FARMERS & MERCHANTS BANCORP INC
Form 10-Q
May 01, 2019
UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

WASHINGTON, D.C. 20549

FORM 10 Q

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

For the quarterly period 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 Number 001-38084

FARMERS & MERCHANTS BANCORP, INC.

(Exact name of registrant as specified in its charter)

OHIO	34-1469491
(State or other jurisdiction of incorporation or organization)	(IRS Employer Identification No.)

307 North Defiance Street, Archbold, Ohio	43502
(Address of principal executive offices)	(Zip Code)

(419) 446-2501

Registrant’s telephone number, including area code

(Former name, former address and former fiscal year, if changed since last report.)

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or Section 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days.
Yes No

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

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

Large accelerated filer	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.

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

Yes No

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

Common Stock, No Par Value	11,106,183
Class	Outstanding as of April 26, 2019

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10Q

FARMERS & MERCHANTS BANCORP, INC.

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101.INS	XBRL Instance Document (1)
101.SCH	XBRL Taxonomy Extension Scheme Document (1)
101.CAL	XBRL Taxonomy Extension Calculation Linkbase Document (1)
101.DEF	XBRL Taxonomy Extension Definition Linkbase Document (1)
101.LAB	XBRL Taxonomy Extension Label Linkbase Document (1)
101.PRE	XBRL Taxonomy Extension Presentation Linkbase Document (1)

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

ITEM 1 FINANCIAL STATEMENTS

FARMERS & MERCHANTS BANCORP, INC. AND SUBSIDIARIES

CONDENSED CONSOLIDATED BALANCE SHEETS

	(in thousands of dollars) March 31, 2019 (Unaudited)	December 31, 2018
Assets		
Cash and due from banks	$48,740	$ 37,492
Federal funds sold	33,109	873
Total cash and cash equivalents	81,849	38,365
Interest-bearing time deposits	4,509	4,019
Securities - available-for-sale	174,682	168,447
Other securities, at cost	5,789	3,679
Loans held for sale	859	495
Loans, net	1,091,829	839,599
Premises and equipment	25,205	22,615
Goodwill	47,340	4,074
Mortgage servicing rights	2,397	2,385
Other real estate owned	510	600
Bank owned life insurance	14,963	14,884
Other assets	15,729	17,001
Total Assets	$1,465,661	$ 1,116,163
Liabilities and Stockholders' Equity		
Liabilities		
Deposits		
Noninterest-bearing	$236,847	$ 215,422
Interest-bearing		
NOW accounts	418,773	298,254
Savings	272,875	227,701
Time	258,929	187,413
Total deposits	1,187,424	928,790
Federal funds purchased and securities sold under agreements to repurchase	25,521	32,181
Federal Home Loan Bank (FHLB) advances	24,682	-
Dividend payable	1,654	1,379
Accrued expenses and other liabilities	9,446	10,526
Total liabilities	1,248,727	972,876
Commitments and Contingencies		
Stockholders' Equity		
Common stock - No par value 20,000,000 shares authorized; issued and outstanding 12,230,000 shares 3/31/19, 10,400,000 shares 12/31/18	81,760	10,823
Treasury stock - 1,122,937 shares 3/31/19, 1,114,739 shares 12/31/18	(12,680)	(12,409)
Retained earnings	149,466	147,887

Accumulated other comprehensive loss	(1,612)	(3,014)
Total stockholders' equity	216,934	143,287
Total Liabilities and Stockholders' Equity	$1,465,661	$ 1,116,163

See Notes to Condensed Consolidated Unaudited Financial Statements.

Note: The December 31, 2018, Condensed Consolidated Balance Sheet has been derived from the audited Consolidated Balance Sheet as of that date.

FARMERS & MERCHANTS BANCORP, INC. AND SUBSIDIARIES

CONDENSED CONSOLIDATED STATEMENTS OF INCOME

(Unaudited)

	(in thousands of dollars, except per share data) Three Months Ended	
	March 31, 2019	March 31, 2018
Interest Income		
Loans, including fees	$ 14,680	$ 10,102
Debt securities:		
U.S. Treasury and government agencies	713	623
Municipalities	211	281
Dividends	88	55
Federal funds sold and other	170	75
Total interest income	15,862	11,136
Interest Expense		
Deposits	2,613	1,319
Federal funds purchased and securities sold under agreements to repurchase	185	124
Borrowed funds	287	20
Total interest expense	3,085	1,463
Net Interest Income - Before Provision for Loan Losses	12,777	9,673
Provision for Loan Losses	30	40
Net Interest Income After Provision For Loan Losses	12,747	9,633
Noninterest Income		
Customer service fees	1,578	1,466
Other service charges and fees	1,041	1,012
Net gain on sale of loans	102	132
Net loss on sale of available-for-sale securities	(26)	-
Total noninterest income	2,695	2,610
Noninterest Expense		
Salaries and wages	4,312	3,310
Employee benefits	1,594	1,136
Net occupancy expense	667	387
Furniture and equipment	696	507
Data processing	1,299	331
Franchise taxes	258	239
ATM expense	447	312
Advertising	260	186
Net loss on sale of other assets owned	15	17
FDIC assessment	96	87
Mortgage servicing rights amortization	75	85
Consulting fees	113	110
Other general and administrative	1,679	933

