

July 24, 2023

Dear Shareholder,

I am pleased to share strong year-to-date net income of \$13.66 million for Merchants Financial Group, Inc. at the midway point of 2023. This earnings performance was \$956,459 ahead of our plan but slightly below 2022 performance by \$149,841.

In addition to a total team effort and all business units exceeding plan targets at mid-year, our strong credit quality and conservative approach to balance sheet management continue to drive results. This past month we reversed \$1.0 million from our provision for Allowance for Credit Loss (ACL) because of the overall performance strength of our consolidated loan portfolio. This would not be possible without the intense focus on the credit culture of the Company while continuing to foster meaningful loan growth in alignment with our mission of providing access to capital in the form of loans throughout our service footprint.

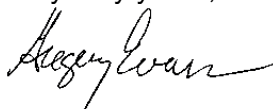
Key performance and balance sheet highlights include:

- We continued to experience loan growth in the second quarter. Total net loans are now \$2.0 billion. While this is a 20.1% year-over-year increase, loan growth moderated and was 3.4% compared to the end of the first quarter. Our commercial loan new business pipeline has softened, so we expect loan growth to taper through the balance of the year.
- Our deposit franchise remains strong; year-over-year deposit runoff has been 10.3% as we managed pricing in alignment with our excess liquidity and municipal customers sought higher-yielding options for excess cash elsewhere. Total deposits are \$2.1 billion, a decline for the quarter of 3.9%.
- Our balance sheet position remains healthy with a loan-to-deposit ratio of 95.2% and the investment portfolio well positioned to provide liquidity management flexibility as necessary.
- With our excess liquidity having been deployed to support significant loan growth over the past six quarters, the rising cost of deposits to fund future loan growth is expected to negatively impact interest margins. However, we expect continued strong performance through the balance of 2023.

I want you to know how much we appreciate the loyalty of our Shareholder base. Because the majority of our Shareholders are local to our service footprint, many of you are loyal Bank depositors and we value the account relationships you maintain. Thank you for your support in allowing us to provide the access to capital in the form of quality loans that makes our local economies vibrant. If you are not already a deposit customer with our Bank, please know that we would be thrilled to have the opportunity to serve your needs.

It's my sincere hope that you have a fun and relaxing balance of summer, and are afforded every opportunity to enjoy this beautiful region we call home. I am grateful for your continued support as we carry out our mission to fulfill the hopes and dreams of our customers.

Very truly yours,



Gregory M. Evans
President and CEO

Merchants Financial Consolidated

Consolidated Statements of Financial Condition

Unaudited

(\$ in thousands, except share data)

	<u>June 30, 2023</u>	<u>December 31, 2022</u>
<u>ASSETS</u>		
Cash and cash equivalents	36,335	225,701
Federal funds sold	365	277
Available-for-sale securities	199,590	276,621
Held-to-maturity securities	40,643	37,070
Loans held for sale	8,501	6,202
Loans and direct financing leases, net	1,990,583	1,852,035
Operating lease assets	21,532	21,558
Premises and equipment	26,062	26,388
Investment in restricted stock	8,256	7,163
Other real estate and other personal property owned	787	806
Accrued interest receivable and other assets	26,405	13,976
Cash value of life insurance	58,940	58,197
Mortgage servicing rights, net	15,718	16,641
Goodwill	35,665	35,665
Intangibles	530	797
Deferred tax assets	-	1,275
Total assets	<u><u>2,469,913</u></u>	<u><u>2,580,373</u></u>
<u>LIABILITIES AND STOCKHOLDERS' EQUITY</u>		
<u>Liabilities</u>		
<u>Deposits</u>		
Noninterest-bearing	526,583	635,853
Interest-bearing	1,572,443	1,621,448
Total deposits	<u>2,099,026</u>	<u>2,257,301</u>
Federal funds purchased	39,230	-
Repurchase agreements	12,147	12,019
Notes payable	7,160	12,120
Subordinated debentures	41,254	41,254
Deferred tax liability	2,676	3,233
Accrued interest payable and other liabilities	17,812	13,286
Total liabilities	<u>2,219,306</u>	<u>2,339,213</u>
<u>Stockholders' Equity</u>		
Common stock, par value \$.025 per share	68	68
Additional paid-in-capital	10,255	10,255
Retained earnings	264,086	254,087
Accumulated other comprehensive gain	(15,450)	(14,899)
Unearned ESOP shares	(8,352)	(8,352)
Total stockholders' equity	<u>250,607</u>	<u>241,159</u>
Total liabilities and stockholders' equity	<u><u>2,469,913</u></u>	<u><u>2,580,373</u></u>

