FMBI must meet specific capital guidelines that involve quantitative measures of the Company's, Merchants Bank, and FMBI's assets, liabilities and certain off-balance-sheet items as calculated under regulatory accounting practices. The Company's, Merchants Bank's, and FMBI's capital amounts and classification are also subject to qualitative judgments by the regulators about components, risk weightings and other factors. Furthermore, the Company's, Merchants Bank's, and FMBI's regulators could require adjustments to regulatory capital not reflected in these financial statements.

Quantitative measures established by regulation to ensure capital adequacy require the Company, Merchants Bank, and FMBI to maintain minimum amounts and ratios (set forth in the table below). Management believes, as of March 31, 2019 and December 31, 2018, that the Company, Merchants Bank, and FMBI met all capital adequacy requirements to which they were subject.

As of March 31, 2019 and December 31, 2018, the most recent notifications from the Board of Governors of the Federal Reserve System ("Federal Reserve") categorized the Company as well capitalized and most recent notifications from the Federal Deposit Insurance Corporation ("FDIC") categorized Merchants Bank and FMBI as well capitalized under the regulatory framework for prompt corrective action. To be categorized as well capitalized, a company must maintain minimum total risk-based, Tier I risk-based and Tier I leverage ratios as set forth in the table. There are no conditions or events since that notification that management believes have changed the Company, Merchants Bank, or FMBI's category.

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The Company, Merchants Bank, and FMBI's actual capital amounts and ratios are also presented in the following tables.

	Actual		Minimum Amount Required for Adequately Capitalized ⁽¹⁾		Minimum Amount To Be Well Capitalized ⁽¹⁾	
	Amount	Ratio	Amount	Ratio	Amount	Ratio
(Dollars in thousands)						
March 31, 2019						
Total capital ⁽¹⁾ (to risk-weighted assets)						
Company	\$ 453,361	13.3 %	\$ 272,136	8.0 %	\$ —	N/A
Merchants Bank	478,574	14.6 %	262,223	8.0 %	327,778	10.0 %
FMBI	19,384	15.7 %	9,876	8.0 %	12,345	10.0 %
Tier 1 capital ⁽¹⁾ (to risk-weighted assets)						
Company	440,007	12.9 %	204,102	6.0 %	—	N/A
Merchants Bank	465,636	14.2 %	196,667	6.0 %	262,223	8.0 %
FMBI	18,966	15.4 %	7,407	6.0 %	9,876	8.0 %
Common Equity Tier 1 capital ⁽¹⁾ (to risk-weighted assets)						
Company	350,157	10.3 %	153,077	4.5 %	—	N/A
Merchants Bank	465,636	14.2 %	147,500	4.5 %	213,056	6.5 %
FMBI	18,966	15.4 %	5,555	4.5 %	8,025	6.5 %
Tier 1 capital ⁽¹⁾ (to average assets)						
Company	440,007	12.0 %	146,417	4.0 %	—	N/A
Merchants Bank	465,636	13.3 %	140,344	4.0 %	175,430	5.0 %
FMBI	18,966	11.9 %	6,384	4.0 %	7,980	5.0 %
(Dollars in thousands)						
December 31, 2018						
Total capital ⁽¹⁾ (to risk-weighted assets)						
Company	\$ 393,654	12.3 %	\$ 255,884	8.0 %	\$ —	N/A
Merchants Bank	412,386	13.3 %	248,290	8.0 %	310,363	10.0 %
FMBI	17,537	18.6 %	7,559	8.0 %	9,448	10.0 %
Tier 1 capital ⁽¹⁾ (to risk-weighted assets)						
Company	380,950	11.9 %	191,913	6.0 %	—	N/A
Merchants Bank	399,815	12.9 %	186,218	6.0 %	248,290	8.0 %
FMBI	17,404	18.4 %	5,669	6.0 %	7,559	8.0 %
Common Equity Tier 1 capital ⁽¹⁾ (to risk-weighted assets)						
Company	339,369	10.6 %	143,935	4.5 %	—	N/A
Merchants Bank	399,815	12.9 %	139,663	4.5 %	201,736	6.5 %
FMBI	17,404	18.4 %	4,252	4.5 %	6,141	6.5 %
Tier 1 capital ⁽¹⁾ (to average assets)						
Company	380,950	10.0 %	152,081	4.0 %	—	N/A
Merchants Bank	399,815	11.0 %	145,723	4.0 %	182,154	5.0 %
FMBI	17,404	10.8 %	6,453	4.0 %	8,066	5.0 %

1 As defined by regulatory agencies.

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Beginning January 1, 2015, a new Basel III Capital Rule applied to Merchants Bank. The following table lists the capital categories and ratios determined by the Board of Governors of the Federal Reserve System and the FDIC.

Capital Category	Total Risk-based Capital ratio	Tier 1 Risk-based Capital ratio	Common Equity Tier 1 Risk-based Capital ratio	Tier 1 Leverage ratio
Well capitalized	10 %	8 %	6.5 %	5 %
Adequately capitalized	8	6	4.5	4
Undercapitalized	<8	<6	<4.5	<4
Significantly undercapitalized	<6	<4	<3	<3
Critically undercapitalized	Tangible Equity/Total Assets \leq 2%			

The Basel III Capital Rules, among other things, (i) introduced a new capital measure called “Common Equity Tier 1” (CET1), (ii) specified that Tier 1 capital consist of CET1 and “Additional Tier 1 Capital” instruments meeting specified requirements, (iii) defined CET1 narrowly by requiring that most deductions/adjustments to regulatory capital measures be made to CET1 and not to the other components of capital and (iv) expanded the scope of the deductions/adjustments as compared to existing regulations.

Implementation of the deductions and other adjustments to CET1 began on January 1, 2015 and are being phased in over a four-year period (beginning on January 1, 2015, and an additional 20% per year thereafter.) Under the new Basel III Capital Rules, in order to avoid limitations on capital distributions of dividend payments and certain discretionary bonus payments to executive officers, a banking organization must hold a capital conservation buffer composed of capital above its minimum risk-based capital requirements. The implementation of the capital conservation buffer began on January 1, 2016, at the 0.625% level and was phased in over a four-year period (increasing by that amount on each subsequent January 1 until it reached 2.5% on January 1, 2019).

Note 5: Derivative Financial Instruments

The Company uses derivative financial instruments to help manage exposure to interest rate risk and the effects that changes in interest rates may have on net income and the fair value of assets and liabilities. The Company enters into forward contracts for the future delivery of mortgage loans to third party investors and enters into interest rate locks with potential borrowers to fund specific mortgage loans that will be sold into the secondary market. The forward contracts are entered into in order to economically hedge the effect of changes in interest rates resulting from the Company’s commitment to fund the loans.

Each of these items are considered derivatives, but are not designated as accounting hedges, and are recorded at fair value with changes in fair value reflected in noninterest income on the condensed consolidated statements of income. The fair value of derivative instruments with a positive fair value are reported in other assets in the condensed consolidated balance sheets while derivative instruments with a negative fair value are reported in other liabilities in the condensed consolidated balance sheets.

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The following table presents the notional amount and fair value of interest rate locks and forward contracts utilized by the Company at March 31, 2019 and December 31, 2018.

	Notional Amount	Balance Sheet Location	Fair Value	
			Asset	(Liability)
March 31, 2019	(In thousands)		(In thousands)	
Interest rate lock commitments	\$ 9,706	Derivative assets/liabilities	\$ 71	\$ 1
Forward contracts	15,260	Derivative assets/liabilities	—	18
			\$ 71	\$ 19

	Notional Amount	Balance Sheet Location	Fair Value	
			Asset	(Liability)
December 31, 2018	(In thousands)		(In thousands)	
Interest rate lock commitments	\$ 8,812	Derivative assets/liabilities	\$ 70	\$ —
Forward contracts	19,640	Derivative assets/liabilities	—	9
			\$ 70	\$ 9

Fair values of derivative financial instruments were estimated using changes in mortgage interest rates from the date the Company entered into the interest rate lock commitment and the balance sheet date. The following table summarizes the periodic changes in the fair value of the derivative financial instruments on the condensed consolidated statements of income for the three months ended March 31, 2019 and 2018.

	Three Months Ended March 31,	
	2019	2018
	(In thousands)	
Interest rate lock commitments	\$ —	\$ 114
Forward contracts ⁽¹⁾	(5)	105
Net derivative gains (losses)	\$ (5)	\$ 219

(1)
Amount includes pair-off settlements.