Total noninterest expense	11,511	7,640
Income Before Income Taxes	3,931	4,603
Income Taxes	707	836
Net Income	$3,224	$ 3,767
Basic and Diluted Earnings Per Share	$0.29	$ 0.41
Dividends Declared	$0.15	$ 0.13

See Notes to Condensed Consolidated Unaudited Financial Statements

FARMERS & MERCHANTS BANCORP, INC. AND SUBSIDIARIES

CONDENSED CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME

(Unaudited)

	(in thousands of dollars) Three Months Ended	
	March 31, 2019	March 31, 2018
Net Income	$3,224	$ 3,767
Other Comprehensive Income (Loss) (Net of Tax):		
Net unrealized gain (loss) on available-for-sale securities	1,749	(2,471)
Reclassification adjustment for loss on sale of available-for-sale securities	26	-
Net unrealized gain (loss) on available-for-sale securities	1,775	(2,471)
Tax expense (benefit)	373	(519)
Other comprehensive income (loss)	1,402	(1,952)
Comprehensive Income	$4,626	$ 1,815

See Notes to Condensed Consolidated Unaudited Financial Statements

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Farmers & Merchants Bancorp, Inc. and Subsidiaries

CONDENSED Consolidated StatementS of Changes TO Stockholders' Equity

For the Three Months Ended March 31, 2018 and 2019

(000's Omitted, Except Per Share Data)

	Shares of Common Stock	Common Stock	Treasury Stock	Retained Earnings	Accumulated Other Comprehensive Income (Loss)	Total Stockholders' Equity
Balance - January 1, 2018	9,265,880	$ 11,546	$ (12,160)	$ 136,547	$ (1,826)	$ 134,107
Net income				3,767		3,767
Other comprehensive loss					(1,952)	(1,952)
Adoption of ASU 2018-02				360	(360)	-
Issuance of 100 shares of restricted stock	100	(16)	2	2		(12)
Stock-based compensation expense		160				160
Cash dividends declared - $0.13 per share				(1,193)		(1,193)
Balance - March 31, 2018	9,265,980	$ 11,690	$ (12,158)	$ 139,483	$ (4,138)	$ 134,877
Balance - January 1, 2019	9,285,261	$ 10,823	$ (12,409)	$ 147,887	$ (3,014)	$ 143,287
Net income				3,224		3,224
Other comprehensive income					1,402	1,402
Issuance of 1,830,000 shares of common stock in acquisition	1,830,000	70,437				70,437
Purchase of Treasury stock	(6,558)		(213)			(213)
Issuance of 400 shares of restricted stock (Net of Forfeitures - 2,040)	(1,640)	66	(58)	9		17
Stock-based compensation expense		434				434
Cash dividends declared - $0.15 per share				(1,654)		(1,654)
Balance - March 31, 2019	11,107,063	$ 81,760	$ (12,680)	$ 149,466	$ (1,612)	$ 216,934

See Notes to Condensed Consolidated Unaudited Financial Statements

FARMERS & MERCHANTS BANCORP, INC. AND SUBSIDIARIES

CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS (Unaudited)

	(in thousands of dollars) Three Months Ended March 31, 2019	March 31, 2018
Cash Flows from Operating Activities		
Net income	$ 3,224	$ 3,767
Adjustments to reconcile net income to net cash from operating activities:		
Depreciation	654	448
Amortization of available-for-sale securities, net	170	252
Amortization of servicing rights	75	85
Amortization of core deposit intangible	182	42
Amortization of fair value adjustments	155	2
Stock-based compensation expense	434	160
Provision for loan loss	30	40
Gain on sale of loans held for sale	(102)	(132)
Originations of loans held for sale	(8,340)	(11,626)
Proceeds from sale of loans held for sale	7,764	9,971
Loss on sale of other assets owned	15	17
Loss on sales of securities available-for-sale	26	-
Change in other assets and other liabilities, net	3,516	(4,015)
Net cash provided by (used in) operating activities	7,803	(989)
Cash Flows from Investing Activities		
Activity in available-for-sale securities:		
Maturities, prepayments and calls	1,703	2,094
Sales	11,100	-
Purchases	35	(1,308)
Sales	237	-
Change in interest-bearing time deposits	(490)	1
Proceeds from sale of other assets owned	75	5
Additions to premises and equipment	(704)	(813)
Loan originations and principal collections, net	5,301	(10,166)
Acquisition of Limberlost, net of cash received	(2,089)	-
Net cash provided by (used in) investing activities	15,168	(10,187)
Cash Flows from Financing Activities		
Net change in deposits	52,416	33,998
Net change in federal funds purchased and securities sold under agreements to repurchase	(6,660)	(16,188)
Repayment of FHLB advances	(23,651)	-
Purchase of treasury stock	(213)	-
Cash dividends paid on common stock	(1,379)	(1,193)
Net cash provided by financing activities	20,513	16,617

