

ENTERPRISE FINANCIAL SERVICES CORP
Form 10-Q
July 31, 2017

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 ended June 30, 2017.

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 001-15373

ENTERPRISE FINANCIAL SERVICES CORP

Incorporated in the State of Delaware
I.R.S. Employer Identification # 43-1706259
Address: 150 North Meramec
Clayton, MO 63105
Telephone: (314) 725-5500

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, 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 and posted on its corporate website, if any, every Interactive Data File required to be submitted and posted 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 and post such files). Yes No

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

Large accelerated filer Accelerated filer
Non-accelerated filer (Do not check if a smaller reporting company) Smaller reporting company

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act)
Yes No

As of July 26, 2017, the Registrant had 23,462,997 shares of outstanding common stock, \$0.01 par value.

This document is also available through our website at <http://www.enterprisebank.com>.

ENTERPRISE FINANCIAL SERVICES CORP AND SUBSIDIARIES
TABLE OF CONTENTS

Page
PART
I -
FINANCIAL
INFORMATION

Item
1.
Financial
Statements

Condensed
Consolidated
Balance
Sheets
(Unaudited)

Condensed
Consolidated
Statements
of 2
Operations
(Unaudited)

Condensed
Consolidated
Statements
of 3
Comprehensive
Income
(Unaudited)

Condensed
Consolidated
Statements
of 4
Shareholders'
Equity
(Unaudited)

Condensed
Consolidated
Statements
of

Cash
Flows
(Unaudited)

Notes
to
Condensed
Consolidated
Financial
Statements
(Unaudited)

Item
2.
Management's
Discussion
and
Analysis
of 29
Financial
Condition
and
Results
of
Operations

Item
3.
Quantitative
and
Qualitative
Disclosures
About
Market
Risk

Item
4.
Controls
and
Procedures

PART
II -
OTHER
INFORMATION

Item
1. 53
Legal
Proceedings

Item
1A. 53
Risk
Factors

Item
2.
Unregistered
Sales
of
Equip~~54~~
Securities
and
Use
of
Proceeds

Item
6. 54
Exhibits

Sign~~55~~atures

PART 1 - ITEM 1 - FINANCIAL STATEMENTS
ENTERPRISE FINANCIAL SERVICES CORP AND SUBSIDIARIES
Condensed Consolidated Balance Sheets (Unaudited)

(in thousands, except share and per share data)	June 30, 2017	December 31, 2016
Assets		
Cash and due from banks	\$77,815	\$ 54,288
Federal funds sold	912	446
Interest-bearing deposits (including \$2,574 and \$675 pledged as collateral)	39,037	144,068
Total cash and cash equivalents	117,764	198,802
Interest-bearing deposits greater than 90 days	1,470	980
Securities available for sale	623,857	460,797
Securities held to maturity	77,641	80,463
Loans held for sale	4,285	9,562
Loans	3,894,770	3,158,161
Less: Allowance for loan losses	41,799	43,409
Total loans, net	3,852,971	3,114,752
Other real estate	529	980
Other investments, at cost	26,477	14,840
Fixed assets, net	33,987	14,910
Accrued interest receivable	11,923	11,117
State tax credits held for sale (including \$1,274 and \$3,585 carried at fair value)	35,247	38,071
Goodwill	116,186	30,334
Intangible assets, net	12,458	2,151
Other assets	123,901	103,569
Total assets	\$5,038,696	\$ 4,081,328
Liabilities and Shareholders' Equity		
Demand deposits	\$1,019,064	\$ 866,756
Interest-bearing transaction accounts	803,104	731,539
Money market accounts	1,306,051	1,050,472
Savings	199,950	111,435
Certificates of deposit:		
Brokered	133,606	117,145
Other	459,476	356,014
Total deposits	3,921,251	3,233,361
Subordinated debentures and notes (net of debt issuance cost of \$1,201 and \$1,267)	118,080	105,540
Federal Home Loan Bank advances	200,992	—
Other borrowings	217,180	276,980
Accrued interest payable	1,459	1,105
Other liabilities	30,981	77,244
Total liabilities	4,489,943	3,694,230
Shareholders' equity:		
Preferred stock, \$0.01 par value;		
5,000,000 shares authorized; 0 shares issued and outstanding	—	—
Common stock, \$0.01 par value; 30,000,000 shares authorized; 23,746,748 and 20,306,353	237	203
shares issued		
Treasury stock, at cost; 261,718 shares	(6,632	) (6,632)

Edgar Filing: ENTERPRISE FINANCIAL SERVICES CORP - Form 10-Q

Additional paid in capital	348,217	213,078
Retained earnings	206,602	182,190
Accumulated other comprehensive income (loss)	329	(1,741)
Total shareholders' equity	548,753	387,098
Total liabilities and shareholders' equity	\$5,038,696	\$4,081,328

See accompanying notes to consolidated financial statements.