Note 6: Disclosures about Fair Value of Assets and Liabilities

Fair value is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. Fair value measurements must maximize the use of observable inputs and minimize the use of unobservable inputs. There is a hierarchy of three levels of inputs that may be used to measure fair value:

- Level 1** Quoted prices in active markets for identical assets or liabilities
- Level 2** Observable inputs other than Level 1 prices, such as quoted prices for similar assets or liabilities; quoted prices in markets that are not active; or other inputs that are observable or can be corroborated by observable market data for substantially the full term of the assets or liabilities
- Level 3** Unobservable inputs supported by little or no market activity and are significant to the fair value of the assets or liabilities

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Recurring Measurements

The following tables present the fair value measurements of assets and liabilities recognized in the accompanying balance sheets measured at fair value on a recurring basis and the level within the fair value hierarchy in which the fair value measurements fall at March 31, 2019 and December 31, 2018:

Assets	Fair Value Measurements Using			
	Fair Value	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
March 31, 2019				
Trading securities	\$ 129,914	\$ —	\$ 129,914	\$ —
Available-for-sale securities:				
Treasury notes	10,743	10,743	—	—
Federal agencies	235,200	—	235,200	—
Municipals	12,480	—	12,480	—
Mortgage-backed - Government-sponsored entity (GSE) - residential	38,246	—	38,246	—
Loans held for sale	6,307	—	6,307	—
Mortgage servicing rights	76,249	—	—	76,249
Derivative assets - interest rate lock commitments	71	—	—	71
Derivative liabilities - interest rate lock commitments	1	—	—	1
Derivative liabilities - forward contracts	18	—	18	—
December 31, 2018				
Trading securities	\$ 163,419	\$ —	\$ 163,419	\$ —
Available-for-sale securities:				
Treasury notes	11,941	11,941	—	—
Federal agencies	236,930	—	236,930	—
Municipals	21,332	—	21,332	—
Mortgage-backed - Government-sponsored entity (GSE) - residential	60,868	—	60,868	—
Loans held for sale	11,886	—	11,886	—
Mortgage servicing rights	77,844	—	—	77,844
Derivative assets - interest rate lock commitments	70	—	—	70
Derivative liabilities - forward contracts	9	—	9	—

Following is a description of the valuation methodologies and inputs used for assets measured at fair value on a recurring basis and recognized in the accompanying balance sheets, as well as the general classification of such assets pursuant to the valuation hierarchy. There have been no significant changes in the valuation techniques during the three months ended March 31, 2019 and the year ended December 31, 2018. For assets classified within Level 3 of the fair value hierarchy, the process used to develop the reported fair value is described below.

Trading and Available-for-Sale Securities

Where quoted market prices are available in an active market, securities are classified within Level 1 of the valuation hierarchy. If quoted market prices are not available, then fair values are estimated by using quoted prices of securities with similar characteristics or independent asset pricing services and pricing models, the inputs of which are

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market-based or independently sourced market parameters, including, but not limited to, yield curves, interest rates, volatilities, prepayments, defaults, cumulative loss projections and cash flows. Such securities are classified in Level 2 of the valuation hierarchy including federal agencies, mortgage-backed securities, U.S. Treasuries, Equities, and Federal Housing Administration participation certificates. In certain cases where Level 1 or Level 2 inputs are not available, securities are classified within Level 3 of the hierarchy.

Loans Held for Sale

Certain loans held for sale at fair value are saleable into the secondary mortgage markets and their fair values are estimated using observable quoted market or contracted prices, or market price equivalents, which would be used by other market participants. These saleable loans are considered Level 2.

Mortgage Servicing Rights

Mortgage servicing rights do not trade in an active, open market with readily observable prices. Accordingly, fair value is estimated using discounted cash flow models having significant inputs of discount rate, prepayment speed and default rate. Due to the nature of the valuation inputs, mortgage servicing rights are classified within Level 3 of the hierarchy.

The Chief Financial Officer's (CFO) office contracts with a pricing specialist to generate fair value estimates on a quarterly basis. The CFO's office challenges the reasonableness of the assumptions used and reviews the methodology to ensure the estimated fair value complies with accounting standards generally accepted in the United States.

Derivative Financial Instruments

The Company estimates the fair value of interest rate lock commitments based on the value of the underlying mortgage loan, quoted mortgage backed security prices, estimates of the fair value of the mortgage servicing rights, and an estimate of the probability that the mortgage loan will fund within the terms of the interest rate lock commitment, net of expenses. The Company estimates the fair value of forward sales commitments based on market quotes of mortgage backed security prices for securities similar to the ones used, which are considered Level 2. With respect to its interest rate lock commitments, management determined that a Level 3 classification was most appropriate based on the various significant unobservable inputs utilized in estimating the fair value of its interest rate lock commitments. Changes in fair value of the Company's derivative financial instruments are recognized through noninterest income on its condensed consolidated statement of income.

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Level 3 Reconciliation

The following is a reconciliation of the beginning and ending balances of recurring fair value measurements recognized in the accompanying balance sheets using significant unobservable (Level 3) inputs:

	Three Months Ended March 31,	
	2019	2018
	(In thousands)	
Mortgage servicing rights		
Balance, beginning of period	\$ 77,844	\$ 66,079
Additions		
Originated and purchased servicing	1,020	3,452
Subtractions		
Paydowns	(1,110)	(1,370)
Changes in fair value due to changes in valuation inputs or assumptions used in the valuation model	(1,505)	(893)
Balance, end of period	<u>\$ 76,249</u>	<u>\$ 67,268</u>
Available-for-sale securities - Municipals		
Balance, beginning of period	\$ —	\$ 6,688
Additions		
Purchased securities	—	—
Subtractions		
Paydowns	—	(258)
Sales	—	—
Unrealized gains (losses) included in other comprehensive income	—	—
Balance, end of period	<u>\$ —</u>	<u>\$ 6,430</u>
Derivative Assets - interest rate lock commitments		
Balance, beginning of period	\$ 70	\$ —
Purchases	—	—
Changes in fair value	1	116
Balance, end of period	<u>\$ 71</u>	<u>\$ 116</u>
Derivative Liabilities - interest rate lock commitments		
Balance, beginning of period	\$ —	\$ —
Purchases	—	—
Changes in fair value	1	2
Balance, end of period	<u>\$ 1</u>	<u>\$ 2</u>

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Nonrecurring Measurements

The following table presents the fair value measurement of assets measured at fair value on a nonrecurring basis and the level within the fair value hierarchy in which the fair value measurements fall at March 31, 2019 and December 31, 2018.

Assets	Fair Value Measurements Using			
	Fair Value	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
(In thousands)				
March 31, 2019				
Impaired loans (collateral-dependent)	\$ 1,600	\$ —	\$ —	\$ 1,600
December 31, 2018				
Impaired loans (collateral-dependent)	\$ 2,639	\$ —	\$ —	\$ 2,639

Following is a description of the valuation methodologies and inputs used for assets measured at fair value on a nonrecurring basis and recognized in the accompanying balance sheet, as well as the general classification of such assets pursuant to the valuation hierarchy. For assets classified within Level 3 of the fair value hierarchy, the process used to develop the reported fair value is described below.

Collateral-Dependent Impaired Loans, Net of Allowance for Loan Losses

The estimated fair value of collateral-dependent impaired loans is based on the appraised fair value of the collateral, less estimated cost to sell. Collateral-dependent impaired loans are classified within Level 3 of the fair value hierarchy.

The Company considers the appraisal or evaluation as the starting point for determining fair value and then considers other factors and events in the environment that may affect the fair value. Appraisals of the collateral underlying collateral-dependent loans are obtained when the loan is determined to be collateral-dependent and subsequently as deemed necessary by the Company's Chief Credit Officer's (CCO) office. Appraisals are reviewed for accuracy and consistency by the CCO's office. Appraisers are selected from the list of approved appraisers maintained by management. The appraised values are reduced by discounts to consider lack of marketability and estimated cost to sell if repayment or satisfaction of the loan is dependent on the sale of the collateral. These discounts and estimates are developed by the CCO's office by comparison to historical results.

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Unobservable (Level 3) Inputs:

The following table presents quantitative information about unobservable inputs used in recurring and nonrecurring Level 3 fair value measurements other than goodwill.

	<u>Fair Value</u> (In thousands)	<u>Valuation</u> <u>Technique</u>	<u>Unobservable Inputs</u>	<u>Range</u>
At March 31, 2019:				
Collateral-dependent impaired loans	\$ 1,600	Market comparable properties	Marketability discount	32%
Mortgage servicing rights	\$ 76,249	Discounted cash flow	Discount rate	8% - 13%
			Constant prepayment rate	1% - 30%
Derivative assets - interest rate lock commitments	\$ 71	Discounted cash flow	loan closing rates	63-99%
Derivative liabilities - interest rate lock commitments	\$ 1	Discounted cash flow	loan closing rates	63-99%
At December 31, 2018:				
Collateral-dependent impaired loans	\$ 2,639	Market comparable properties	Marketability discount	17%-59%
Mortgage servicing rights	\$ 77,844	Discounted cash flow	Discount rate	8% - 13%
			Constant prepayment rate	1% - 30%
Derivative assets - interest rate lock commitments	\$ 70	Discounted cash flow	loan closing rates	95-100%

Sensitivity of Significant Unobservable Inputs

The following is a discussion of the sensitivity of significant unobservable inputs, the interrelationships between those inputs and other unobservable inputs used in recurring fair value measurement and of how those inputs might magnify or mitigate the effect of changes in the unobservable inputs on the fair value measurement.

Mortgage Servicing Rights

The significant unobservable inputs used in the fair value measurement of the Company's mortgage servicing rights are discount rates and constant prepayment rates. Significant increases or decreases in any of those inputs in isolation would result in a significantly different fair value measurement.

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Fair Value of Financial Instruments

The following table presents the carrying amount and estimated fair values of the Company's financial instruments not carried at fair value and the level within the fair value hierarchy in which the fair value measurements fall at March 31, 2019 and December 31, 2018.