Net Increase in Cash and Cash Equivalents	43,484	5,441
Cash and Cash Equivalents - Beginning of year	38,365	34,467
Cash and Cash Equivalents - End of period	$ 81,849	$ 39,908

(continued)

FARMERS & MERCHANTS BANCORP, INC. AND SUBSIDIARIES

CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS (Unaudited) (Continued)

	(in thousands of dollars) Three Months Ended	
	March 31, 2019	March 31, 2018
Supplemental Information		
Cash paid during the year for:		
Interest	$2,655	$ 1,479
Income taxes	-	-
Noncash investing activities:		
Transfer of loans to other real estate owned	-	-
The Company purchased all of the capital stock of Limberlost for $78,902 on January 1, 2019. In conjunction with the acquisition, liabilities were assumed as follows:		
Fair value of assets acquired	336,380	-
Less: common stock issued	70,437	-
Cash paid for the capital stock	8,465	-
Liabilities assumed	257,478	-

See Notes to Condensed Consolidated Unaudited Financial Statements.

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

NOTE 1 BASIS OF PRESENTATION AND OTHER

The accompanying unaudited condensed consolidated financial statements have been prepared in accordance with generally accepted accounting principles for interim financial information and with the instructions for Form 10Q and Rule 10-01 of Regulation S-X; accordingly, they do not include all of the information and footnotes required by generally accepted accounting principles for complete financial statements. In the opinion of management, all adjustments, consisting of normal recurring accruals, considered necessary for a fair presentation have been included. Operating results for the three months ended March 31, 2019 are not necessarily indicative of the results that are expected for the year ended December 31, 2019. The condensed consolidated balance sheet of the Company as of December 31, 2018, has been derived from the audited consolidated balance sheet of the Company as of that date. These condensed consolidated financial statements should be read in conjunction with the consolidated financial statements and footnotes thereto included in the Company's Annual Report on Form 10-K for the year ended December 31, 2018.

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

Reclassification

Certain amounts in the 2018 condensed consolidated financial statements have been reclassified to conform with the 2019 presentation. These reclassifications had no effect on income.

NOTE 2 BUSINESS COMBINATION AND ASSET PURCHASE

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

In 2018, the Company incurred $742.1 thousand of third-party acquisition-related costs. The largest portion of the expenses recognized in 2018 related to consulting fees of $340 thousand, other general and administration expenses of $331.5 thousand and data processing expenses of $58.6 thousand. These three categories of expense accounted for

98.4% of the total acquisition expenses impacting the 2018 financial statements of the Company.

In 2019, the Company has incurred additional third-party acquisition-related costs of $1.3 million. These expenses are comprised of data processing of $891.7 thousand, employee benefits of $107.6 thousand, ATM expense of $31.4 thousand, consulting fees of $18.3 thousand and other general and administrative expense of $238.3 thousand in the Company's consolidated statement of income for the quarter ended March 31, 2019.

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

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

NOTE 2 BUSINESS COMBINATION AND ASSET PURCHASE (Continued)

Fair Value of Consideration Transferred

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

Recognized amounts of identifiable assets acquired and liabilities assumed

Assets	
Cash and cash equivalents	$ 6,376
Securities - available-for-sale	17,494
Other securities, at cost	2,347
Loans, net	257,183
Premises and equipment	2,538
Goodwill	43,266
Other assets	7,176
Total Assets Purchased	$ 336,380
Liabilities	
Deposits	
Noninterest bearing	$ 37,822
Interest bearing	168,312
Total deposits	206,134
Federal Home Loan Bank (FHLB) advances	48,196
Accrued expenses and other liabilities	3,148
Total Liabilities Assumed	$ 257,478

The fair value of the assets acquired includes loans with a fair value of $257.2 million. The gross principal and contractual interest due under the contracts is $359.2 million, of which $4.7 million is expected to be uncollectible. The loans have a weighted average life of 70 months.

The fair value of building and land included in premises and equipment was written down by $1.2 million and will be amortized based on the remaining life of each building. The combined average remaining life is 16.75 years.