1

ENTERPRISE FINANCIAL SERVICES CORP AND SUBSIDIARIES

Condensed Consolidated Statements of Operations (Unaudited)

(in thousands, except per share data)	Three months ended June 30,		Six months ended June 30,	
	2017	2016	2017	2016
Interest income:				
Interest and fees on loans	\$47,307	\$34,183	\$87,233	\$66,791
Interest on debt securities:				
Taxable	3,585	2,397	6,815	4,784
Nontaxable	304	328	690	660
Interest on interest-bearing deposits	234	58	364	119
Dividends on equity securities	112	67	180	139
Total interest income	51,542	37,033	95,282	72,493
Interest expense:				
Interest-bearing transaction accounts	523	329	1,198	635
Money market accounts	1,938	1,013	3,431	2,019
Savings accounts	125	63	207	123
Certificates of deposit	1,373	1,183	2,588	2,202
Subordinated debentures and notes	1,288	361	2,452	709
Federal Home Loan Bank advances	522	191	852	373
Notes payable and other borrowings	140	110	279	221
Total interest expense	5,909	3,250	11,007	6,282
Net interest income	45,633	33,783	84,275	66,211
Provision for portfolio loan losses	3,623	716	5,156	1,549
Provision reversal for purchased credit impaired loan losses	(207)	(336)	(355)	(409)
Net interest income after provision for loan losses	42,217	33,403	79,474	65,071
Noninterest income:				
Service charges on deposit accounts	2,816	2,188	5,326	4,231
Wealth management revenue	2,054	1,644	3,887	3,306
Other service charges and fee income	1,661	952	2,941	1,820
Gain on sale of other real estate	17	706	17	828
Gain on state tax credits, net	9	153	255	671
Miscellaneous income	1,377	1,406	2,484	2,198
Total noninterest income	7,934	7,049	14,910	13,054
Noninterest expense:				
Employee compensation and benefits	15,798	12,660	31,006	25,307
Occupancy	2,265	1,609	4,194	3,292
Data processing	1,806	1,187	3,439	2,291
Professional fees	1,079	719	1,916	1,403
FDIC and other insurance	650	738	1,474	1,461
Loan legal and other real estate expense	613	353	958	710
Merger related expenses	4,480	—	6,147	—
Other	5,960	4,087	10,253	7,651
Total noninterest expense	32,651	21,353	59,387	42,115
Income before income tax expense	17,500	19,099	34,997	36,010
Income tax expense	5,545	6,747	10,651	12,633
Net income	\$11,955	\$12,352	\$24,346	\$23,377

Edgar Filing: ENTERPRISE FINANCIAL SERVICES CORP - Form 10-Q

Earnings per common share

Basic	\$0.51	\$0.62	\$1.07	\$1.17
Diluted	0.50	0.61	1.06	1.16

See accompanying notes to consolidated financial statements.

2

ENTERPRISE FINANCIAL SERVICES CORP AND SUBSIDIARIES
Condensed Consolidated Statements of Comprehensive Income (Unaudited)

(in thousands)	Three months ended June 30,		Six months ended June 30,	
	2017	2016	2017	2016
Net income	\$11,955	\$12,352	\$24,346	\$23,377
Other comprehensive income, net of tax:				
Unrealized gains on investment securities arising during the period, net of income tax expense for three months of \$921 and \$986, and for six months of \$1,268 and 1,502		1,588	2,070	5,299
\$3,290, respectively				
Total other comprehensive income	1,502	1,588	2,070	5,299
Total comprehensive income	\$13,457	\$13,940	\$26,416	\$28,676

See accompanying notes to consolidated financial statements.

ENTERPRISE FINANCIAL SERVICES CORP AND SUBSIDIARIES
Condensed Consolidated Statements of Shareholders' Equity (Unaudited)

(in thousands, except per share data)	Preferred Stock	Common Stock	Treasury Stock	Additional paid in capital	Retained earnings	Accumulated other comprehensive income (loss)	Total shareholders' equity
Balance December 31, 2016	\$ —	\$ 203	\$(6,632)	\$213,078	\$182,190	\$ (1,741)	\$ 387,098
Net income	—	—	—	—	24,346	—	24,346
Reclassification adjustment for realized gain on sale of securities included in net income, net of tax	—	—	—	—	—	2,070	2,070
Total comprehensive income	—	—	—	—	24,346	2,070	26,416
Cash dividends paid on common shares, \$0.22 per share	—	—	—	—	(5,163)	—	(5,163)
Issuance under equity compensation plans, 140,531 shares, net	—	1	—	(2,904)	—	—	(2,903)
Share-based compensation	—	—	—	1,576	—	—	1,576
Shares issued in connection with acquisition of Jefferson County Bancshares, Inc.	—	33	—	141,696	—	—	141,729
Reclassification for the adoption of ASU 2016-09	—	—	—	(5,229)	5,229	—	—
Balance June 30, 2017	\$ —	\$ 237	\$(6,632)	\$348,217	\$206,602	\$ 329	\$ 548,753