Merchants Financial Consolidated

Consolidated Statements of Income

Unaudited

(\$ in thousands, except share data)

	<u>June 30, 2023</u>	<u>June 30, 2022</u>
<u>INTEREST INCOME:</u>		
Loan interest	43,969	33,032
Loan fees	3,874	5,141
Securities	3,831	1,961
Direct financing leases	816	1,301
Other income	<u>3,464</u>	<u>2,243</u>
Total interest income	55,954	43,678
<u>INTEREST EXPENSE:</u>		
Deposits	10,487	2,350
Notes payable, federal funds purchased and repurchase agreements	267	127
Subordinated debentures	<u>1,389</u>	<u>868</u>
Total interest expense	<u>12,143</u>	<u>3,345</u>
	-	
Net interest income	43,811	40,333
	-	
Provision for loan and lease losses	<u>488</u>	<u>(1,390)</u>
	-	
Net interest income after provision for loan and lease losses	43,323	41,724
<u>NON-INTEREST INCOME:</u>		
Trust department	1,125	1,027
Service charges and other fees	3,168	2,573
Loan servicing fees	3,534	3,611
Net gain on sale of available-for sale securities	(134)	-
Net gain on sale of loans	521	1,607
Net gain(loss) on sale of other real estate & other personal prop.	(23)	0
Other income	<u>3,995</u>	<u>3,422</u>
Total Non-interest income	12,185	12,240
<u>NON-INTEREST EXPENSE:</u>		
Salaries and employee benefits	19,887	19,404
Occupancy	8,839	7,912
Net loss on disposal of premises and equipment	-	15
Mortgage servicing rights	1,400	1,774
Other expense	<u>6,817</u>	<u>6,010</u>
Total non-interest expense	<u>36,943</u>	<u>35,116</u>
Income before income taxes	18,564	18,848
Provision for income taxes	<u>4,900</u>	<u>5,034</u>
Net income	<u>13,664</u>	<u>13,814</u>