The fair value for certificates of deposit incorporates a valuation amount of $0.5 million which will be amortized over 1.5 years. The fair value of Federal Home Loan Bank (FHLB) advances includes a valuation amount of $1.3 million which will be amortized over 2.3 years.

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

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

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

NOTE 2 BUSINESS COMBINATION AND ASSET PURCHASE (Continued)

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

	2019 (In Thousands)
Balance - January 1, 2019	
Commercial	$ 4,094
Consumer RE	231
Consumer	71
Carrying amount, net of allowance of $2,118	$ 2,278
Balance - March 31, 2019	
Commercial	$ 4,091
Consumer RE	231
Consumer	33
Carrying amount, net of allowance of $2,081	$ 2,274

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

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

No allowances for loan losses were reversed in 2019. The balance of the allowance for loan losses for loans acquired and accounted for under this guidance (ASC 310-30) was $2.081 million at March 31, 2019 and $2.118 million on January 1, 2019, respectively.

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

	2019 (In Thousands)
Balance - January 1, 2019	$ 2,544
Additions	1
Accretion	(109)

Reclassification from nonaccretable difference	-
Disposals	-
Balance - March 31, 2019	$ 2,436

The results of operations of Bank of Geneva have been included in the Company's consolidated financial statements since the acquisition date of January 1, 2019. The following schedule includes pro-forma results for the three months ended March 31, 2019 and 2018 as if the Bank of Geneva acquisitions had occurred as of the beginning of the comparable prior reporting period.

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

NOTE 2 BUSINESS COMBINATION AND ASSET PURCHASE (Continued)

	(in thousands of dollars, except per share data) Three Months Ended	
	March 31, 2019	March 31, 2018
Summary of Operations		
Net Interest Income - Before Provision for Loan Losses	$12,777	$ 12,639
Provision for Loan Losses	30	145
Net Interest Income After Provision For Loan Losses	12,747	12,494
Noninterest Income	2,695	2,762
Noninterest Expense	10,224	9,346
Income Before Income Taxes	5,218	5,910
Income Taxes	965	1,108
Net Income	$4,253	$ 4,802
Basic and Diluted Earnings Per Share	$0.38	$ 0.43

The pro-forma information includes adjustments for interest income on loans, amortization of intangibles arising from the transaction, interest expense on deposits acquired, premises expense for the branches acquired and the related income tax effects. The pro-forma information for the quarter ended March 31, 2019 includes approximately $2.1 million, net of tax, of operating revenue from Bank of Geneva since acquisition.

The pro-forma financial information is presented for informational purposes only and is not indicative of the results of operations that actually would have been achieved had the acquisition been consummated as of that time, nor is it intended to be a projection of future results.

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

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

The amortization expense for the three months ended March 31, 2018 was $42 thousand. Of the $727 thousand to be expensed in 2019, $182 thousand has been expensed for the three months ended March 31, 2019.

	(In Thousands)	(In Thousands)	(In Thousands)
	Custar	Geneva	Total
2019	$ 167	$ 560	$ 727
2020	161	560	721
2021	-	560	560
2022	-	560	560
2023	-	560	560
2024	-	560	560
2025	-	560	560
	$ 328	$ 3,920	$ 4,248

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

NOTE 3 SECURITIES

Mortgage-backed securities, as shown in the following tables, are all government sponsored enterprises. The amortized cost and fair value of securities, with gross unrealized gains and losses at March 31, 2019 and December 31, 2018, follows:

	(In Thousands) March 31, 2019			
	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
Available-for-Sale:				
U.S. Treasury	$23,059	$ 6	$ (182)	$22,883
U.S. Government agencies	75,289	131	(1,205)	74,215
Mortgage-backed securities	38,619	97	(822)	37,894
State and local governments	39,756	296	(362)	39,690
Total available-for-sale securities	$176,723	$ 530	$ (2,571)	$174,682

	(In Thousands) December 31, 2018			
	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
Available-for-Sale:				
U.S. Treasury	$23,078	$ 6	$ (254)	$22,830
U.S. Government agencies	71,235	2	(1,910)	69,327
Mortgage-backed securities	37,342	62	(1,142)	36,262
State and local governments	40,608	225	(805)	40,028
Total available-for-sale securities	$172,263	$ 295	$ (4,111)	$168,447

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

1. The fair value of the security has significantly declined from book value.
2. A downgrade has occurred that lowered the credit rating to below investment grade (below Baa3 by Moody and BBB – by Standard and Poors.)
3. Dividends have been reduced or eliminated or scheduled interest payments have not been made.

4. The underwater security has longer than 10 years to maturity and the loss position had existed for more than 3 years.
5. Management does not possess both the intent and ability to hold the security for a period of time sufficient to allow for any anticipated recovery in fair value.