(in thousands, except per share data)	Preferred Stock	Common Stock	Treasury Stock	Additional paid in capital	Retained earnings	Accumulated other comprehensive income (loss)	Total shareholders' equity
Balance December 31, 2015	\$ —	\$ 201	\$(1,743)	\$210,589	\$141,564	\$ 218	\$ 350,829
Net income	—	—	—	—	23,377	—	23,377
Other comprehensive income	—	—	—	—	—	5,299	5,299
Cash dividends paid on common shares, \$0.19 per share	—	—	—	—	(3,804)	—	(3,804)
Repurchase of common shares	—	—	(4,711)	—	—	—	(4,711)
Issuance under equity compensation plans, 141,116 shares, net	—	1	—	(1,812)	—	—	(1,811)
Share-based compensation	—	—	—	1,626	—	—	1,626
Excess tax benefit related to equity compensation plans	—	—	—	824	—	—	824
Balance June 30, 2016	\$ —	\$ 202	\$(6,454)	\$211,227	\$161,137	\$ 5,517	\$ 371,629

See accompanying notes to consolidated financial statements.

ENTERPRISE FINANCIAL SERVICES CORP AND SUBSIDIARIES

Condensed Consolidated Statements of Cash Flows (Unaudited)

Six months ended June 30,

(in thousands, except share data)	2017		2016	
Cash flows from operating activities:				
Net income	\$ 24,346		\$ 23,377	
Adjustments to reconcile net income to net cash provided by operating activities				
Depreciation	1,583		1,070	
Provision for loan losses	4,800		1,140	
Deferred income taxes	4,166		3,509	
Net amortization of debt securities	1,708		1,513	
Amortization of intangible assets	1,207		486	
Mortgage loans originated for sale	(80,697	)	(70,018)
Proceeds from mortgage loans sold	86,127		67,278	
Gain on sale of other real estate	(17	)	(828)
Gain on state tax credits, net	(255	)	(671)
Excess tax benefit of share-based compensation	—		(824)
Share-based compensation	1,576		1,626	
Valuation adjustment on other real estate	18		1	
Net accretion of loan discount	(3,001	)	(5,692)
Changes in:				
Accrued interest receivable	1,988		276	
Accrued interest payable	(299	)	(4)
Other assets	465		(5,284)
Other liabilities	(51,359	)	(9,295)
Net cash (used in) provided by operating activities	(7,644	)	7,660	
Cash flows from investing activities:				
Proceeds from JCB acquisition, net of cash purchase price	4,456		—	
Net increase in loans	(65,592	)	(112,500)
Proceeds from the sale of securities, available for sale	143,554		—	
Proceeds from the paydown or maturity of securities,	107,603		29,398	

Edgar Filing: ENTERPRISE FINANCIAL SERVICES CORP - Form 10-Q

available for sale			
Proceeds from the paydown			
or maturity of securities,	2,722		1,145
held to maturity			
Proceeds from the			
redemption of other	23,390		34,314
investments			
Proceeds from the sale of			
state tax credits held for sale	4,286		3,952
Proceeds from the sale of			
other real estate	2,513		6,355
Payments for the			
purchase/origination of:			
Available for sale debt and			
equity securities	(263,453	)	(49,012
Other investments	(30,977	)	(34,263
State tax credits held for sale—			(2,349
Fixed assets	(1,140	)	(740
Net cash used in investing			
activities	(72,638	)	(123,700
Cash flows from financing			
activities:			
Net increase (decrease) in			
noninterest-bearing deposit	(8,162	)	35,713
accounts			
Net increase (decrease) in			
interest-bearing deposit	(69,117	)	207,932
accounts			
Proceeds from Federal			
Home Loan Bank advances	1,141,181		981,000
Repayments of Federal			
Home Loan Bank advances	(940,681	)	(1,013,000
Net decrease in other			
borrowings	(115,911	)	(69,964
Cash dividends paid on			
common stock	(5,163	)	(3,804
Excess tax benefit of			
share-based compensation	—		824
Payments for the repurchase			
of common stock	—		(4,711
Issuance of common stock,			
net	(2,903	)	(1,811
Net cash (used in) provided			
by financing activities	(756	)	132,179
Net increase (decrease) in			
cash and cash equivalents	(81,038	)	16,139
Cash and cash equivalents,			
beginning of period	198,802		94,157
Cash and cash equivalents,			
end of period	\$ 117,764		\$ 110,296

Supplemental disclosures of
cash flow information:

Cash paid during the period
for:

Interest	\$	10,653	\$	6,286
Income taxes		6,386		19,124

Noncash transactions:

Transfer to other real estate owned in settlement of loans	\$	289	\$	2,683
---	----	-----	----	-------

Sales of other real estate financed	—			140
--	---	--	--	-----

Common shares issued in connection with JCB acquisition		141,729		—
---	--	---------	--	---

See accompanying notes to consolidated financial statements.

