

October 24, 2024

Dear Shareholder,

I've been consistently transparent about the challenging market environment that continues to impact both Merchants Financial Group, Inc., and the broader industry. Merchants continues to maintain a strong, profitable position while navigating in this economic cycle, but our third quarter performance results fell short of our expectations. Net income through the first three quarters of 2024 was \$14.26 million, which was \$3.92 million below our plan and \$5.84 million below performance through three quarters of 2023. While we are disappointed in the year-to-date results, our prudent disciplines at Merchants will continue to position your Company for future strength and performance.

The uncompromised confidence of the Board of Directors in our ability to continue to drive profitable performance going forward is represented in the Board's approval of the retention of our semi-annual dividend payment level at \$.36/share. This dividend will be paid on December 20 to all Shareholders of record as of November 22.

Our core bank earnings remained solid through the third quarter with the biggest variance to plan coming from identified elevated risk in our consolidated loan portfolio, primarily driven by a small number of specific credit facilities. This required an additional provision of \$4.62 million to be added to our Allowance for Credit Loss in the third quarter. Credit risk identification and mitigation is a historic strength for Merchants, consistently resulting in nominal net charge-offs. Adding to provision as risk is identified is in full alignment with our responsibility to depositors and shareholders and is critical to the expectation that we will continue to drive long-term earnings success.

Additional third quarter performance notes and highlights include:

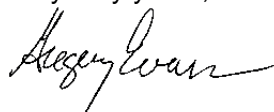
- Continued strong deposit growth; total deposits increased to \$2.33 billion, which is \$74.5 million above plan and \$179.8 million ahead of 2023 (an 8.36% increase year-over-year). I'm extraordinarily proud of our team for its intense focus on deposit growth and the performance to date.
- Total net loans declined slightly to \$2.137 billion; this is \$42 million below our plan, but growth of \$75.3 million compared to 2023. We continue to manage loan growth with intentionality, given modest identification of economic softening, uncertainty about the future interest rate environment and as appropriate to manage our liquidity.
- Our residential mortgage loan activity through three quarters continued to slightly exceed our projections, with \$199 million of production. We're hopeful that conditions in 2025 will allow for a more robust housing market and we can get back to production levels that will exceed the past two years.

While our third quarter performance is not where we would like it to be, I am confident that our 2024 results will compare favorably to the broader industry. I am grateful for your support and belief in our work as a mission-focused community bank.

On a lighter note, winter will be here before we know it. If you have plans to snowbird this winter, please share your alternate address with Becky Tiedje to ensure all stock-related mail reaches you and is not returned to the bank. You can reach Becky at shareholderrelations@merchantsbank.com or 507-457-9323. For those of you who will be changing your address with your local teller or banker, please request your address update is provided to Becky.

As we approach the end of the year and on behalf of the entire Merchants team, I wish you a wonderful holiday season.

Very truly yours,



Gregory M. Evans
President and CEO

Merchants Financial Consolidated

Consolidated Statements of Financial Condition

Unaudited

(\$ in thousands, except share data)

	<u>September 30, 2024</u>	<u>December 31, 2023</u>
<u>ASSETS</u>		
Cash and cash equivalents	119,978	39,056
Federal funds sold	330	-
Available-for-sale securities	216,756	202,215
Held-to-maturity securities	37,162	37,721
Loans held for sale	5,241	1,929
Loans and direct financing leases, net	2,130,166	2,131,813
Operating lease assets	17,903	20,469
Premises and equipment	25,051	25,728
Investment in restricted stock	5,624	9,430
Other real estate and other personal property owned	959	1,005
Accrued interest receivable and other assets	18,657	19,917
Cash value of life insurance	60,610	59,753
Mortgage servicing rights, net	14,443	15,336
Goodwill	35,665	35,665
Intangibles	100	317
Deferred tax assets	-	-
Total assets	<u>2,688,643</u>	<u>2,600,354</u>
<u>LIABILITIES AND STOCKHOLDERS' EQUITY</u>		
<u>Liabilities</u>		
Deposits		
Noninterest-bearing	473,905	482,293
Interest-bearing	<u>1,855,905</u>	<u>1,692,116</u>
Total deposits	2,329,810	2,174,409
Federal funds purchased	-	94,691
Repurchase agreements	15,060	15,065
Notes payable	17,280	7,262
Subordinated debentures	28,351	28,351
Deferred tax liability	2,530	1,617
Accrued interest payable and other liabilities	<u>18,237</u>	<u>15,024</u>
Total liabilities	2,411,268	2,336,418
<u>Stockholders' Equity</u>		
Common stock, par value \$.025 per share	68	68
Additional paid-in-capital	10,274	10,274
Retained earnings	284,486	273,170
Accumulated other comprehensive gain	(7,795)	(12,598)
Unearned ESOP shares	<u>(9,659)</u>	<u>(6,978)</u>
Total stockholders' equity	<u>277,375</u>	<u>263,936</u>
Total liabilities and stockholders' equity	<u>2,688,643</u>	<u>2,600,354</u>