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

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

NOTE 3 SECURITIES (Continued)

Information pertaining to securities with gross unrealized losses at March 31, 2019 and December 31, 2018, aggregated by investment category and length of time that individual securities have been in a continuous loss position follows:

	(In Thousands) March 31, 2019			
	Less Than Twelve Months		Twelve Months & Over	
	Gross Unrealized Losses	Fair Value	Gross Unrealized Losses	Fair Value
U.S. Treasury	$ -	$ -	$ (182)	$ 20,908
U.S. Government agencies	-	-	(1,205)	65,412
Mortgage-backed securities	(1)	720	(821)	29,528
State and local governments	-	-	(362)	27,792
Total available-for-sale securities	$ (1)	$ 720	$ (2,570)	$ 143,640

	(In Thousands) December 31, 2018			
	Less Than Twelve Months		Twelve Months & Over	
	Gross Unrealized Losses	Fair Value	Gross Unrealized Losses	Fair Value
U.S. Treasury	$ -	$ -	$ (254)	$ 20,861
U.S. Government agencies	-	-	(1,910)	64,727
Mortgage-backed securities	(4)	697	(1,138)	30,347
State and local governments	(22)	3,254	(783)	29,413
Total available-for-sale securities	$ (26)	$ 3,951	$ (4,085)	$ 145,348

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

Below are the gross realized gains and losses for the three months ended March 31, 2019 and March 31, 2018.

	Three Months (In Thousands) 2019	2018
Gross realized gains	$ 16	$ -
Gross realized losses	(42)	-
Net realized losses	$ (26)	$ -
Tax expense related to net realized losses	$ (5)	$ -

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

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

NOTE 3 SECURITIES (Continued)

The amortized cost and fair value of debt securities at March 31, 2019, by contractual maturity, are shown below. Expected maturities will differ from contractual maturities because borrowers may have the right to call or prepay obligations with or without call or prepayment penalties.

	(In Thousands) Amortized Cost	Fair Value
One year or less	$30,977	$30,820
After one year through five years	60,395	59,594
After five years through ten years	45,454	45,152
After ten years	1,278	1,222
Total	$138,104	$136,788
Mortgage-backed securities	38,619	37,894
Total	$176,723	$174,682

Investments with a carrying value of $83.1 million and $81.8 million at March 31, 2019 and December 31, 2018, respectively, were pledged to secure public deposits and securities sold under repurchase agreements.

Other securities include Federal Home Loan Bank of Cincinnati and Indianapolis stock as of March 31, 2019. As of December 31, 2018, other securities only includes Federal Home Loan Bank of Cincinnati stock.

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

NOTE 4 LOANS

Loan balances as of March 31, 2019 and December 31, 2018:

Loans:	(In Thousands) March 31, 2019	December 31, 2018
Consumer Real Estate	$161,180	$ 80,766
Agricultural Real Estate	192,903	68,609
Agricultural	114,920	108,495
Commercial Real Estate	441,200	419,784
Commercial and Industrial	137,936	121,793
Consumer	47,573	41,953
Industrial Development Bonds	7,384	5,889
	1,103,096	847,289
Less: Net deferred loan fees and costs	(1,133)	(915)
	1,101,963	846,374
Less: Allowance for loan losses	(6,636)	(6,775)
Less: Purchase Accounting Adjustments	(3,498)	-
Loans - Net	$1,091,829	$ 839,599

The following is a contractual maturity schedule by major category of loans as of March 31, 2019:

	(In Thousands) Within One Year	After One Year Within Five Years	After Five Years
Consumer Real Estate	$6,370	$17,260	$137,550
Agricultural Real Estate	680	6,082	186,141
Agricultural	71,544	31,632	11,744
Commercial Real Estate	18,402	169,066	253,732
Commercial and Industrial	74,195	53,787	9,954
Consumer	6,025	30,870	10,678
Industrial Development Bonds	424	291	6,669

The distribution of fixed rate loans and variable rate loans by major loan category is as follows as of March 31, 2019:

	(In Thousands)	
	Fixed Rate	Variable Rate
Consumer Real Estate	$66,857	$94,323
Agricultural Real Estate	86,756	106,147
Agricultural	41,061	73,859
Commercial Real Estate	272,827	168,373
Commercial and Industrial	54,861	83,075
Consumer	42,487	5,086
Industrial Development Bonds	7,282	102

As of March 31, 2019 and December 31, 2018 one to four family residential mortgage loans amounting to $85.5 and $14.9 million, respectively, have been pledged as security for future loans and existing loans the Bank has received from the Federal Home Loan Bank.