Assets	Carrying Value	Fair Value	Fair Value Measurements Using		
			Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
March 31, 2019					
Financial assets:					
Cash and cash equivalents	\$ 313,451	\$ 313,451	\$ 313,451	\$ —	\$ —
Securities purchased under agreements to resell	6,838	6,838	—	6,838	—
FHLB stock	18,880	18,880	—	18,880	—
Loans held for sale	875,764	875,764	—	875,764	—
Loans, net	2,168,256	2,170,521	—	—	2,170,521
Interest receivable	14,365	14,365	—	14,365	—
Financial liabilities:					
Deposits	3,121,027	3,120,546	2,438,323	682,223	—
Lines of credit	31,605	31,605	—	31,605	—
Short-term subordinated debt	13,486	13,486	—	13,486	—
FHLB advances	292,940	292,823	—	292,823	—
Interest payable	4,930	4,930	—	4,930	—
December 31, 2018					
Financial assets:					
Cash and cash equivalents	\$ 336,524	\$ 336,524	\$ 336,524	\$ —	\$ —
Securities purchased under agreements to resell	6,875	6,875	—	6,875	—
FHLB stock	7,974	7,974	—	7,974	—
Loans held for sale	820,569	820,569	—	820,569	—
Loans, net	2,045,423	2,041,772	—	—	2,041,772
Interest receivable	13,827	13,827	—	13,827	—
Financial liabilities:					
Deposits	3,231,086	3,230,397	2,550,632	679,765	—
Lines of credit	33,150	33,150	—	33,150	—
Short-term subordinated debt	10,582	10,582	—	10,582	—
FHLB advances	151,721	151,723	—	151,723	—
Interest payable	4,132	4,132	—	4,132	—

The following methods were used to estimate the fair value of all other financial instruments recognized in the accompanying balance sheets at amounts other than fair value.

Cash and Cash Equivalents and Securities Purchased Under Agreement to Resell

The carrying amount approximates fair value.

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Federal Home Loan Bank Stock

The fair value of Federal Home Loan Bank of Indianapolis and Federal Home Loan Bank of Chicago (“FHLB”) stock is based on the price at which it may be sold to the FHLB.

Loans Held For Sale

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

Loans

Fair value is estimated by discounting the future cash flows using the market rates at which similar notes would be made to borrowers with similar credit ratings and for the same remaining maturities. The market rates used are based on current rates the Company would impose for similar loans and reflect a market participant assumption about risks associated with nonperformance, illiquidity, and the structure and term of the loans along with local economic and market conditions.

Interest Receivable and Payable

The carrying amount approximates fair value. The carrying amount is determined using the interest rate, balance and last payment date.

Deposits

The fair values of noninterest-bearing demand and savings accounts are equal to the amount payable on demand at the balance sheet date. Fair values for fixed-rate certificates and time deposits are estimated using a discounted cash flow calculation that applies interest rates currently being offered on certificates to a schedule of expected monthly maturities on such time deposits.

Line of Credit and Short-term Subordinated Debt

The carrying amount approximates fair value.

Federal Home Loan Bank Advances

Fair value is estimated by discounting the future cash flows using rates of similar advances with similar maturities. These rates were obtained from current rates offered by the FHLB.

Off-Balance Sheet Commitments

Commitments include commitments to purchase and originate mortgage loans, commitments to sell mortgage loans and standby letters of credit and are generally of a short-term nature. The fair value of such commitments are based on fees currently charged to similar agreements, taking into account the remaining terms of the agreements and the counterparties’ credit standing. The fair value of commitments to extend credit and letters of credit is not presented in the previous table since the fair value is considered to be insignificant.

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Note 7: Earnings Per Share

Earnings per share were computed as follows:

	Three Month Periods Ended March 31,					
	2019			2018		
	Net Income	Weighted- Average Shares	Per Share Amount	Net Income	Weighted- Average Shares	Per Share Amount
	(In thousands)			(In thousands)		
Net income	\$ 10,570			\$ 15,061		
Dividends on preferred stock	(833)			(833)		
Net income allocated to common shareholders	<u>\$ 9,737</u>			<u>\$ 14,228</u>		
Basic earnings per share		28,702,250	\$ 0.34		28,690,876	\$ 0.50
Effect of dilutive securities-restricted stock awards		35,189			19,604	
Diluted earnings per share		<u>28,737,439</u>	<u>\$ 0.34</u>		<u>28,710,480</u>	<u>\$ 0.50</u>

Note 8: Share-Based Payment Plans

Equity-based incentive awards are currently made through our 2017 Equity Incentive Plan (the “2017 Incentive Plan”). Prior to the adoption of the 2017 Incentive Plan, the equity awards we issued historically consisted of restricted stock awards issued pursuant to the Incentive Plan for Merchants Bank of Indiana Executive Officers (the “Prior Incentive Plan”). As of the effective date of the 2017 Equity Incentive Plan, no further awards will be granted under the Prior Incentive Plan. However, any previously outstanding incentive award granted under the Prior Incentive Plan remains subject to the terms of such plans until the time it is no longer outstanding. During the three months ended March 31, 2019 and March 31, 2018, the Company issued 10,127 and 7,039 shares, respectively, pursuant to the Prior Incentive Plan. As of March 31, 2019, the Company has not issued any shares pursuant to the 2017 Equity Incentive Plan.

During 2018, the Compensation Committee of the Board of Directors approved a plan for non-executive directors to receive a portion of their annual retainer fees in the form of common stock equal to \$10,000, rounded up to the nearest whole share. No shares were issued to directors during the three months ended March 31, 2019 or March 31, 2018.

Note 9: Segment Information

Our business segments are defined as Multi-family Mortgage Banking, Mortgage Warehousing, and Banking. The reportable business segments are consistent with the internal reporting and evaluation of the principal lines of business of the Company. The Multi-family Mortgage Banking segment originates and services government sponsored mortgages for multi-family and healthcare facilities. The Mortgage Warehousing segment funds agency eligible residential loans from origination or purchase to sale in the secondary market, as well as commercial loans to non-depository financial institutions. The Banking segment provides a wide range of financial products and services to consumers and businesses, including retail banking, commercial lending, agricultural lending, retail and correspondent residential mortgage banking, and Small Business Administration (“SBA”) lending. Other includes general and administrative expenses that provide services to all segments; internal funds transfer pricing offsets resulting from allocations to/from the other segments; certain elimination entries and investments in qualified affordable housing limited partnerships. All operations are domestic.

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The tables below present selected business segment financial information for the three months ended March 31, 2019 and 2018.

	Multi-family Mortgage Banking	Mortgage Warehousing	Banking	Other	Total
	(In thousands)				
Three Months Ended March 31, 2019					
Total interest income	\$ 331	\$ 14,380	\$ 24,492	\$ 471	\$ 39,674
Total interest expense	—	7,529	8,982	(968)	15,543
Net interest income	331	6,851	15,510	1,439	24,131
Provision for loan losses	—	133	516	—	649
Net interest income after provision for loan losses	331	6,718	14,994	1,439	23,482
Total noninterest income	2,691	753	883	(663)	3,664
Total noninterest expense	3,977	2,336	4,120	2,602	13,035
Income before income taxes	(955)	5,135	11,757	(1,826)	14,111
Income taxes	(243)	1,303	2,988	(507)	3,541
Net income (loss)	\$ (712)	\$ 3,832	\$ 8,769	\$ (1,319)	\$ 10,570
Total assets	\$ 160,609	\$ 1,554,233	\$ 2,223,890	\$ 37,993	\$ 3,976,725

	Multi-family Mortgage Banking	Mortgage Warehousing	Banking	Other	Total
	(In thousands)				
Three Months Ended March 31, 2018					
Total interest income	\$ 163	\$ 11,857	\$ 16,753	\$ 265	\$ 29,038
Total interest expense	—	3,797	5,593	(460)	8,930
Net interest income	163	8,060	11,160	725	20,108
Provision for loan losses	—	674	732	—	1,406
Net interest income after provision for loan losses	163	7,386	10,428	725	18,702
Total noninterest income	10,511	486	652	(336)	11,313
Noninterest expense	3,382	1,736	3,169	1,983	10,270
Income before income taxes	7,229	6,136	7,911	(1,594)	19,745
Income taxes	1,808	1,506	1,931	(561)	4,684
Net income (loss)	\$ 5,484	\$ 4,630	\$ 5,980	\$ (1,033)	\$ 15,061
Total assets	\$ 141,703	\$ 1,603,584	\$ 1,908,823	\$ 21,739	\$ 3,675,849

Note 10: Recent Accounting Pronouncements

The Company is an emerging growth company and as such will be subject to the effective dates noted for the private companies if they differ from the effective dates noted for public companies.

FASB ASU 2014-09, Revenue from Contracts with Customers

In May 2014, the Financial Accounting Standards Board (the “FASB”) issued Accounting Standards Update (“ASU”) 2014-09, “Revenue from Contracts with Customers,” which requires an entity to recognize the amount of revenue to which it expects to be entitled for the transfer of promised goods or services to customers. The ASU will replace most existing revenue recognition guidance in U.S. GAAP when it becomes effective. In March 2016 the FASB

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issued ASU 2016-08, “Principal versus Agent Considerations (Reporting Revenue Gross versus Net),” which clarifies the guidance in determining revenue recognition as principal versus agent. In April 2016, the FASB issued ASU 2016-10, “Identifying Performance Obligations and Licensing,” which provides guidance in accounting for immaterial performance obligations and shipping and handling. In May 2016, the FASB issued ASU 2016-12, “Narrow-Scope Improvements and Practical Expedients,” which provides clarification on assessing the collectability criterion, presentation of sales taxes, measurement date for noncash consideration and completed contracts at transition. This ASU also provides a practical expedient for contract modifications.