ENTERPRISE FINANCIAL SERVICES CORP AND SUBSIDIARIES

Notes to Condensed Consolidated Financial Statements (Unaudited)

NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The significant accounting policies used by Enterprise Financial Services Corp (the "Company" or "Enterprise") in the preparation of the condensed consolidated financial statements are summarized below:

Business and Consolidation

Enterprise is a financial holding company that provides a full range of banking and wealth management services to individuals and corporate customers located in the St. Louis, Kansas City, and Phoenix metropolitan markets through its banking subsidiary, Enterprise Bank & Trust (the "Bank").

Operating results for the three and six months ended June 30, 2017 are not necessarily indicative of the results that may be expected for any other interim period or for the year ending December 31, 2017. For further information, refer to the consolidated financial statements and footnotes thereto included in the Company's Annual Report on Form 10-K for the year ended December 31, 2016.

Basis of Financial Statement Presentation

The condensed consolidated financial statements of the Company and its subsidiaries have been prepared in accordance with the accounting principles generally accepted in the United States of America ("U.S. GAAP") for interim financial information and with the instructions to Form 10-Q and Rule 10-01 of Regulation S-X. The condensed consolidated financial statements include the accounts of the Company and its subsidiaries, all of which are wholly owned. All intercompany accounts and transactions have been eliminated. In 2017, the Company changed its presentation of loans on the face of the Condensed Consolidated Balance Sheets to combine originated loans with purchased loans. See Note 5 - Loans for more information. The Company adopted Accounting Standards Update (ASU) 2016-09, Compensation-Stock Compensation (Topic 718): Improvements to Employee Share-Based Payment Accounting during the first quarter of 2017. Among other elements, the ASU requires an entity to recognize all excess tax benefits and deficiencies related to stock-based compensation expense as income tax expense or benefit in the statements of operations. The ASU requires adjustments be reflected as of the beginning of the fiscal year of adoption and as a result, \$5.2 million of previously recognized excess tax benefits were reclassified from Additional paid in capital to Retained earnings during the first quarter of 2017. The adoption resulted in a decrease to income tax expense of \$1.8 million for the six months ended June 30, 2017. Excess tax benefits related to stock compensation are presented as a cash inflow from operating activities for the six months ended June 30, 2017 due to the prospective adoption of employee share-based payment guidance in 2017. In the opinion of management, all adjustments (consisting of normal recurring accruals) considered necessary for a fair presentation have been included.

Acquisitions

Acquisitions and business combinations are accounted for using the acquisition method of accounting. The assets and liabilities of the acquired entities have been recorded at their estimated fair values at the date of acquisition. Goodwill represents the excess of the purchase price over the fair value of net assets acquired, including the amount assigned to identifiable intangible assets.

The purchase price allocation process requires an estimation of the fair values of the assets acquired and the liabilities assumed. When a business combination agreement provides for an adjustment to the cost of the combination contingent on future events, the Company includes an estimate of the acquisition-date fair value as part of the cost of

the combination. To determine the fair values, the Company relies on third party valuations, such as appraisals, or internal valuations based on discounted cash flow analyses or other valuation techniques. The results of operations of the acquired business are included in the Company's consolidated financial statements from the date of acquisition. Merger-related costs are costs the Company incurs to effect a business combination. In 2017, the Company changed its

6

presentation of Merger related expenses as a separate component of Noninterest expenses on the Condensed Consolidated Statements of Operations. Merger related expenses include costs directly related to merger or acquisition activity and include legal and professional fees, system consolidation and conversion costs, and compensation costs such as severance and retention incentives for employees impacted by acquisition activity. The Company accounts for merger-related costs as expenses in the periods in which the costs are incurred and the services are received.