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

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

NOTE 4 LOANS (Continued)

The following table represents the contractual aging of the recorded investment (in thousands) in past due loans by portfolio classification of loans as of March 31, 2019 and December 31, 2018, net of deferred loan fees and costs:

March 31, 2019	30-59 Days Past Due	60-89 Days Past Due	Greater Than 90 Days	Total Past Due	Current	Total Financing Receivables	Recorded Investment > 90 Days and Accruing
Consumer Real Estate	$ 844	$ 142	$ 700	$ 1,686	$ 158,803	$ 160,489	$ -
Agricultural Real Estate	-	-	-	-	192,887	192,887	-
Agricultural	74	-	-	74	114,969	115,043	-
Commercial Real Estate	-	-	-	-	440,488	440,488	-
Commercial and Industrial	-	-	-	-	145,360	145,360	-
Consumer	77	4	35	116	47,580	47,696	-
Total	$ 995	$ 146	$ 735	$ 1,876	$ 1,100,087	$ 1,101,963	$ -

December 31, 2018	30-59 Days Past Due	60-89 Days Past Due	Greater Than 90 Days	Total Past Due	Current	Total Financing Receivables	Recorded Investment > 90 Days and Accruing
Consumer Real Estate	$ 342	$ 24	$ 254	$ 620	$ 79,612	$ 80,232	$ -
Agricultural Real Estate	-	-	-	-	68,588	68,588	-
Agricultural	-	-	-	-	108,616	108,616	-
Commercial Real Estate	-	-	-	-	419,131	419,131	-
Commercial and Industrial	-	-	-	-	127,752	127,752	-
Consumer	85	24	8	117	41,938	42,055	-
Total	$ 427	$ 48	$ 262	$ 737	$ 845,637	$ 846,374	$ -

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

NOTE 4 LOANS (Continued)

The following table presents the recorded investment in nonaccrual loans by class of loans as of March 31, 2019 and December 31, 2018:

	(In Thousands)	
	March 31, 2019	December 31, 2018
Consumer Real Estate	$1,071	$ 462
Agricultural Real Estate	-	-
Agricultural	-	-
Commercial Real Estate	-	-
Commercial & Industrial	70	72
Consumer	47	8
Total	$1,188	$ 542

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

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

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

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

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

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

Industrial Development Bonds (IDB): Funds for public improvements in the Bank’s service area. Repayment ability is based on the continuance of the taxation revenue as the source of repayment.

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

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

The risk ratings are described as follows.

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

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

NOTE 4 LOANS (Continued)

3. Two (2) Good. Desirable loans of somewhat less stature than Grade 1, but with strong financial statements. Loan supported by financial statements containing strong balance sheets, generally with a leverage position less than 1.50, and a history of profitability. Probability of serious financial deterioration is unlikely. Possessing a sound repayment source (and a secondary source), which would allow repayment in a reasonable period of time. Individual loans backed by liquid personal assets, established history and unquestionable character.
4. Three (3) Satisfactory. Satisfactory loans of average or slightly above average risk – having some deficiency or vulnerability to changing economic conditions, but still fully collectible. Projects should normally demonstrate acceptable debt service coverage. Generally, customers should have a leverage position less than 2.00. May be some weakness but with offsetting features of other support readily available. Loans that are meeting the terms of repayment.

Loans may be graded 3 when there is no recent information on which to base a current risk evaluation and the following conditions apply:

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

a. At inception, the loan was secured with collateral possessing a loan-to-value adequate to protect the Bank from loss;
b. The loan exhibited two or more years of satisfactory repayment with a reasonable reduction of the principal balance;
c. During the period that the loan has been outstanding, there has been no evidence of any credit weakness. Some examples of weakness include slow payment, lack of cooperation by the borrower, breach of loan covenants, or the business is in an industry which is known to be experiencing problems. If any of these credit weaknesses are observed, a lower risk grade is warranted.

5. Four (4) Satisfactory / Monitored. A “4” (Satisfactory/Monitored) risk grade may be established for a loan considered satisfactory but which is of average credit risk due to financial weakness or uncertainty. The loans warrant a higher than average level of monitoring to ensure that weaknesses do not advance. The level of risk in Satisfactory/Monitored classification is considered acceptable and within normal underwriting guidelines so long as the loan is given management supervision.
6. Five (5) Special Mention. Loans that possess some credit deficiency or potential weakness which deserve close attention but do not yet warrant substandard classification. Such loans pose unwarranted financial risk that if not corrected could weaken the loan and increase risk in the future. The key distinctions of a 5 (Special Mention) classification are that (1) it is indicative of an unwarranted level of risk, and (2) weaknesses are considered “potential” versus “defined” impairments to the primary source of loan repayment and collateral.
7. Six (6) Substandard. One or more of the following characteristics may be exhibited in loans classified substandard:

a. Loans which possess a defined credit weakness and the likelihood that a loan will be paid from the primary source and are uncertain. Financial deterioration is underway and very close attention is warranted to ensure that the loan is collected without loss.
b. Loans are inadequately protected by the current net worth and paying capacity of the borrower.
c. The primary source of repayment is weakened and the Bank is forced to rely on a secondary source of repayment such as collateral liquidation or guarantees.
d. Loans are characterized by the distinct possibility that the Bank will sustain some loss if deficiencies are not corrected.
e. Unusual courses of action are needed to maintain a high probability of repayment.
f. The borrower is not generating enough cash flow to repay loan principal but continues to make interest payments.
g. The lender is forced into a subordinate position or unsecured collateral position due to flaws in documentation.