As an emerging growth company, these amendments are effective for annual reporting periods beginning after December 15, 2018, and for interim periods within annual periods beginning after December 15, 2019. The Company’s revenue is primarily comprised of net interest income on financial assets and financial liabilities, which is explicitly excluded from the scope of ASU 2014-09. The Company has evaluated the impact of adopting ASU 2014-09, but does not expect the impact to have a material impact on the Company’s financial position or results of operations.

FASB ASU 2016-01, Recognition and Measurement of Financial Assets and Financial Liabilities

In January 2016, the FASB issued ASU 2016-01, “Recognition and Measurement of Financial Assets and Financial Liabilities.” For public business entities, the amendments in this update include the elimination of the requirement to disclose the method(s) and significant assumptions used to estimate fair value that is required to be disclosed for financial instruments measured at amortized cost on the balance sheet, the requirement to use the exit price notion when measuring fair value of financial instruments for disclosure purposes, the requirement to present separately in other comprehensive income the portion of the total change in the fair value of a liability resulting from a change in the instrument-specific credit risk when the entity has elected to measure the liability at fair value in accordance with the fair value option for financial instruments, the requirement for separate presentation of financial assets and financial liabilities by measurement category and form of financial asset (that is, securities or loans and receivables) on the balance sheet or accompanying notes to the financial statements, and the amendments clarify that an entity should evaluate the need for a valuation allowance on a deferred tax asset related to available-for-sale securities in combination with the entity’s other deferred tax assets. An entity should apply the amendments to this update by means of a cumulative-effect adjustment to the balance sheet as of the beginning of the fiscal year of adoption.

As an emerging growth company, the amendments in this update are effective for fiscal years beginning after December 15, 2018, and interim periods within years beginning after December 15, 2019. Early adoption of the amendments in the update is not permitted, except that early application by public business entities to financial statements of fiscal years or interim periods that have not yet been issued or, by all other entities, that have not yet been made available for issuance, are permitted as of the beginning of the fiscal year of adoption for the following amendment: An entity should present separately in other comprehensive income the portion of the total change in the fair value of a liability at fair value in accordance with the fair value option for financial instruments. An entity should apply the amendments to this update by means of a cumulative-effect adjustment to the balance sheet as of the beginning of the fiscal year of adoption. The Company is continuing to evaluate the impact of adopting this new guidance on its consolidated financial statements, but the adoption of ASU 2016-01 is not expected to have a material impact on the Company’s financial position or results of operation.

FASB ASU 2016-02, Leases

In February 2016, the FASB issued ASU 2016-02, “Leases.” Under the new guidance, lessees will be required to recognize the following for all leases (with the exception of short-term leases) at the commencement date:

- A lease liability, which is a lessee’s obligation to make lease payments arising from a lease, measured on a discounted basis; and
- A right-of-use asset, which is an asset that represents the lessee’s right to use, or control the use of, a specified asset for the lease term.

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Under the new guidance, lessor accounting is largely unchanged. Certain targeted improvements were made to align, where necessary, lessor accounting with the lessee accounting model and Topic 606, “Revenue from Contracts with Customers.” The new lease guidance simplified the accounting for sale and leaseback transactions primarily because lessees must recognize lease assets and lease liabilities. Lessees will no longer be provided with a source of off-balance sheet financing. Lessees (for capital and operating leases) and lessors (for sales-type, direct financing, and operating leases) must apply a modified retrospective transition approach for leases existing at, or entered into after, the beginning of the earliest comparative period presented in the financial statements. The modified retrospective approach would not require any transition accounting for leases that expired before the earliest comparative period presented. Lessees and lessors may not apply a full retrospective transition approach.

As an emerging growth company, the amendments in ASU 2016-02 are effective, as an emerging growth company, beginning after December 15, 2019, and for interim periods for years beginning after January 1, 2020. Management is in the process of gathering documentation on current lease agreements to assess the impact of adopting this guidance on the Company’s financial statements, but its impact is not expected to be material.

FASB ASU 2016-13, Financial Instruments—Credit Losses

In June 2016, the FASB issued ASU 2016-13, “Financial Instruments—Credit Losses”. The amendments in this ASU replace the incurred loss model with a methodology that reflects expected credit losses over the life of the loan and requires consideration of a broader range of reasonable and supportable information to calculate credit loss estimates. ASU 2016-13 replaces the incurred loss impairment methodology with a new methodology that reflects expected credit losses over the lives of the loans and requires consideration of a broader range of information to form credit loss estimates. The ASU requires an organization to estimate all expected credit losses for financial assets measured at amortized cost, including loans and held-to-maturity debt securities, based on historical experience, current conditions, and reasonable and supportable forecasts. Additional disclosures are required.

As an emerging growth company, the amendments in ASU 2016-13 are effective, for fiscal years beginning after December 15, 2021, including interim periods within those fiscal years. The Company has established a cross-functional committee that is developing a project plan to review modeling data currently available and technology needed to ensure compliance of this standard. The committee has also met with multiple vendors to potentially assist in generating specific loan level details within our core systems, as well as compiling peer and industry data that would be useful in our modeling forecasts. While the Company generally expects to recognize a one-time cumulative effect adjustment to the allowance for loan losses as of the beginning of the first reporting period in which the new standard is effective, the Company cannot yet determine the magnitude of any such one-time adjustment or the overall impact of the new guidance on the Company’s consolidated financial statements. Management continues to expect that the implementation of this ASU may increase the balance of the allowance for loan losses and is continuing to evaluate the potential impact on the Company’s financial position and results of operations.

FASB ASU No. 2017-04, Intangibles—Goodwill and Other (Topic 350)

In January 2017, the FASB issued ASU 2017-04, “Intangibles—Goodwill and Other (Topic 350).” This ASU simplifies the test for goodwill impairment. Specifically, these amendments eliminate Step 2 from the goodwill impairment test, and 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.

As an emerging growth company, the amendments in this ASU are effective for annual goodwill impairment tests in fiscal years beginning after December 15, 2021. Management continues to believe that the changes will not have a material effect on the Company’s financial position and results of operations.

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FASB ASU 2017-08, Premium Amortization of Purchased Callable Debt

In March 2017, the FASB issued ASU 2017-08, “Premium Amortization of Purchased Callable Debt.” This ASU applies to all entities that hold investments in callable debt securities that have an amortized cost basis in excess of the amount that is repayable by the issuer at the earliest call date (that is, at a premium). The ASU requires the premium to be amortized to the earliest call date, not the maturity date. The amendments do not require an accounting change for securities held at a discount; the discount continues to be amortized to maturity.

As an emerging growth company, ASU 2017-08 is effective as to the Company for years beginning after December 15, 2019 and interim periods within years beginning after December 15, 2020. Early adoption is permitted. Management is still in the process of evaluating the impact of adopting this guidance, but does not expect the ASU to have a material effect on the Company’s financial position or results of operations.

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Forward-Looking Statements

Certain statements in this Form 10-Q, including, but not limited to, statements within Management’s Discussion and Analysis of Financial Condition and Results of Operations, are “forward-looking statements” within the meaning of the rules and regulations of the Securities and Exchange Commission (“SEC”). These forward-looking statements reflect our current views with respect to, among other things, future events and our financial performance. These statements are often, but not always, made through the use of words or phrases such as “may,” “might,” “should,” “could,” “predict,” “potential,” “believe,” “expect,” “continue,” “will,” “anticipate,” “seek,” “estimate,” “intend,” “plan,” “projection,” “goal,” “target,” “outlook,” “aim,” “would,” “annualized” and “outlook,” or the negative version of those words or other comparable words or phrases of a future or forward-looking nature. These forward-looking statements are not historical facts, and are based on current expectations, estimates and projections about our industry, management’s beliefs and certain assumptions made by management, many of which, by their nature, are inherently uncertain and beyond our control. Accordingly, we caution that any such forward-looking statements are not guarantees of future performance and are subject to risks, assumptions, estimates and uncertainties that are difficult to predict. Although we believe that the expectations reflected in these forward-looking statements are reasonable as of the date made, actual results may prove to be materially different from the results expressed or implied by the forward-looking statements.

A number of important factors could cause our actual results to differ materially from those indicated in these forward-looking statements, including those factors identified in the “Risk Factors” section of our Annual Report on Form 10-K for the year ended December 31, 2018 or “Item 2 - Management’s Discussion and Analysis of Financial Condition and Results of Operations” of this Form 10-Q or the following:

- business and economic conditions, particularly those affecting the financial services industry and our primary market areas;
- our ability to successfully manage our credit risk and the sufficiency of our allowance for loan loss;
- factors that can impact the performance of our loan portfolio, including real estate values and liquidity in our primary market areas, the financial health of our commercial borrowers and the success of construction projects that we finance, including any loans acquired in acquisition transactions;
- compliance with governmental and regulatory requirements, including the Dodd-Frank Act and others relating to banking, consumer protection, securities and tax matters;
- our ability to maintain licenses required in connection with multi-family mortgage origination, sale and servicing operations;
- our ability to identify and address cyber-security risks, fraud and systems errors;
- our ability to effectively execute our strategic plan and manage our growth;
- changes in our senior management team and our ability to attract, motivate and retain qualified personnel;
- governmental monetary and fiscal policies, and changes in market interest rates;
- liquidity issues, including fluctuations in the fair value and liquidity of the securities we hold for sale and our ability to raise additional capital, if necessary;
- incremental costs and obligations associated with operating as a public company;

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- effects of competition from a wide variety of local, regional, national and other providers of financial, investment and insurance services;
- the impact of any claims or legal actions to which we may be subject, including any effect on our reputation; and
- changes in federal tax law or policy.