Purchased Credit Impaired ("PCI") Loans

Purchased credit impaired ("PCI") loans were acquired in a business combination or transaction that have evidence of deterioration of credit quality since origination and for which it is probable, at acquisition, that the Company will be unable to collect all contractually required payments receivable. PCI loans were initially recorded at fair value (as determined by the present value of expected future cash flows) with no valuation allowance. The difference between the undiscounted cash flows expected at acquisition and the investment in the loans, or the "accretable yield," is recognized as interest income on a level-yield method over the life of the loans. Contractually required payments for interest and principal that exceed the undiscounted cash flows expected at acquisition, or the "nonaccretable difference," are not recognized as a yield adjustment or as a loss accrual or a valuation allowance. The Company aggregates individual loans with common risk characteristics into pools of loans. Increases in expected cash flows subsequent to the initial investment are recognized prospectively through adjustment of the yield on the loans over their remaining lives. Decreases in expected cash flows due to an inability to collect contractual cash flows are recognized as impairment through the provision for loan losses account. Any allowance for loan loss on these pools reflect only losses incurred after the acquisition. Disposals of loans, including sales of loans, paydowns, payments in full or foreclosures result in the removal or reduction of the loan from the loan pool.

PCI loans are generally considered accruing and performing, as the loans accrete income over the estimated life of the loan, in circumstances where cash flows are reasonably estimable by management. Accordingly, PCI loans that could be contractually past due could be considered to be accruing and performing. If the timing and amount of future cash flows is not reasonably estimable or is less than the carrying value, the loans may be classified as nonaccrual loans and the purchase price discount on those loans is not recorded as interest income until the timing and amount of future cash flows can be reasonably estimable.

Allowance for Loan Losses on PCI Loans

The Company updates its cash flow projections for purchased credit-impaired loans on a periodic basis. Assumptions utilized in this process include projections related to probability of default, loss severity, prepayment, extensions and recovery lag. Projections related to probability of default and prepayment are calculated utilizing a loan migration analysis and management's assessment of loss exposure including the fair value of underlying collateral. The loan migration analysis is a matrix that specifies the probability of a loan pool transitioning into a particular delinquency or liquidation state given its current performance at the measurement date. Loss severity factors are based upon industry data and historical experience.

Any decreases in expected cash flows after the acquisition date and subsequent measurement periods are recognized by recording an impairment in allowance for loan losses through a provision for loan losses.

NOTE 2 - ACQUISITIONS

Acquisition of Jefferson County Bancshares, Inc.

On February 10, 2017, the Company closed its acquisition of 100% of Jefferson County Bancshares, Inc. ("JCB") and its wholly-owned subsidiary, Eagle Bank and Trust Company of Missouri. JCB operated 13 full service retail and commercial banking offices in the metropolitan St. Louis area and one in Perry County, Missouri.

JCB shareholders received, based on their election, cash consideration in an amount of \$85.39 per share of JCB common stock or 2.75 shares of EFSC common stock per share of JCB common stock, subject to allocation and proration procedures. Aggregate consideration at closing was 3.3 million shares of EFSC common stock and \$29.3 million cash

paid to JCB shareholders and holders of JCB stock options. Based on EFSC's closing stock price of \$42.95 on February 10, 2017, the overall transaction had a value of \$171.0 million, including JCB's common stock and stock options. The Company also recognized \$6.1 million and \$1.4 million of merger related costs that were recorded in noninterest expense in the statement of operations for the six months ended June 30, 2017, and year ended December 31, 2016, respectively.

The acquisition of JCB has been accounted for as a business combination using the acquisition method of accounting which requires assets acquired and liabilities assumed to be recognized at fair value as of the acquisition date. The estimates of fair value are preliminary and subject to refinement as the Company completes its evaluation of the acquired assets and liabilities. Goodwill of \$85.9 million arising from the acquisition consists largely of the synergies and economies of scale expected from combining the operations of JCB into Enterprise. The goodwill is assigned as part of the Company's Banking reporting unit. None of the goodwill recognized is expected to be deductible for income tax purposes.

The following table presents the assets acquired and liabilities assumed of JCB as of February 10, 2017, and their preliminary estimated fair values:

(in thousands)	As Recorded by JCB	Adjustments	As Recorded by EFSC
Assets acquired:			
Cash and cash equivalents	\$ 33,739	\$ —	\$ 33,739
Interest-bearing deposits	1,715	—	1,715
Securities	148,670	—	148,670
Portfolio loans, net	685,905	(11,094)	(a) 674,811
Other real estate owned	6,762	(5,082)	(b) 1,680
Other investments	2,695	—	2,695
Fixed assets, net	21,780	(2,259)	(c) 19,521
Accrued interest receivable	2,794	—	2,794
Goodwill	7,806	(7,806)	(d) —
Other intangible assets	25	11,489	(e) 11,514
Deferred tax assets	4,634	4,144	(f) 8,778
Other assets	19,107	(296)	(g) 18,811
Total assets acquired	\$ 935,632	\$ (10,904)	\$ 924,728
Liabilities assumed:			
Deposits	\$ 764,539	\$ 629	(h) \$ 765,168
Other borrowings	55,430	681	(i) 56,111
Trust preferred securities	12,887	(382)	(j) 12,505
Accrued interest payable	653	—	653
Other liabilities	5,006	125	5,131
Total liabilities assumed	\$ 838,515	\$ 1,053	\$ 839,568
Net assets acquired	\$ 97,117	\$ (11,957)	\$ 85,160
Consideration paid:			
Cash			\$ 29,283
Common stock			141,729
Total consideration paid			\$ 171,012
Goodwill			\$ 85,852