h. Loans have been restructured so that payment schedules, terms and collateral represent concessions to the borrower when compared to the normal loan terms.
i. The lender is seriously contemplating foreclosure or legal action due to the apparent deterioration in the loan.
j. There is significant deterioration in the market conditions and the borrower is highly vulnerable to these conditions.

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

NOTE 4 LOANS (Continued)

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

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

NOTE 4 LOANS (Continued)

The following table represents the risk category of loans by portfolio class, net of deferred fees and costs, based on the most recent analysis performed as of March 31, 2019 and December 31, 2018:

(In Thousands)	Agricultural Real Estate	Agricultural	Commercial Real Estate	Commercial and Industrial	Industrial Development Bonds
March 31, 2019					
1-2	$42,560	$ 7,515	$ 9,985	$ 4,641	$ -
3	60,378	44,179	82,470	27,547	2,505
4	74,077	60,588	340,200	93,937	4,879
5	15,740	2,761	5,262	6,217	-
6	132	-	2,571	4,753	-
7	-	-	-	881	-
8	-	-	-	-	-
Total	$192,887	$ 115,043	$ 440,488	$ 137,976	$ 7,384

	Agricultural Real Estate	Agricultural	Commercial Real Estate	Commercial and Industrial	Industrial Development Bonds
December 31, 2018					
1-2	$ 4,442	$ 5,753	$ 4,698	$ 3,199	$ -
3	14,118	38,852	64,341	16,284	3,135
4	49,596	63,380	346,072	100,644	2,754
5	422	631	2,171	308	-
6	10	-	1,849	542	-
7	-	-	-	886	-
8	-	-	-	-	-
Total	$ 68,588	$ 108,616	$ 419,131	$ 121,863	$ 5,889

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

NOTE 4 LOANS (Continued)

For consumer residential real estate, and other, the Company also evaluates credit quality based on the aging status of the loan, as was previously stated, and by payment activity. The following tables present the recorded investment in those classes based on payment activity and assigned risk grading as of March 31, 2019 and December 31, 2018.

	(In Thousands) Consumer Real Estate March 31, 2019	Consumer Real Estate December 31, 2018
Grade		
Pass	$158,309	$ 79,121
Special Mention (5)	135	232
Substandard (6)	2,045	879
Doubtful (7)	-	-
Total	$160,489	$ 80,232

	(In Thousands) Consumer - Credit		Consumer - Other	
	March 31, 2019	December 31, 2018	March 31, 2019	December 31, 2018
Performing	$3,861	$ 3,909	$43,366	$ 38,073
Nonperforming	14	19	455	54
Total	$3,875	$ 3,928	$43,821	$ 38,127

Information about impaired loans as of March 31, 2019, December 31, 2018 and March 31, 2018 are as follows:

	March 31, 2019	(In Thousands) December 31, 2018	March 31, 2018
Impaired loans without a valuation allowance	$ 1,915	$ 1,808	$ 999
Impaired loans with a valuation allowance	254	246	607
Total impaired loans	$ 2,169	$ 2,054	$ 1,606
Valuation allowance related to impaired loans	$ 59	$ 31	$ 104
Total non-accrual loans	$ 1,188	$ 542	$ 900

Total loans past-due ninety days or more and still accruing	$ -	$ -	$ -
Quarter ended average investment in impaired loans	$ 2,135	$ 2,533	$ 1,688
Year to date average investment in impaired loans	$ 2,135	$ 1,958	$ 1,688

Additional funds of $1 thousand are available to be advanced in connection with impaired loans.

The Bank had approximately $102 thousand of its impaired loans classified as troubled debt restructured (TDR) as of March 31, 2019, $178 thousand as of December 31, 2018 and $527 thousand as of March 31, 2018. During the year to date 2019 and 2018, there were no new loans considered TDR.

For the three month period ended March 31, 2019 and 2018, there were no TDRs that subsequently defaulted after modification.

For the three month period ended March 31, 2019, there were no impaired loans classified as TDR paid off.

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

NOTE 4 LOANS (Continued)

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

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

The following tables present loans individually evaluated for impairment by class of loans for three months ended March 31, 2019 and March 31, 2018.