Merchants Financial Consolidated

Consolidated Financial Highlights

Second Quarter 2023

Unaudited

(\$ in thousands, except share data)	Quarterly					Year to Date	
	2nd Qtr 2023	1st Qtr 2023	4th Qtr 2022	3rd Qtr 2022	2nd Qtr 2022	June 30, 2023	June 30, 2022
\$ Earnings							
Net Interest Income	\$ 21,313	22,497	24,889	23,451	20,829	43,811	40,333
Provision (Reversal) for loan loss	\$ (489)	977	(390)	(496)	206	488	(1,390)
Other non-interest income	6,517	5,691	6,802	6,380	6,198	12,185	12,240
Security gains/losses	\$ 114	(248)	-	-	-	(134)	-
Other non-interest expense	19,541	17,426	21,228	19,033	18,018	36,967	35,116
Pre-tax income	\$ 8,778	9,786	10,852	11,294	8,805	18,564	18,848
Taxes	2,298	2,602	2,542	2,994	2,339	4,900	5,034
Net Income	\$ 6,480	7,184	8,310	8,300	6,466	13,664	13,814
Pre-tax, pre-provision earnings	\$ 8,289	10,763	10,462	10,798	9,010	19,052	17,458
Earnings per share	\$ 0.79	0.88	1.02	1.01	0.79	1.67	1.69
Performance Ratios							
Return on average assets	1.05%	1.14%	1.26%	1.27%	0.95%	1.09%	1.00%
Return on average equity	10.49%	11.97%	14.14%	14.93%	11.26%	11.22%	12.07%
Yield on earning assets	5.08%	4.79%	4.63%	4.20%	3.54%	4.93%	3.41%
Cost of funds (inc non-int bearing deposits)	1.73%	1.20%	0.76%	0.39%	0.33%	1.46%	0.35%
Net interest margin	3.81%	3.92%	3.75%	3.61%	3.05%	3.87%	2.92%
Efficiency ratio	69.41%	60.89%	66.16%	62.77%	65.31%	65.12%	65.63%
Net overhead ratio	3.05%	2.65%	3.09%	2.78%	2.49%	2.85%	2.42%
Capital							
Tier 1 leverage capital ratio	11.47%	10.99%	10.11%	9.80%	9.43%	11.47%	9.43%
Common equity risk-based capital ratio	10.14%	10.28%	10.21%	10.25%	12.40%	10.14%	12.40%
Tier 1 risk-based capital ratio	11.83%	12.02%	11.99%	12.09%	14.69%	11.83%	14.69%
Total risk-based capital ratio	12.84%	13.27%	13.24%	13.34%	15.94%	13.08%	15.94%
Tangible capital to tangible assets	8.76%	8.47%	7.98%	7.60%	7.34%	8.76%	7.34%
Book value per share	\$ 30.64	30.32	29.49	28.61	28.15	30.64	28.15
Tangible book value per share	\$ 24.29	23.91	22.99	22.08	21.58	24.29	21.58
Outstanding shares	8,178,741	8,178,741	8,178,741	8,178,741	2,726,247	8,178,741	2,726,247
Asset Quality							
Net charge-offs (recoveries) YTD	\$ 211	277	264	164	30	211	30
Net charge-offs (recoveries) to average loans	0.01%	0.01%	0.01%	0.01%	0.00%	0.01%	0.00%
Allowance for loan losses	23,899	24,008	26,110	26,600	27,230	23,899	27,230
Allowance to total loans	1.18%	1.23%	1.39%	1.48%	1.61%	1.18%	1.61%
Allowance to total loans (excluding PPP loans)	1.18%	1.23%	1.39%	1.48%	1.62%	1.18%	1.62%
Nonperforming loans (Non-accrual & 90 days Past Due)	\$ 6,442	7,712	8,523	10,735	12,874	6,442	12,874
Other real estate owned	\$ 787	866	806	803	1,034	787	1,034
Nonperforming loans to total loans	0.32%	0.39%	0.45%	0.60%	0.76%	0.32%	0.76%
Nonperforming assets to total assets	0.29%	0.34%	0.36%	0.44%	0.53%	0.29%	0.53%
End of Period Balances							
Assets	\$ 2,469,913	2,519,186	2,580,373	2,610,794	2,647,781	2,469,913	2,647,781
Earning Assets	\$ 2,244,271	2,304,601	2,364,994	2,397,498	2,440,300	2,244,271	2,440,300
Total investments	\$ 308,702	323,459	379,396	349,991	328,707	308,702	328,707
Total loans	\$ 2,022,958	1,957,515	1,884,384	1,799,929	1,692,173	2,022,958	1,692,173
Paycheck Protection Program loans	\$ -	575	980	3,307	10,112	-	10,112
Intangible assets	\$ 51,913	52,470	53,103	53,480	53,730	51,913	53,730
Deposit	\$ 2,099,026	2,183,447	2,257,301	2,301,431	2,340,997	2,099,026	2,340,997
Customer repurchase agreements	\$ 12,147	15,020	12,019	6,450	14,923	12,147	14,923
Borrowings	\$ 7,160	11,660	12,120	12,040	12,040	7,160	12,040
Shareholders' Equity	\$ 250,607	248,011	241,159	234,028	230,234	250,607	230,234
Average Balances							
Assets	\$ 2,473,264	2,562,819	2,623,438	2,594,556	2,733,221	2,517,795	2,778,648
Earning Assets	\$ 2,257,859	2,349,958	2,408,189	2,389,460	2,528,827	2,303,654	2,577,192
Total investments	\$ 311,096	373,068	368,803	336,860	305,710	341,911	296,009
Total loans	\$ 1,967,528	1,910,675	1,825,894	1,680,303	1,660,766	1,939,258	1,640,772
Paycheck Protection Program loans	\$ 287	778	2,144	6,710	15,299	287	15,299
Intangible assets	\$ 52,123	52,756	53,231	53,507	53,615	52,438	53,468
Deposit	\$ 2,137,709	2,237,256	2,308,114	2,355,357	2,422,069	2,187,208	2,466,671
Customer repurchase agreements	\$ 12,359	11,470	12,197	11,173	9,935	11,917	8,863
Borrowings	\$ 10,720	11,668	12,043	12,040	14,265	11,192	14,402
Shareholders' Equity	\$ 247,898	243,384	233,103	220,500	230,249	245,654	230,789
Stock Valuation							
Closing Market Price (OTCPink)	\$ 26.00	27.90	29.10	27.00	25.50	26.00	25.50
Multiple of Tangible Book Value	1.07	1.17	1.27	1.22	1.18	1.07	1.18

**Previous quarter per share data restated to reflect May 13, 2022 Stock Split