Fair value adjustments based on the Company's evaluation of the acquired loan portfolio, write-off of net deferred loan costs, reclassification from other real estate owned, and elimination of the allowance for loan losses recorded (a) by JCB. The fair value discount recorded to the loan portfolio is \$24.7 million. An increase in the loan fair value discount was recorded during the second quarter of 2017 in the amount of \$0.5 million upon continued refinement of the fair values.

(b) Fair value adjustment based on the Company's evaluation of the acquired other real estate portfolio, and reclassification to portfolio loans.

(c) Fair value adjustments based on the Company's evaluation of the acquired premises and equipment.

(d) Eliminate JCB's recorded goodwill.

Record the core deposit intangible asset on the acquired core deposit accounts. Amount to be amortized using a (e) sum of years digits method over a 10 year useful life. The adjustment was increased \$1.5 million during the second quarter due to continued refinement of the purchase accounting calculations.

- (f) Adjustment for deferred taxes at the acquisition date. The adjustment decreased by \$2.9 million during the current quarter due to continued refinement of the purchase accounting calculations.
- (g) Fair value adjustment based on evaluation of other assets.
- (h) Fair value adjustment to time deposits based on current interest rates.
- (i) Fair value adjustment to the FHLB advances based on current interest rates.
- (j) Fair value adjustment based on the Company's evaluation of the trust preferred securities.

The following table provides the unaudited pro forma information for the results of operations for the six months ended June 30, 2017 and 2016, as if the acquisition had occurred on January 1, 2016. The pro forma results combine the historical results of JCB with the Company's Consolidated Statements of Income, adjusted for the impact of the application of the acquisition method of accounting including loan discount accretion, intangible assets amortization, and deposit and trust preferred securities premium accretion, net of taxes. The pro forma results have been prepared for comparative purposes only and are not necessarily indicative of the results that would have been obtained had the acquisition actually occurred on January 1, 2016. No assumptions have been applied to the pro forma results of operations regarding possible revenue enhancements, expense efficiencies or asset dispositions. Only the acquisition related expenses that have been incurred as of June 30, 2017 are included in net income in the table below.

	Pro Forma	
	Six months ended June 30,	
(in thousands, except per share data)	2017	2016
Total revenues (net interest income plus noninterest income)	\$101,954	\$97,208
Net income	23,845	27,721
Diluted earnings per common share	1.00	1.18

NOTE 3 - EARNINGS PER SHARE

Basic earnings per common share data is calculated by dividing net income by the weighted average number of common shares outstanding during the period. Common shares outstanding include common stock and restricted stock awards where recipients have satisfied the vesting terms. Diluted earnings per common share gives effect to all dilutive potential common shares outstanding during the period using the treasury stock method.

The following table presents a summary of per common share data and amounts for the periods indicated.

	Three months ended June 30,		Six months ended June 30,	
	2017	2016	2017	2016
(in thousands, except per share data)				
Net income as reported	\$11,955	\$12,352	\$24,346	\$23,377
Weighted average common shares outstanding	23,475	20,003	22,706	20,002
Additional dilutive common stock equivalents	257	213	314	224
Weighted average diluted common shares outstanding	23,732	20,216	23,020	20,226
Basic earnings per common share:	\$0.51	\$0.62	\$1.07	\$1.17
Diluted earnings per common share:	\$0.50	\$0.61	\$1.06	\$1.16

For the three and six months ended June 30, 2017 and 2016, there were no common stock equivalents excluded from the earnings per share calculations because their effect would have been anti-dilutive.

NOTE 4 - INVESTMENTS

The following table presents the amortized cost, gross unrealized gains and losses and fair value of securities available for sale and held to maturity:

	June 30, 2017			
(in thousands)	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
Available for sale securities:				
Obligations of U.S. Government-sponsored enterprises	\$99,855	\$ 386	\$ (6)	\$100,235
Obligations of states and political subdivisions	34,083	1,001	—	35,084
Agency mortgage-backed securities	488,951	2,108	(2,521)	488,538
Total securities available for sale	\$622,889	\$ 3,495	\$ (2,527)	\$623,857
Held to maturity securities:				
Obligations of states and political subdivisions	\$14,722	\$ 189	\$ (7)	\$14,904
Agency mortgage-backed securities	62,919	135	(127)	62,927
Total securities held to maturity	\$77,641	\$ 324	\$ (134)	\$77,831
	December 31, 2016			
(in thousands)	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
Available for sale securities:				
Obligations of U.S. Government-sponsored enterprises	\$107,312	\$ 348	\$ —	\$107,660
Obligations of states and political subdivisions	36,486	630	(485)	36,631
Agency mortgage-backed securities	319,345	1,101	(3,940)	316,506
Total securities available for sale	\$463,143	\$ 2,079	\$ (4,425)	\$460,797
Held to maturity securities:				
Obligations of states and political subdivisions	\$14,759	\$ 11	\$ (242)	\$14,528
Agency mortgage-backed securities	65,704	45	(638)	65,111
Total securities held to maturity	\$80,463	\$ 56	\$ (880)	\$79,639

At June 30, 2017, and December 31, 2016, there were no holdings of securities of any one issuer in an amount greater than 10% of shareholders' equity, other than U.S. Government agencies and sponsored enterprises. The agency mortgage-backed securities are all issued by U.S. Government-sponsored enterprises. Available for sale securities having a fair value of \$418.9 million and \$407.3 million at June 30, 2017, and December 31, 2016, respectively, were pledged as collateral to secure deposits of public institutions and for other purposes as required by law or contract provisions.

The amortized cost and estimated fair value of debt securities at June 30, 2017, by contractual maturity, are shown below. Expected maturities may differ from contractual maturities because borrowers may have the right to call or prepay obligations with or without call or prepayment penalties. The weighted average life of the mortgage-backed securities is approximately 5 years.

(in thousands)	Available for sale		Held to maturity	
	Amortized Cost	Estimated Fair Value	Amortized Cost	Estimated Fair Value
Due in one year or less	\$1,780	\$1,791	\$—	\$—
Due after one year through five years	111,987	112,761	—	—
Due after five years through ten years	16,807	17,391	12,367	12,529
Due after ten years	3,364	3,375	2,355	2,375
Agency mortgage-backed securities	488,951	488,539	62,919	62,927
	\$622,889	\$623,857	\$77,641	\$77,831

The following table represents a summary of investment securities that had an unrealized loss:

(in thousands)	June 30, 2017					
	Less than 12 months		12 months or more		Total	
	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses
Obligations of U.S. Government-sponsored enterprises	\$10,142	\$ 6	\$—	\$ —	\$10,142	\$ 6
Obligations of states and political subdivisions	\$1,642	\$ 7	\$—	\$ —	\$1,642	\$ 7
Agency mortgage-backed securities	293,426	2,197	12,918	451	306,344	2,648
	\$305,210	\$ 2,210	\$12,918	\$ 451	\$318,128	\$ 2,661

(in thousands)	December 31, 2016					
	Less than 12 months		12 months or more		Total	
	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses
Obligations of states and political subdivisions	\$21,361	\$ 408	\$3,553	\$ 320	\$24,914	\$ 728
Agency mortgage-backed securities	267,734	4,084	12,883	493	280,617	4,577
	\$289,095	\$ 4,492	\$16,436	\$ 813	\$305,531	\$ 5,305

The unrealized losses at both June 30, 2017, and December 31, 2016, were primarily attributable to changes in market interest rates since the securities were purchased. Management systematically evaluates investment securities for other-than-temporary declines in fair value on a quarterly basis. This analysis requires management to consider various factors, which include among other considerations (1) the present value of the cash flows expected to be collected compared to the amortized cost of the security, (2) duration and magnitude of the decline in value, (3) the financial condition of the issuer or issuers, (4) structure of the security, and (5) the intent to sell the security or whether it is more likely than not the Company would be required to sell the security before its anticipated recovery in market value. At June 30, 2017, management performed its quarterly analysis of all securities with an unrealized loss and concluded no individual securities were other-than-temporarily impaired.

NOTE 5 - LOANS

The loan portfolio is comprised of loans originated by the Company and loans that were acquired in connection with the Company's acquisitions. These loans are accounted for using the guidance in the Accounting Standards Codification (ASC) section 310-30 and 310-20. Loans accounted for using ASC 310-30 are sometimes referred to as purchased credit impaired, or PCI, loans.

The table below shows the loan portfolio composition including carrying value by segment of loans accounted for under ASC 310-30 (PCI loans) and loans not accounted for under this guidance, which includes our originated loans.

(in thousands)	June 30, 2017	December 31, 2016
Loans not accounted for as ASC 310-30	\$3,810,470	\$3,118,392
Loans accounted for as ASC 310-30	84,300	39,769
Total loans	\$3,894,770	\$3,158,161

The following tables refer to loans not accounted for as ASC 310-30 loans.