The foregoing factors should not be construed as exhaustive and should be read together with the other cautionary statements included in this Form 10-Q. Any forward-looking statement speaks only as of the date on which it is made, and we do not undertake any obligation to update or review any forward-looking statement, whether as a result of new information, future developments or otherwise.

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

Management's discussion and analysis of the financial condition at March 31, 2019 and results of operations for the three months ended March 31, 2019 and 2018, is intended to assist in understanding the financial condition and results of operations of the Company. The information contained in this section should be read in conjunction with the unaudited condensed consolidated financial statements and the notes thereto, appearing in Part I, Item 1 of this Form 10-Q.

The words "the Company," "we," "our" and "us" refer to Merchants Bancorp and its consolidated subsidiaries, unless we indicate otherwise.

Introduction

We are a diversified bank holding company headquartered in Carmel, Indiana and registered under the Bank Holding Company Act of 1956, as amended. We currently operate multiple lines of business, including multi-family housing and servicing, mortgage warehouse financing, retail and correspondent residential mortgage banking, agricultural lending and traditional community banking.

Our business consists primarily of funding low risk loans that sell within 90 days of origination. The sale of loans and servicing fees generated from the multi-family rental real estate loans servicing portfolio contribute to noninterest income. The funding source is primarily from mortgage custodial, municipal, and retail and commercial deposits. We believe that the combination of net interest income and noninterest income from the sale of low risk profile assets results in lower than industry charge offs and a lower expense base serving to maximize net income and shareholder return.

Critical Accounting Policies and Estimates

The preparation of our consolidated financial statements requires management to make estimates and judgments that affect the reported amounts of assets, liabilities, revenues and expenses. These estimates are based upon historical experience and on various other assumptions that management believes are reasonable under the current circumstances. These estimates form the basis for making judgments about the carrying value of certain assets and liabilities that are not readily available from other sources. Actual results may differ from these estimates under different assumptions or conditions.

The Jumpstart Our Business Startups Act of 2012 ("JOBS Act") contains provisions that, among other things, reduce certain reporting requirements for qualifying public companies. As an "emerging growth company" we may delay adoption of new or revised accounting pronouncements applicable to public companies until such pronouncements are made applicable to private companies. We are taking advantage of the benefits of this extended transition period. Accordingly, our financial statements may not be comparable to companies that comply with such new or revised accounting standards.

The estimates and judgments that management believes have the most effect on its reported financial position and results of operations are set forth within "Management's Discussion and Analysis of Financial Condition and Results of Operations" in our Annual Report on Form 10-K for the fiscal year ended December 31, 2018. There have been no significant changes in critical accounting policies or the assumptions and judgments utilized in applying these policies since those reported for the year ended December 31, 2018.

Financial Condition

As of March 31, 2019, we had approximately \$4.0 billion in total assets, \$3.1 billion in deposits, and \$477.8 million in total shareholders' equity. Total assets as of March 31, 2019 included approximately \$313.5 million of cash and cash equivalents, \$882.1 million of loans held for sale and \$2.2 billion of loans held for investment. It also includes \$129.9 million of trading securities that represent pre-sold multi-family rental real estate loan originations in primarily Government National Mortgage Association ("GNMA") mortgage backed securities pending settlements that typically

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occur within 30 days. There are \$296.7 million of available for sale securities that are match funded with related custodial deposits. There are restrictions on the types of securities, as these are funded by certain custodial deposits where we set the cost of deposits based on the yield of the related securities. Mortgage servicing rights were \$76.2 million at March 31, 2019 based on the fair value of the multi-family rental real estate loan servicing, which are primarily GNMA servicing rights with 10-year call protection.

Comparison of Financial Condition at March 31, 2019 and December 31, 2018

Total Assets. Total assets increased \$92.6 million, or 2%, to \$4.0 billion at March 31, 2019 from \$3.9 billion at December 31, 2018. The increase was due primarily to increases in net loans receivable of \$122.8 million, which were partially offset by decreases in available for sale securities of \$34.4 million and trading securities of \$33.5 million.

Cash and Cash Equivalents. Cash and cash equivalents decreased \$23.1 million, or 7%, to \$313.5 million at March 31, 2019 from \$336.5 million at December 31, 2018.

Trading Securities. Trading securities decreased \$33.5 million, or 21%, to \$129.9 million at March 31, 2019, from \$163.4 million at December 31, 2018. The trading securities represent loans that our banking subsidiary, Merchants Bank, has funded and are held pending settlement, primarily as GNMA mortgage-backed securities with a firm investor commitment to purchase the securities.

Securities Available-for-Sale. Investment securities available-for-sale decreased \$34.4 million, or 10%, to \$296.7 million at March 31, 2019 from \$331.1 million at December 31, 2018. The decrease in securities available-for-sale was primarily due to calls, maturities, sales, and repayments of securities totaling \$80.1 million during the period, partially offset by purchases of \$45.0 million. We invest in available for sale securities primarily using funds from escrow deposits held at Merchants Bank, received in connection with our multi-family mortgage servicing activities.

The available for sale securities are funded by, and paired with as to interest rates, escrow custodial deposits held at the Company on loans serviced by us. This portfolio of securities is structured to achieve a favorable interest rate spread.

Federal Home Loan Bank ("FHLB") stock. FHLB stock increased \$10.9 million, or 137%, to \$18.9 million at March 31, 2019 from \$8.0 million at December 31, 2018. The increase in FHLB stock was due primarily to our strategic shift to reduce our reliance on brokered deposits, in favor of additional borrowing that allows us to manage our liquidity more effectively. Additional stock purchases are required by the FHLB in order to facilitate increased borrowing capacity.

Loans Held for Sale. Loans held for sale, comprised primarily of single-family residential real estate loan participations, increased \$49.6 million, or 6%, to \$882.1 million at March 31, 2019 from \$832.5 million at December 31, 2018. The increase in loans held for sale was due primarily to higher volumes at the end of the quarter ended March 31, 2019.

Loans Receivable, Net. Loans receivable, net, which are comprised of loans held for investment, increased \$122.8 million, or 6%, to \$2.2 billion at March 31, 2019 compared to December 31, 2018. The increase in net loans was comprised primarily of:

- an increase of \$74.8 million, or 22%, in mortgage warehouse lines of credit, to \$412.2 million at March 31, 2019, and
- an increase of \$51.0 million, or 6%, in multi-family and healthcare financing loans, to \$965.4 million at March 31, 2019.

The increase in multi-family and healthcare financing was due to origination volume in excess of paydowns during the three months ended March 31, 2019. The increase in mortgage warehouse lines of credit was despite an industry

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decline in volume. There was a 5.0% industry decline in single-family residential loan volumes from the three months ended March 31, 2018 to the three months ended March 31, 2019, according to the Mortgage Bankers Association. This compares to the 6.0% increase in mortgage warehouse volumes we reported during the same period.

Mortgage Servicing Rights. Mortgage servicing rights decreased \$1.6 million, or 2%, to \$76.3 million at March 31, 2019 compared to December 31, 2018. During the three months ended March 31, 2019, originated and purchased servicing of \$1.0 million was offset by paydowns of \$1.1 million and a fair value decrease of \$1.5 million. Mortgage servicing rights are recognized in connection with sales of multi-family loans when we retain servicing of the sold loans, as well as upon purchases of loan servicing portfolios. The mortgage servicing rights are recorded and carried at fair value.

Deposits. Deposits decreased \$110.1 million, or 3%, to \$3.1 billion at March 31, 2019 from \$3.2 billion at December 31, 2018. The decrease was due to a reduction in demand accounts that reduced our reliance on brokered deposits, in favor of additional borrowing for more effective liquidity management.

Demand deposits decreased \$156.0 million, or 10%, to \$1.4 billion at March 31, 2019, savings deposits increased \$43.7 million, or 4%, to \$1.0 billion at March 31, 2019, while certificates of deposit accounts increased \$2.2 million, to \$682.7 million at March 31, 2019. The decrease in demand accounts was driven by the lower level of brokered deposits outstanding period to period. Brokered demand accounts decreased by \$250.1 million, or 83%, to \$50.1 million at March 31, 2019. Brokered certificates of deposit accounts decreased \$1.6 million, to \$576.9 million at March 31, 2019 from \$578.5 million at December 31, 2018. Brokered savings deposits increased \$20.5 million, or 19%, to \$130.1 million at March 31, 2019 from \$109.6 million at December 31, 2018. In total, brokered deposits decreased \$231.1 million, or 23%, to \$757.1 million at March 31, 2019 from \$988.2 million at December 31, 2018. Brokered deposits represented 24% of total deposits at March 31, 2019, compared with 31% at December 31, 2018.

Interest-bearing deposits decreased \$55.2 million, or 2%, to \$3.0 billion at March 31, 2019, and noninterest-bearing deposits decreased \$54.9 million, or 30%, to \$128.0 million at March 31, 2019.

Borrowings. Borrowings totaled \$338.0 million at March 31, 2019, an increase of \$142.6 million, or 73%, from December 31, 2018, in order to maintain an appropriate level of cash to fund our businesses. Depending on rates and timing, borrowing can be a more effective liquidity management alternative than utilizing brokered deposits.

Total Shareholders' Equity. Total shareholders' equity increased \$56.6 million, or 13%, to \$477.8 million at March 31, 2019 from \$421.2 million at December 31, 2018. The increase resulted primarily from the \$48.3 million increase in preferred stock associated with the issuance of 2 million shares and an increase in net income of \$10.6 million. These increases were partially offset by dividends paid on common and preferred shares of \$2.0 million and \$833,000, respectively, during the period.

