

October 24, 2019

Dear Shareholder,

I am pleased to report strong third quarter results for Merchants Financial Group, Inc. (MFGI) with year-to-date consolidated net income of \$14.46 million through September. This is \$2.64 million ahead of plan and \$673,000 above 2018. Our confidence in the sustainability of our earnings growth resulted in your Board of Directors declaring an increase in our semi-annual dividend to \$0.75/share, an increase of \$0.05 (7.1%) from our June payment. This dividend will be paid on December 20, 2019 to Shareholders of record as of November 22, 2019.

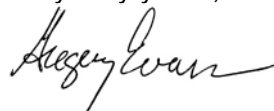
A significant impact to our quarterly performance and strategic progress includes the addition of the First National Bank of Northfield to Merchants Financial Group, Inc. The purchase was finalized on August 30, and First National's earnings were officially included in our September results, contributing nearly \$200,000 in income. Our team at Merchants has now been bolstered by an incredible team in Northfield and we're proud to have them officially under the Merchants umbrella. It should be noted that before adding Northfield's income into our consolidated earnings report, Merchants was \$2.5 million ahead of plan and \$475,000 ahead of 2018.

As always, our performance is the result of a total team effort across the company. All four of our Bank regions are ahead of plan year-to-date, as is our Secondary Market Mortgage division. Key performance highlights for the third quarter included:

- Our emphasis on credit quality and mitigation of risk continues to make a difference. Our quarterly analysis of Allowance for Loan/Lease Loss Provision revealed a surplus of reserves and we were able to take approximately \$385,000 back into income at the end of September.
- As a result of the significant drop in mortgage rates over the past few weeks, our mortgage volume has exploded. Our current mortgage loan pipeline exceeds \$140 million, which is the highest we've experienced since 2013. This activity in one of our key lines of business and should contribute to a strong performance finish for 2019.
- We remain intensely focused on strategic execution associated with enhancing our digital banking solutions, including introducing digital wallet capabilities and launching enhanced online and mobile banking platforms in the near future.

I'm looking forward to a strong finish for the year and continued progress on many strategic initiatives we've set out to accomplish. I know none of this can be achieved without your support and the customers we are privileged to serve. Our entire team remains committed to delivering value-added care and attention to our customers, which is ultimately what drives Merchants' continued success. Thank you for your continued loyalty.

Very truly yours,

A handwritten signature in black ink, appearing to read 'Gregory Evans', written in a cursive style.

Gregory M. Evans
President and CEO

Balance Sheet Highlights

Period-end	September 30, 2019	September 30, 2018 *	Variance	June 30, 2019	Variance
Assets					
Cash & Fed Funds	\$ 109,822,890	\$ 44,671,355	145.85%	\$ 42,272,935	159.79%
Investments	147,846,463	141,969,823	4.14%	130,676,964	13.14%
Net Loans	1,695,723,549	1,396,366,793	21.44%	1,501,164,125	12.96%
Intangible assets	39,521,743	23,188,400	70.44%	23,060,516	71.38%
Other assets	110,085,078	101,416,152	8.55%	99,192,728	10.98%
Total Assets	2,102,999,723	1,707,612,523	23.15%	1,796,367,268	17.07%
Liabilities & Equity					
Deposits	1,800,873,533	1,410,866,679	27.64%	1,477,855,878	21.86%
Trust Preferred Securities	41,254,000	41,254,000	0.00%	41,254,000	0.00%
Other Liabilities	69,203,471	82,729,034	-16.35%	91,111,096	-24.04%
Equity	191,668,719	172,762,810	10.94%	186,146,294	2.97%
Total Liabilities & Equity	2,102,999,723	1,707,612,523	23.15%	1,796,367,268	17.07%
*Restated to align with audit reclassifications					

Income Statement Highlights

	Nine months ended			2019 Per Quarter Results			Year Ended	
	September 30, 2019	September 30, 2018 *	Variance	Third Quarter	Second Quarter	First Quarter	December 31, 2018	9 Mo %
	Actual	Actual		Actual	Actual	Actual	Actual	of YE
Income								
Investments & Funds Sold	\$ 3,275,419	\$ 3,250,498	0.77%	\$ 1,109,458	\$ 1,063,547	\$ 1,102,414	\$ 4,395,508	74.52%
Loan Interest	58,666,669	49,982,701	17.37%	20,676,852	19,850,937	18,138,880	66,871,564	87.73%
Total Interest Income	61,942,088	53,233,199	16.36%	21,786,310	20,914,484	19,241,294	71,267,072	86.92%
Interest Expense	(10,216,836)	(6,372,377)	60.33%	(3,666,619)	(3,451,686)	(3,098,531)	(9,260,759)	110.32%
Net Interest Income	51,725,252	46,860,822	10.38%	18,119,691	17,462,798	16,142,763	62,006,313	83.42%
Non-interest Income	17,345,845	16,883,768	2.74%	6,539,688	5,836,555	4,969,603	23,964,946	72.38%
Non-interest expense	(47,725,725)	(44,761,288)	6.62%	(16,982,093)	(14,977,968)	(15,765,665)	(59,922,746)	79.65%
Provision expense	(1,711,909)	(354,017)	383.57%	(73,803)	(973,003)	(665,103)	(811,155)	211.05%
Pretax Income	19,633,463	18,629,285	5.39%	7,603,483	7,348,382	4,681,598	25,237,358	77.80%
Taxes	(5,175,000)	(4,844,000)	6.83%	(2,073,000)	(1,893,000)	(1,209,000)	(6,350,050)	81.50%
Net Income	14,458,463	13,785,285	4.88%	5,530,483	5,455,382	3,472,598	18,887,308	76.55%
*Restated to align with audit reclassifications								