Merchants Financial Consolidated

Consolidated Statements of Income

Unaudited

(\$ in thousands, except share data)

	<u>September 30, 2024</u>	<u>September 30, 2023</u>
<u>INTEREST INCOME:</u>		
Loan interest	84,467	68,953
Loan fees	4,915	5,805
Securities	5,470	5,344
Direct financing leases	1,269	1,252
Other income	2,085	4,290
Total interest income	<u>98,205</u>	<u>85,644</u>
<u>INTEREST EXPENSE:</u>		
Deposits	33,419	17,942
Notes payable, federal funds purchased and repurchase agreements	2,195	587
Subordinated debentures	1,488	2,084
Total interest expense	<u>37,103</u>	<u>20,614</u>
Net interest income	61,103	65,030
Provision for loan and lease losses	<u>6,389</u>	<u>1,531</u>
Net interest income after provision for loan and lease losses	54,714	63,499
<u>NON-INTEREST INCOME:</u>		
Trust department	1,988	1,723
Service charges and other fees	5,239	4,888
Loan servicing fees	5,148	5,270
Net gain on sale of available-for sale securities	532	(134)
Net gain on sale of loans	1,520	1,231
Net gain(loss) on sale of other real estate & other personal prop.	(6)	(23)
Other income	6,785	6,185
Total Non-interest income	<u>21,207</u>	<u>19,155</u>
<u>NON-INTEREST EXPENSE:</u>		
Salaries and employee benefits	30,022	29,933
Occupancy	14,137	13,460
Net loss on disposal of premises and equipment	-	-
Mortgage servicing rights	2,337	2,055
Other expense	10,652	10,198
Total non-interest expense	<u>57,148</u>	<u>55,646</u>
Income before income taxes	18,772	27,008
Provision for income taxes	<u>4,511</u>	<u>6,905</u>
Net income	<u>14,261</u>	<u>20,103</u>