Comparison of Operating Results for the Three Months Ended March 31, 2019 and 2018

General. Net income for the three months ended March 31, 2019 was \$10.6 million, a decrease of \$4.5 million, or 30%, from net income of \$15.1 million for the three months ended March 31, 2018. The decrease was due to a \$8.2 million decrease in gain on sale of loans and a \$2.8 million increase in noninterest expenses, which were partially offset by a \$4.0 million increase in net interest income and a \$1.1 million decrease in the provision for income taxes

Interest Income. Interest income increased \$10.6 million, or 37%, to \$39.7 million for the three months ended March 31, 2019, compared with the three months ended March 31, 2018. This increase was primarily attributable to a \$9.8 million increase in interest on loans and loans held for sale and a \$538,000 increase in interest on other interest-earning deposits.

The average balance of loans, including loans held for sale, during the three months ended March 31, 2019 increased \$498.7 million, or 22%, to \$2.7 billion from \$2.2 billion for the three months ended March 31, 2018, while the

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average yield on loans increased 65 basis points, to 5.09%, for the three months ended March 31, 2019, compared to 4.44% for the three months ended March 31, 2018. The increase in the average yield on loans was due to the overall increase in interest rates in the economy period to period.

The average balance of interest-earning assets and other decreased \$87.5 million, or 19%, to \$369.7 million for the three months ended March 31, 2019 from \$457.2 million for the three months ended March 31, 2018, while the average yield increased 109 basis points to 2.77% for the three months ended March 31, 2019.

The average balance of trading securities decreased \$11.6 million, or 10%, to \$109.4 million for the three months ended March 31, 2019, compared to \$121.0 million for the three months ended March 31, 2018, while the average yield increased 56 basis points to 3.87% for the three months ended March 31, 2019.

The average balance of taxable available-for-sale securities decreased \$123.8 million, or 30%, to \$292.5 million for the three months ended March 31, 2019, compared with \$416.3 million for the three months ended March 31, 2018, and the average yield increased 65 basis points to 2.15% for the three months ended March 31, 2019.

Interest Expense. Total interest expense increased \$6.6 million, or 74%, to \$15.5 million for the three months ended March 31, 2019, compared with the three months ended March 31, 2018.

Interest expense on deposits increased \$7.2 million, or 103%, to \$14.2 million for the three months ended March 31, 2019 from the three months ended March 31, 2018. The increase was attributable to a 67 basis point increase in the average cost of interest-bearing deposits, to 1.94% for the three months ended March 31, 2019 from 1.27% for the same period in 2018, and an increase in the average balance of interest-bearing deposits of \$730.9 million, or 33%, to \$3.0 billion for the three months ended March 31, 2019. The increase in the cost of deposits was primarily due to the overall increase in interest rates in the economy period to period and the increase in the average balance of interest-bearing deposits was primarily due to growth in interest-bearing checking accounts.

Interest expense on borrowings decreased \$598,000, or 31%, to \$1.3 million for the three months ended March 31, 2019 from \$1.9 million for the three months ended March 31, 2018. The decrease was due primarily to a 579 basis point decrease in the average cost of borrowings of 6.04%, compared to 11.83%, partially offset by a \$22.7 million, or 35%, increase in the average balance of borrowings outstanding for the three months ended March 31, 2018. The lower cost of borrowings was primarily due to the repayment of \$30 million of subordinated debt associated with the acquisition of NattyMac assets on December 31, 2018. Our short-term subordinated debt instruments have carried a higher cost than our other categories of borrowing, as they includes a variable interest rate equal to the one-month LIBOR rate plus an applicable margin. Additionally, our warehouse structured financing agreements provide for an additional interest payment for a portion of the earnings generated. As a result, the cost of borrowings increased from a base rate of 3.68% and 4.22%, to an effective rate of 6.04% and 11.83% for the three months ended March 31, 2019 and 2018, respectively.

Net Interest Income. Net interest income increased \$4.0 million, or 20%, to \$24.1 million for the three months ended March 31, 2019, compared with the three months ended March 31, 2018. The increase was due to a 44 basis point increase in our interest rate spread, to 2.50%, for the three months ended March 31, 2019, from 2.06% for the three months ended March 31, 2018. Also contributing to the increase was the overall growth in our interest-earning assets period to period. Our net interest margin increased 25 basis points, to 2.77%, for the three months ended March 31, 2019 from 2.52% for the three months ended March 31, 2018.

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The following table presents, for the periods indicated, information about (i) average balances, the total dollar amount of interest income from interest-earning assets and the resultant average yields; (ii) average balances, the total dollar amount of interest expense on interest-bearing liabilities and the resultant average rates; (iii) net interest income; (iv) the interest rate spread; and (v) the net interest margin. Yields have been calculated on a pre-tax basis. Nonaccrual loans are included in loans and loans held for sale.

	Three Months Ended March 31,					
	2019			2018		
	Average Balance	Interest Income/Expense	Yield/Rate	Average Balance	Interest Income/Expense	Yield/Rate
(Dollars in thousands)						
Assets:						
Interest-bearing deposits, and other	\$ 369,736	\$ 2,527	2.77 %	\$ 457,235	\$ 1,895	1.68 %
Securities available for sale - taxable	292,500	1,551	2.15 %	416,266	1,542	1.50 %
Securities available for sale - tax exempt	12,460	96	3.12 %	—	—	— %
Trading securities	109,423	1,045	3.87 %	121,029	989	3.31 %
Loans and loans held for sale	2,746,562	34,455	5.09 %	2,247,890	24,612	4.44 %
Total interest-earning assets	3,530,681	39,674	4.56 %	3,242,420	29,038	3.63 %
Allowance for loan losses	(12,704)			(9,071)		
Noninterest-earning assets	179,968			130,816		
Total assets	<u>\$ 3,697,945</u>			<u>\$ 3,364,165</u>		
Liabilities/Equity:						
Interest-bearing checking	\$ 1,314,733	6,434	1.98 %	\$ 645,339	2,425	1.52 %
Savings deposits	147,534	80	0.22 %	381,749	215	0.23 %
Money market	892,806	4,208	1.91 %	816,707	2,887	1.43 %
Certificates of deposit	618,646	3,505	2.30 %	398,992	1,489	1.51 %
Total deposits	2,973,719	14,227	1.94 %	2,242,787	7,016	1.27 %
Borrowings	88,353	1,316	6.04 %	65,635	1,914	11.83 %
Total interest-bearing liabilities	3,062,072	15,543	2.06 %	2,308,422	8,930	1.57 %
Noninterest-bearing deposits	155,218			656,284		
Noninterest-bearing liabilities	51,425			23,772		
Total liabilities	3,268,715			2,988,478		
Equity	429,230			375,687		
Total liabilities and equity	<u>\$ 3,697,945</u>			<u>\$ 3,364,165</u>		
Net interest income		<u>\$ 24,131</u>			<u>\$ 20,108</u>	
Interest rate spread			<u>2.50 %</u>			<u>2.06 %</u>
Net interest-earning assets	<u>\$ 468,609</u>			<u>\$ 933,998</u>		
Net interest margin			<u>2.77 %</u>			<u>2.52 %</u>
Average interest-earning assets to average interest-bearing liabilities			<u>115.30 %</u>			<u>140.46 %</u>

Provision for Loan Losses. We recorded a provision for loan losses of \$649,000 for the three months ended March 31, 2019, a decrease of \$757,000, over the three months ended March 31, 2018. The allowance for loan losses was \$13.4 million, or 0.61% of total loans, at March 31, 2019, compared to \$12.7 million, or 0.62% of total loans, at December 31, 2018, and \$9.7 million, or 0.62%, at March 31, 2018. Total nonperforming loans (nonaccrual and greater than 90 days late but still accruing) were \$2.6 million at March 31, 2019, compared to \$2.4 million at December 31, 2018 and \$4.9 million at March 31, 2018. Special Mention (Watch) loans were \$73.2 million at March 31, 2019, compared to \$90.6 million at December 31, 2018 and \$33.6 million at March 31, 2018. The increase compared to March 31, 2018 primarily reflected the active monitoring of certain construction projects with cost over-runs that were funded by the borrowers. The loan payments on these projects have remained current. Classified (substandard,

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doubtful and loss) loans were \$13.4 million at March 31, 2019, \$11.2 million at December 31, 2018 and \$8.6 million at March 31, 2018. Total loans greater than 30 days past due were \$6.3 million at March 31, 2019, \$3.2 million at December 31, 2018 and \$5.9 million at March 31, 2018. We had no charge-offs and \$3,000 in recoveries during the three months ended March 31, 2019. For the three months ended March 31, 2018, there were \$17,000 in charge-offs and \$5,000 in recoveries. As a percentage of nonperforming loans, the allowance for loan losses was 523.1% at March 31, 2019 compared to 526.9% at December 31, 2018 and 198.1% at March 31, 2018. The increase compared to March 31, 2018 was primarily due to the decrease in nonperforming loans.

Noninterest Income. Noninterest income decreased \$7.6 million, or 68%, to \$3.7 million for the three months ended March 31, 2019 compared to the three months ended March 31, 2018. The decrease was due to a decrease of \$8.2 million in gain on sale of loans. The gain on sale of loans amounted to \$2.6 million during the three months ended March 31, 2019, compared to \$10.9 million in the year earlier period, a decrease of 76%, due primarily to a decrease in the volume of multi-family rental real estate loan sales. The lower gain on sale of loans reflects the volatility we have reported from quarter to quarter in this business based on loan volumes, which were also negatively impacted by loan processing delays caused by the federal government shutdown in January 2019. Furthermore, loan servicing fees included a \$1.5 million decrease in the fair value of mortgage servicing rights for the three months ended March 31, 2019, compared with a decrease of \$893,000 for the three months ended March 31, 2018.