Three Months Ended March 31, 2019	(In Thousands) Recorded Investment	Unpaid Principal Balance	Related Allowance	QTD Average Recorded Investment	QTD Interest Income Recognized	QTD Interest Income Recognized Cash Basis
With no related allowance recorded:						
Consumer Real Estate	$648	$ 648	$ -	$ 603	$ 7	$ 1
Agricultural Real Estate	-	-	-	-	-	-
Agricultural	-	-	-	-	-	-
Commercial Real Estate	192	192	-	193	3	-
Commercial and Industrial	1,075	1,075	-	1,085	15	-
Consumer	-	-	-	-	-	-
With a specific allowance recorded:						
Consumer Real Estate	254	254	59	254	-	-
Agricultural Real Estate	-	-	-	-	-	-
Agricultural	-	-	-	-	-	-
Commercial Real Estate	-	-	-	-	-	-
Commercial and Industrial	-	-	-	-	-	-
Consumer	-	-	-	-	-	-
Totals:						
Consumer Real Estate	$902	$ 902	$ 59	$ 857	$ 7	$ 1
Agricultural Real Estate	$-	$ -	$ -	$ -	$ -	$ -

Agricultural	$ -	$ -	$ -	$ -	$ -	$ -
Commercial Real Estate	$ 192	$ 192	$ -	$ 193	$ 3	$ -
Commercial and Industrial	$ 1,075	$ 1,075	$ -	$ 1,085	$ 15	$ -
Consumer	$ -	$ -	$ -	$ -	$ -	$ -

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

NOTE 4 LOANS (Continued)

Three Months Ended March 31, 2018	(In Thousands) Recorded Investment	Unpaid Principal Balance	Related Allowance	QTD Average Recorded Investment	QTD Interest Income Recognized	QTD Interest Income Recognized Cash Basis
With no related allowance recorded:						
Consumer Real Estate	$489	$ 489	$ -	$ 492	$ 8	$ 6
Agricultural Real Estate	-	-	-	67	-	-
Agricultural	-	-	-	-	-	-
Commercial Real Estate	200	200	-	201	3	-
Commercial and Industrial	310	310	-	209	4	-
Consumer	-	-	-	-	-	-
With a specific allowance recorded:						
Consumer Real Estate	80	80	20	80	-	-
Agricultural Real Estate	-	-	-	-	-	-
Agricultural	-	-	-	-	-	-
Commercial Real Estate	418	418	42	420	4	-
Commercial and Industrial	109	109	42	219	-	-
Consumer	-	-	-	-	-	-
Totals:						
Consumer Real Estate	$569	$ 569	$ 20	$ 572	$ 8	$ 6
Agricultural Real Estate	$-	$ -	$ -	$ 67	$ -	$ -
Agricultural	$-	$ -	$ -	$ -	$ -	$ -
Commercial Real Estate	$618	$ 618	$ 42	$ 621	$ 7	$ -
Commercial and Industrial	$419	$ 419	$ 42	$ 428	$ 4	$ -
Consumer	$-	$ -	$ -	$ -	$ -	$ -

As of March 31, 2019, the Company had no foreclosed residential real estate property obtained by physical possession and $639 thousand of consumer mortgage loans secured by residential real estate properties for which foreclosure proceedings are in process according to local jurisdictions. As of March 31, 2018, the Company had $3 thousand of foreclosed residential real estate property obtained by physical possession and $49 thousand of consumer mortgage loans secured by residential real estate properties for which foreclosure proceedings were in process according to local jurisdictions.

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

NOTE 4 LOANS (Continued)

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

	(In Thousands) Three Months Ended March 31, 2019	Twelve Months Ended December 31, 2018
Allowance for Loan & Lease Losses		
Balance at beginning of year	$6,775	$ 6,868
Provision for loan loss	30	324
Loans charged off	(207)	(580)
Recoveries	38	163
Allowance for Loan & Lease Losses	$6,636	$ 6,775
Allowance for Unfunded Loan Commitments & Letters of Credit	$346	$ 274
Total Allowance for Credit Losses	$6,982	$ 7,049

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

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

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

NOTE 4 LOANS (Continued)

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

Additional analysis, presented in thousands, related to the allowance for credit losses for three months ended March 31, 2019 and March 31, 2018 in addition to the ending balances as of December 31, 2018 is as follows:

	Consumer Real Estate	Agricultural Real Estate	Agricultural	Commercial Real Estate	Commercial and Industrial	Consumer	Unfunded Loan Commitment & Letters of Credit	Unallocated	Total
Three Months Ended March 31, 2019									
ALLOWANCE FOR CREDIT LOSSES:									
Beginning balance	$ 247	$ 250	$ 768	$ 3,217	$ 1,305	$ 484			