Merchants Financial Consolidated

Consolidated Financial Highlights

Third Quarter 2024

Unaudited

	Quarterly					Year to Date	
	3rd Qtr 2024	2nd Qtr 2024	1st Qtr 2024	4th Qtr 2023	3rd Qtr 2023	September 30, 2024	September 30, 2023
(\$ in thousands, except share data)							
\$ Earnings							
Net Interest Income	\$ 21,125	20,713	19,265	20,765	21,220	61,103	65,030
Provision (Reversal) for loan loss	\$ 4,845	1,188	355	(152)	1,044	6,389	1,531
Other non-interest income	7,360	6,837	6,555	7,414	6,970	20,753	19,312
Security gains/losses	\$ -	-	532	-	-	532	(134)
Other non-interest expense	18,480	20,080	18,666	21,367	18,702	57,226	55,669
Pre-tax income	\$ 5,160	6,282	7,330	6,964	8,444	18,772	27,008
Taxes	\$ 1,133	1,497	1,881	1,565	2,005	4,511	6,905
Net Income	\$ 4,027	4,785	5,449	5,399	6,439	14,261	20,103
Pre-tax, pre-provision earnings	\$ 10,005	7,470	7,686	6,813	9,488	25,161	28,539
Earnings per share	\$ 0.49	0.58	0.67	0.66	0.79	1.74	2.46
Performance Ratios							
Return on average assets	0.60%	0.71%	0.77%	0.82%	1.02%	0.69%	1.07%
Return on average equity	5.91%	5.39%	4.13%	8.40%	10.18%	4.94%	10.86%
Yield on earning assets	5.47%	5.46%	5.22%	5.51%	5.47%	5.38%	5.29%
Cost of funds (inc non-int bearing deposits)	2.70%	2.63%	2.59%	2.37%	1.97%	2.64%	1.64%
Net interest margin	3.67%	3.70%	3.50%	3.71%	3.99%	3.98%	4.09%
Loan to Deposit Ratio	92.25%	97.29%	97.44%	98.27%	95.90%	92.25%	95.90%
Efficiency ratio	63.35%	72.18%	70.32%	74.94%	65.54%	68.57%	65.26%
Net overhead ratio	2.59%	2.88%	2.56%	3.10%	2.85%	2.67%	2.85%
Capital							
Tier 1 leverage capital ratio	11.13%	11.21%	11.20%	11.35%	11.76%	11.13%	11.76%
Common equity risk-based capital ratio	11.11%	10.78%	10.56%	10.17%	10.24%	11.11%	10.24%
Tier 1 risk-based capital ratio	12.29%	11.93%	11.70%	11.29%	11.90%	12.29%	11.90%
Total risk-based capital ratio	13.54%	13.18%	12.95%	12.54%	13.15%	13.54%	13.15%
Tangible capital to tangible assets	9.09%	9.07%	9.10%	8.84%	8.82%	9.09%	8.82%
Book value per share	\$ 33.91	33.32	32.97	32.27	31.38	33.91	31.38
Tangible book value per share	\$ 27.78	27.10	26.72	26.00	25.03	27.78	25.03
Outstanding shares	8,178,741	8,178,741	8,178,741	8,178,741	8,178,741	8,178,741	8,178,741
Average outstanding shares	8,178,741	8,178,741	8,178,741	8,178,741	8,178,741	8,178,741	8,178,741
Asset Quality							
Net charge-offs (recoveries) YTD	\$ 3,511	595	366	573	333	3,511	277
Net charge-offs (recoveries) to average loans	0.16%	0.03%	0.02%	0.03%	0.02%	0.16%	0.01%
Allowance for loan losses	29,210	26,996	25,644	25,030	24,736	29,210	24,736
Allowance to total loans	1.34%	1.22%	1.17%	1.14%	1.16%	1.34%	1.16%
Nonperforming loans (Nonaccrual & 90 days Past Due)	\$ 17,131	12,338	13,889	9,582	5,383	17,131	5,383
Other real estate owned	\$ 959	959	1,336	1,005	780	959	780
Nonperforming loans to total loans	0.79%	0.56%	0.63%	0.44%	0.25%	0.79%	0.25%
Nonperforming assets to total assets	0.67%	0.50%	0.59%	0.41%	0.24%	0.67%	0.24%
End of Period Balances							
Assets	\$ 2,690,456	2,636,537	2,594,133	2,603,726	2,521,613	2,690,456	2,521,613
Earning Assets	\$ 2,463,825	2,423,815	2,390,477	2,382,969	2,295,928	2,463,825	2,295,928
Total investments	\$ 322,646	302,119	288,772	310,638	297,284	322,646	297,284
Total loans	\$ 2,178,368	2,219,416	2,195,096	2,202,036	2,124,458	2,178,368	2,124,458
Intangible assets	\$ 50,207	50,925	51,067	51,317	51,924	50,207	51,924
Deposit	\$ 2,329,810	2,253,576	2,226,551	2,174,408	2,149,979	2,329,810	2,149,979
Customer repurchase agreements	\$ 15,060	15,063	15,057	15,065	15,029	15,060	15,029
Borrowings	\$ 17,280	17,280	6,780	7,262	7,160	17,280	7,160
Shareholders' Equity	\$ 277,375	272,538	269,633	263,936	256,635	277,375	256,635
Average Balances							
Assets	\$ 2,660,575	2,706,479	2,861,109	2,605,263	2,509,050	2,742,422	2,514,848
Earning Assets	\$ 2,587,516	2,543,818	2,519,719	2,384,629	2,289,640	2,550,487	2,298,928
Total investments	\$ 308,377	285,506	292,043	300,024	300,959	295,357	328,110
Total loans	\$ 2,191,253	2,202,839	2,173,215	2,121,982	2,048,773	2,189,110	1,976,161
Intangible assets	\$ 50,525	50,902	51,098	51,654	51,727	50,840	52,198
Deposit	\$ 2,302,998	2,246,055	2,201,175	2,248,983	2,157,232	2,250,269	2,177,106
Customer repurchase agreements	\$ 15,004	14,997	13,843	15,004	12,148	14,616	11,995
Borrowings	\$ 17,280	6,851	6,785	7,167	7,160	10,331	9,833
Shareholders' Equity	\$ 271,292	356,872	530,294	254,972	250,827	385,734	247,397
Stock Valuation							
Closing Market Price (OTCPink)	\$ 25.50	23.70	23.75	23.75	24.93	25.50	24.93
Multiple of Tangible Book Value	0.92	0.87	0.89	0.91	1.00	0.92	1.00
Price/EPS	10.61	8.78	6.16	4.20	5.00	14.62	10.14

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