Noninterest Expense. Noninterest expense increased \$2.8 million, or 27%, to \$13.0 million for the three months ended March 31, 2019 compared to the three months ended March 31, 2018. The increase was due primarily to a \$2.1 million, or 32% increase in salaries and employee benefits. The increase in salaries and employee benefits was due primarily to an increase in the number of employees resulting from business growth and acquisitions that closed during the fourth quarter of 2018. The efficiency ratio was at 46.9% in the three months ended March 31, 2019, compared with 32.7% the first quarter of 2018.

Income Taxes. Income tax expense decreased \$1.1 million, or 24%, to \$3.5 million for the three months ended March 31, 2019 from the three months ended March 31, 2018. The decrease was due primarily to a 29% decrease in pretax income period to period. The effective tax rate was 25.1% for the three months ended March 31, 2019 and 23.7% for the three months ended March 31, 2018.

Our Segments

We operate in three primary segments: Multi-family Mortgage Banking, Mortgage Warehousing, and Banking. We believe that Merchants Bank's subsidiary, Merchants Capital Corp. ("MCC"), which operates in our Multi-Family Mortgage Banking segment, is one of the largest FHA lenders and GNMA servicers in the country based on aggregate loan principal value. As of March 31, 2019, MCC originated and acquired \$262.4 million loans during the three months ended March 31, 2019 and services or subservices \$10.3 billion. The servicing portfolio is primarily GNMA and is a significant source of our noninterest income and deposits.

Our Mortgage Warehousing segment funds agency eligible loans for non-depository financial institutions from the date of origination or purchase until the date of sale to an investor, which typically takes less than 30 days and is a significant source of our net interest income, loans, and deposits. Mortgage Warehousing has grown to fund over \$20 billion of loan principal annually since 2015. Mortgage Warehousing also provides commercial loans and collects deposits related to the mortgage escrow accounts of its customers.

The Banking segment includes retail banking, commercial lending, agricultural lending, retail and correspondent residential mortgage banking, and SBA lending. Banking operates primarily in Indiana and Illinois, except for correspondent mortgage banking which, like Multi-family Mortgage Banking and Mortgage Warehousing, is a national business. The Banking segment has a well-diversified customer and borrower base and has experienced significant growth over the past three years. These segments diversify the net income of Merchants Bank and provide synergies across the segments. The strategic opportunities include that MCC loans are funded by the Banking segment and the Banking segment provides GNMA custodial services to MCC. The securities available for sale funded by MCC

Merchants Bancorp

custodial deposits, as well as loans generated by Merchants Bank, are pledged to the FHLB to provide advance capacity during periods of high residential loan volume for mortgage warehousing. Mortgage Warehousing provides leads to correspondent residential lending in the banking segment. Retail and commercial customers provide cross selling opportunities within the banking segment. These and other synergies form a part of our strategic plan.

For the three months ended March 31, 2019 and 2018, we had total net income of \$10.6 million and \$15.1 million, respectively. Net income for our three segments for the respective periods was as follows:

	For the three months ended March 31,	
	2019	2018
	(In thousands)	
Multi-family Mortgage Banking	\$ (712)	\$ 5,484
Mortgage Warehousing	3,832	4,630
Banking	8,769	5,980
Other	(1,319)	(1,033)
Total	<u>\$ 10,570</u>	<u>\$ 15,061</u>

Multi-family Mortgage Banking. The Multi-family Mortgage Banking segment reported a net loss for the three months ended March 31, 2019, of \$712,000, a decrease of \$6.2 million, or 113%, from the \$5.5 million reported for the three months ended March 31, 2018. The decrease was due to a \$7.8 million decrease in noninterest income, primarily associated with lower gain on sale of loans. The volume of loans originated and acquired for sale in the secondary market decreased by \$217.9 million, or 90%, to \$24.4 million for the three months ended March 31, 2019 compared to the three months ended March 31, 2018. The lower volume reflected the volatility we have reported from quarter to quarter in this business and was also negatively impacted by the federal government shutdown that resulted in loan processing delays. During the three months ended March 31, 2019, noninterest income also included a \$1.5 decrease in the fair value of the mortgage servicing rights asset, compared with a \$900,000 decrease for the three months ended March 31, 2018.

Mortgage Warehousing. The Mortgage Warehousing segment reported net income for the three months ended March 31, 2019 of \$3.8 million, a decrease of \$798,000, or 17%, over the \$4.6 million reported for the three months ended March 31, 2018. The lower net income was primarily due to a \$668,000, or 9%, decrease in net interest income after provision for loan loss, associated with higher costs of deposits and a \$600,000, or 35%, increase in noninterest expense. The increase in noninterest expense was associated with higher salaries and benefits, primarily due to additional employees associated with an acquisition that were not included in the three months ending March 31, 2018, and to support planned business growth. These higher costs were partially offset by a \$267,000, or 55%, increase in noninterest income and \$203,000 decrease in income taxes. The volume of loans funded during the three months ended March 31, 2019 amounted to \$5.4 billion, an increase of \$311.8 million, or 6.0%, compared to the same period in 2018. This compared favorably to the 5.0% industry decline in single-family residential loan volumes from the three months ended March 31, 2018 to the three months ended March 31, 2019, according to the Mortgage Bankers Association.

Banking. The Banking segment reported net income for the three months ended March 31, 2019, of \$8.7 million, an increase of \$2.8 million, or 47%, over the three months ended March 31, 2018. The increase was comprised primarily of a \$4.6 million increase in net interest income after provision for loan losses, including an increase in both the average loan balance outstanding and the average yield on loans. The growth in net interest income was partially offset by an increase of \$951,000 of noninterest expenses associated with higher salaries and benefits, reflecting additional employees associated with an acquisition that were not included in the three months ending March 31, 2018. The results of FMNBP in the Banking segment during the three months ended March 31, 2019 did not make a material contribution to the increase in net income compared to the three months ended March 31, 2018.

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Liquidity and Capital Resources

Our primary sources of funds are business and consumer deposits, escrow and custodial deposits, principal and interest payments on loans, and proceeds from sale of loans. While maturities and scheduled amortization of loans are predictable sources of funds, deposit flows and mortgage prepayments are greatly influenced by market interest rates, economic conditions, and competition. Our most liquid assets are cash, short-term investments, including interest-bearing demand deposits, trading securities and loans held for sale. The levels of these assets are dependent on our operating, financing, lending, and investing activities during any given period. Our cash flows are comprised of three primary classifications: cash flows from operating activities, investing activities, and financing activities. Net cash provided by (used in) operating activities was \$2.7 million and \$(123.8) million for the three months ended March 31, 2019 and 2018, respectively. Net cash provided by (used in) investing activities, which consists primarily of net change in loans receivable and purchases, sales and maturities of investment securities, was \$(103.6) million and \$(169.2) million for the three months ended March 31, 2019 and 2018, respectively. Net cash provided by financing activities, which is comprised primarily of net change in deposits and borrowings, was \$77.7 million and \$221.2 million for the three months ended March 31, 2019 and 2018, respectively.

At March 31, 2019, we had outstanding commitments to originate loans of \$408.3 million, unused lines of credit of \$150.8 million and outstanding letters of credit of \$16.2 million. We anticipate that we will have sufficient funds available to meet our current loan origination commitments. Certificates of deposit that are scheduled to mature in less than one year from March 31, 2019 totaled \$635.6 million. Management expects that a substantial portion of the maturing certificates of deposit will be renewed. However, if a substantial portion of these deposits is not retained, we may decide to utilize FHLB advances or raise interest rates on deposits to attract new accounts, which may result in higher levels of interest expense. At March 31, 2019, based on available collateral and our ownership of FHLB stock we had access to additional FHLB advances of up to \$559.1 million.

At March 31, 2019, Merchants Bank exceeded all of its regulatory capital requirements with a Tier 1 leverage capital level of \$465.6 million, or 13.3% of adjusted total assets, which is above the required level of \$140.3 million, or 4.0%; total risk-based capital of \$478.6 million, or 14.6% of risk-weighted assets, which is above the required level of \$262.2 million, or 8.0%; and common equity Tier 1 capital of \$465.6 million, or 14.2% of risk-weighted assets, which is above the required level of \$147.5 million, or 4.5% of risk-weighted assets. Accordingly, Merchants Bank was categorized as well capitalized at March 31, 2019. Management is not aware of any conditions or events since the most recent notification that would change Merchants Bank's category.

At March 31, 2019, FMBI exceeded all of its regulatory capital requirements with a Tier 1 leverage capital level of \$19.0 million, or 11.9% of adjusted total assets, which is above the required level of \$6.4 million, or 4.0%; total risk-based capital of \$19.4 million, or 15.7% of risk-weighted assets, which is above the required level of \$9.9 million, or 8.0%; and common equity Tier 1 capital of \$19.0 million, or 15.4% of risk-weighted assets, which is above the required level of \$5.6 million, or 4.5% of risk-weighted assets. Accordingly, FMBI was categorized as well capitalized at March 31, 2019. Management is not aware of any conditions or events since the most recent notification that would change FMBI's category.