Bank Yield and Margin Highlights

	September 30, 2019		June 30, 2019		September 30, 2018	
	Balances	Rate	Balances	Rate	Balances	Rate
Earning Assets						
Fed Funds Excess	\$ 39,085,370	1.78%	\$ -	0.00%	\$ -	0.00%
Investments	\$ 202,912,931	2.91%	\$ 177,911,261	2.90%	\$ 188,417,413	3.02%
Loans	\$ 1,643,915,845	4.47%	\$ 1,450,793,588	4.40%	\$ 1,348,698,371	4.24%
OREO & Non-accrual	\$ 26,568,239	0.00%	\$ 26,236,621	0.00%	\$ 26,305,542	0.00%
Earning Assets Total	\$ 1,912,482,385	4.19%	\$ 1,654,941,470	4.17%	\$ 1,563,421,326	4.02%
Paying Liabilities						
Non-interest deposits	\$ 443,215,721	0.00%	\$ 337,838,684	0.00%	\$ 336,288,495	0.00%
Interest deposits	\$ 1,357,881,240	0.97%	\$ 1,140,520,901	0.96%	\$ 1,075,209,524	0.69%
Non-core deposits	\$ 16,053,232	1.14%	\$ 14,325,485	0.98%	\$ 17,744,047	0.72%
Borrowings	\$ 27,000,000	2.18%	\$ 22,000,000	2.30%	\$ 10,000,000	2.55%
Fed Funds Purchased	\$ -	0.00%	\$ 13,161,883	2.54%	\$ 24,993,446	2.37%
Paying Liabilities Total	\$ 1,844,150,193	0.76%	\$ 1,527,846,953	0.78%	\$ 1,464,235,512	0.57%
Net Interest Spread		3.43%		3.39%		3.45%

Credit Quality Ratios

Period ended	September 30, 2019	June 30, 2019	March 31, 2019
Classified Loans to Total Loans	4.52%	4.07%	4.41%
Criticized Loans to Total Loans	7.25%	6.35%	6.51%
Classified Loans to Capital	31.52%	26.52%	28.53%
Criticized Loans to Capital	50.59%	41.32%	42.12%
Non-accrual Loans to Total Loans *	1.94%	1.65%	1.85%
Past Due > 90 days to Total Loans *	0.00%	0.00%	2.00%
Net Charge-offs to Total Loans *	0.10%	0.03%	0.00%
Loss Reserve to Total Loans *	1.23%	1.30%	1.30%

* Total loans includes held for sale and operating leases

Key Ratios

Period-end	September 30, 2019	September 30, 2018	June 30, 2019	March 31, 2019	December 31, 2018
<u>Internal Ratios</u>					
Return on Average Assets	0.96%	1.08%	1.00%	0.81%	1.10%
Return on Ending Equity	10.09%	10.48%	9.60%	7.60%	10.51%
Efficiency Ratio	67.86%	69.20%	68.18%	73.90%	68.83%
Net Interest Margin	3.77%	4.09%	4.13%	4.07%	4.04%
Common Equity Tier 1	10.29%	9.92%	10.13%	10.32%	10.11%
Tier 1 Capital Ratio	12.61%	12.40%	12.49%	12.77%	12.56%
Total Capital Ratio	13.70%	13.54%	13.65%	13.94%	13.69%
Tier 1 Leverage Ratio	11.44%	11.85%	12.04%	12.18%	11.93%
<u>Investor Ratios</u>					
Number of Shares Outstanding	2,726,247	2,726,247	2,726,247	2,726,247	2,726,247
YTD Earnings Per Share	5.30	5.06	3.27	1.27	6.93
Book Value Per Share	70.30	63.37	68.28	66.75	65.19
Tangible Book Value (TBV)	57.22	54.44	59.82	58.29	56.73
Share price	72.75	77.00	72.50	75.00	71.50
Price to TBV	127.13%	141.45%	121.20%	128.67%	126.04%

*Ratios with shares use outstanding shares versus GAAP weighted average shares