At March 31, 2019, the Company exceeded all of its regulatory capital requirements with a Tier 1 leverage capital level of \$440.0 million, or 12.0% of adjusted total assets, which is above the required level of \$146.4 million, or 4.0%; total risk-based capital of \$453.4 million, or 13.3% of risk-weighted assets, which is above the required level of \$272.1 million, or 8.0%; and common equity Tier 1 capital of \$350.2 million, or 10.3% of risk-weighted assets, which is above the required level of \$153.1 million, or 4.5% of risk-weighted assets. Management is not aware of any conditions or events since the most recent notification that would change the Company's category.

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Quantitative and Qualitative Disclosures About Market Risk

Market Risk. Market risk represents the risk of loss due to changes in market values of assets and liabilities. We incur market risk in the normal course of business through exposures to market interest rates, equity prices, and credit spreads. We have identified two primary sources of market risk: interest rate risk and price risk.

Interest Rate Risk

Our Asset-Liability Committee, or ALCO, is a management committee that manages our interest rate risk within broad policy limits established by our board of directors. In general, we seek to minimize the impact of changing interest rates on net interest income and the economic values of assets and liabilities. Our ALCO meets quarterly to monitor the level of interest rate risk sensitivity to ensure compliance with the board of directors' approved risk limits.

Income Simulation and Economic Value Analysis. Interest rate risk measurement is calculated and reported to the ALCO at least quarterly. The information reported includes period-end results and identifies any policy limits exceeded, along with an assessment of the policy limit breach and the action plan and timeline for resolution, mitigation, or assumption of the risk.

We use two approaches to model interest rate risk: Net Interest Income at Risk (NII at Risk) and Economic Value of Equity (EVE). Under NII at Risk, net interest income is modeled utilizing various assumptions for assets, liabilities, and derivatives. EVE measures the period end market value of assets minus the market value of liabilities and the change in this value as rates change. EVE is a period end measurement.

We report NII at Risk to isolate the change in income related solely to interest-earning assets and interest-bearing liabilities. The NII at Risk results reflect the analysis used quarterly by management. It models gradual -200, -100, +100 and +200 basis point parallel shifts in market interest rates, implied by the forward yield curve over the next one-year period. The following table presents NII at Risk for Merchants Bank as of March 31, 2019 and December 31, 2018.

	Net Interest Income Sensitivity			
	Twelve Months Forward			
	- 200	- 100	+ 100	+ 200
	(Dollars in thousands)			
March 31, 2019:				
Dollar change	\$ (20,752)	\$ (9,793)	\$ 8,738	\$ 17,330
Percent change	(28.7)%	(13.6)%	12.1 %	24.0 %
December 31, 2018:				
Dollar change	\$ (25,230)	\$ (11,716)	\$ 11,225	\$ 22,407
Percent change	(24.1)%	(11.2)%	10.7 %	21.4 %

Our interest rate risk management policy limits the change in our net interest income to 20% for a +/-100 basis point move in interest rates, and 30% for a +/-200 basis point move in rates. At March 31, 2019 we estimated that we are within policy limits set by our board of directors for the -200, -100, +100, and +200 basis point scenarios. The results reported as of March 31, 2019 show an asset sensitive position.

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The EVE results for Merchants Bank included in the table below reflect the analysis used quarterly by management. It models immediate -200, -100, +100 and +200 basis point parallel shifts in market interest rates.

	Economic Value of Equity Sensitivity (Shock)			
	Immediate Change in Rates			
	- 200	- 100	+ 100	+ 200
	(Dollars in thousands)			
March 31, 2019:				
Dollar change	\$ 1,254	\$ 1,151	\$ (5,385)	\$ (11,864)
Percent change	0.3 %	0.2 %	(1.1)%	(2.4)%
December 31, 2018:				
Dollar change	\$ 4,746	\$ 3,193	\$ (4,622)	\$ (9,757)
Percent change	1.1 %	0.8 %	(1.1)%	(2.3)%

Our interest rate risk management policy limits the change in our EVE to 15% for a +/-100 basis point move in interest rates, and 20% for a +/-200 basis point move in rates. We are within policy limits set by our board of directors for the -200, -100, +100 and +200 basis point scenarios. The EVE reported at March 31, 2019 projects that as interest rates increase (decrease) immediately, the economic value of equity position will be expected to decrease (increase). When interest rates rise, fixed rate assets generally lose economic value; the longer the duration, the greater the value lost. The opposite is true when interest rates fall.

ITEM 3 Quantitative and Qualitative Disclosures About Market Risk

The information required under this item is included as part of “Management’s Discussion and Analysis of Financial Condition and Results of Operations” of this Form 10-Q under the headings “Liquidity and Capital Resources” and “Interest Rate Risk.”

ITEM 4 Controls and Procedures

(a) Evaluation of disclosure controls and procedures.

Our management, under the supervision and with the participation of our Chief Executive Officer and Chief Financial Officer, evaluated the effectiveness of the design and operation of our disclosure controls and procedures (as defined in Rule 13a-15(e) and 15d-15(e) under the Exchange Act) as of the end of the period covered by this Form 10-Q. Based upon that evaluation, the Chief Executive Officer and Chief Financial Officer have concluded that, as of March 31, 2019, the Company’s disclosure controls and procedures were effective.

(b) Changes in internal control.

There has been no change made in the Company’s internal control over financial reporting during the period covered by this report that has materially affected, or is reasonably likely to materially affect, the Company’s internal control over financial reporting.

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Merchants Bancorp Part II Other Information

ITEM 1. Legal Proceedings

None.

ITEM 1A. Risk Factors

There have been no material changes from the risk factors previously disclosed in the “Risk Factors” section included in our Annual Report on Form 10-K for the fiscal year ended December 31, 2018.

ITEM 2. Unregistered Sales of Equity Securities and Use of Proceeds

None.

ITEM 3. Defaults Upon Senior Securities

None.

ITEM 4. Mine Safety Disclosures

Not applicable.

ITEM 5. Other Information

None.

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ITEM 6. Exhibits

<u>Exhibit Number</u>	<u>Description</u>
3.1	<u>First Amended and Restated Articles of Incorporation of Merchants Bancorp (incorporated herein by reference to Exhibit 3.1 to the Company's Registration Statement on Form S-1, as amended (File No. 333- 220623) filed on September 25, 2018)</u>
3.2	<u>Articles of Amendment to the First Amended and Restated Articles of Incorporation dated March 27, 2019 designating the 7.00% Fixed-to-Floating Rate Series A Non-Cumulative Perpetual Preferred Stock (incorporated by reference to Exhibit 3.2 of the registration statement on Form 8-A filed on March 28, 2019)</u>
3.3	<u>Second Amended and Restated By-Laws of Merchants Bancorp (incorporated by reference to Exhibit 3.1 of the Company's Current Report on Form 8-K filed on November 20, 2018)</u>
31.1	<u>Certification of Chief Executive Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002</u>
31.2	<u>Certification of Chief Financial Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002</u>
32	<u>Written Statement of Chief Executive Officer and Chief Financial Officer furnished pursuant to Section 906 of the Sarbanes-Oxley Act of 2002</u>
101.INS	XBRL Instance Document
101.SCH	XBRL Taxonomy Extension Schema Document
101.CAL	XBRL Taxonomy Extension Calculation Linkbase Document
101.DEF	XBRL Taxonomy Extension Definition Linkbase Document
101.LAB	XBRL Taxonomy Extension Label Linkbase Document
101.PRE	XBRL Taxonomy Extension Presentation Linkbase Document

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Merchants Bancorp
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.

Merchants Bancorp

Date: May 10, 2019

By: /s/ Michael F. Petrie
Michael F. Petrie
Chief Executive Officer

Date: May 10, 2019

By: /s/ John F. Macke
John F. Macke
Chief Financial Officer
(Principal Financial Officer)

**CERTIFICATION OF THE CHIEF EXECUTIVE OFFICER
PURSUANT TO SECTION 302 OF THE SARBANES-OXLEY ACT OF 2002**

I, Michael F. Petrie, the Chief Executive Officer of Merchants Bancorp, certify that:

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

May 10, 2019

Date

/s/Michael F. Petrie

Michael F. Petrie
Chief Executive Officer

**CERTIFICATION OF THE CHIEF FINANCIAL OFFICER
PURSUANT TO SECTION 302 OF THE SARBANES-OXLEY ACT OF 2002**

I, John F. Macke, the Principal Financial Officer of Merchants Bancorp, certify that:

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

May 10, 2019
Date

/s/John F. Macke
John F. Macke
Principal Financial Officer

**CERTIFICATION OF CHIEF EXECUTIVE OFFICER AND CHIEF FINANCIAL OFFICER
PURSUANT TO SECTION 906 OF THE SARBANES-OXLEY ACT OF 2002**

Michael F. Petrie, Chief Executive Officer, and John F. Macke, Principal Financial Officer, of Merchants Bancorp (the "Registrant"), each hereby certify, in their capacity as an officer of the Registrant that he has reviewed the quarterly report of the Registrant on Form 10-Q for the quarter ended March 31, 2019 (the "Report"), and that to the best of his knowledge:

- (1) The Report fully complies with the requirements of Sections 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 the Registrant.

May 10, 2019
Date

/s/ Michael F. Petrie
Michael F. Petrie
Chief Executive Officer

May 10, 2019
Date

/s/John F. Macke
John F. Macke
Principal Financial Officer

A signed original of this written statement required by Section 906 has been provided to the Registrant and will be retained by the Registrant and furnished to the SEC or its staff upon request.