Below is a summary of loans by category at June 30, 2017 and December 31, 2016:

(in thousands)	June 30, 2017	December 31, 2016
Commercial and industrial	\$1,795,667	\$1,632,714
Real estate:		
Commercial - investor owned	711,702	544,808
Commercial - owner occupied	523,185	350,148
Construction and land development	283,226	194,542
Residential	345,895	240,760
Total real estate loans	1,864,008	1,330,258
Consumer and other	151,670	156,182
Loans, before unearned loan fees	3,811,345	3,119,154
Unearned loan fees, net	(875)	(762)
Loans, including unearned loan fees	\$3,810,470	\$3,118,392

A summary of the activity in the allowance for loan losses and the recorded investment in loans by class and category based on impairment method through June 30, 2017, and at December 31, 2016, is as follows:

(in thousands)	Commercial and industrial	CRE - investor owned	CRE - owner occupied	Construction and land development	Residential real estate	Consumer and other	Total
Allowance for loan losses:							
Balance at December 31, 2016	\$ 26,996	\$3,420	\$ 2,890	\$ 1,304	\$ 2,023	\$ 932	\$37,565
Provision (provision reversal) for loan losses	1,835	(105)	(249)	(11)	(3)	66	1,533
Losses charged off	(133)	—	—	—	(9)	(29)	(171)
Recoveries	80	9	89	9	25	9	221
Balance at March 31, 2017	\$ 28,778	\$3,324	\$ 2,730	\$ 1,302	\$ 2,036	\$ 978	\$39,148
Provision (provision reversal) for loan losses	2,955	(39)	354	(51)	451	(47)	3,623

Edgar Filing: ENTERPRISE FINANCIAL SERVICES CORP - Form 10-Q

Losses charged off	(6,035)	—	(45)	(5)	(265)	(39)	(6,389)
Recoveries	57	102	1	49	62	20	291
Balance at June 30, 2017	\$ 25,755	\$ 3,387	\$ 3,040	\$ 1,295	\$ 2,284	\$ 912	\$ 36,673

13

Edgar Filing: ENTERPRISE FINANCIAL SERVICES CORP - Form 10-Q

(in thousands)	Commercial and industrial	CRE - investor owned	CRE - owner occupied	Construction and land development	Residential real estate	Consumer and other	Total
Balance June 30, 2017							
Allowance for loan losses - Ending balance:							
Individually evaluated for impairment	\$ 1,616	\$—	\$—	\$ 131	\$ 52	\$—	\$ 1,799
Collectively evaluated for impairment	24,139	3,387	3,040	1,164	2,232	912	34,874
Total	\$ 25,755	\$ 3,387	\$ 3,040	\$ 1,295	\$ 2,284	\$ 912	\$ 36,673
Loans - Ending balance:							
Individually evaluated for impairment	\$ 10,209	\$ 287	\$ 1,552	\$ 1,489	\$ 1,293	\$ 9	\$ 14,839
Collectively evaluated for impairment	1,785,458	711,415	521,633	281,737	344,602	150,786	3,795,631
Total	\$ 1,795,667	\$ 711,702	\$ 523,185	\$ 283,226	\$ 345,895	\$ 150,795	\$ 3,810,470
Balance December 31, 2016							
Allowance for loan losses - Ending balance:							
Individually evaluated for impairment	\$ 2,909	\$—	\$—	\$ 155	\$—	\$—	\$ 3,064
Collectively evaluated for impairment	24,087	3,420	2,890	1,149	2,023	932	34,501
Total	\$ 26,996	\$ 3,420	\$ 2,890	\$ 1,304	\$ 2,023	\$ 932	\$ 37,565
Loans - Ending balance:							
Individually evaluated for impairment	\$ 12,523	\$ 430	\$ 1,854	\$ 1,903	\$ 62	\$—	\$ 16,772
Collectively evaluated for impairment	1,620,191	544,378	348,294	192,639	240,698	155,420	3,101,620
Total	\$ 1,632,714	\$ 544,808	\$ 350,148	\$ 194,542	\$ 240,760	\$ 155,420	\$ 3,118,392

A summary of non-performing loans individually evaluated for impairment by category at June 30, 2017 and December 31, 2016, is as follows:

(in thousands)	June 30, 2017					
	Unpaid Contractual Principal Balance	Recorded Investment With No Allowance	Recorded Investment With Allowance	Total Recorded Investment	Related Allowance	Average Recorded Investment
Commercial and industrial Real estate:	\$ 15,548	\$ 3,751	\$ 6,534	\$ 10,285	\$ 1,572	\$ 15,283
Commercial - investor owned	288	288	—	288	—	288
Commercial - owner occupied	—	—	—	—	—	—
Construction and land development	1,935	1,603	332	1,935	131	1,550
Residential	1,540	632	678	1,310	52	1,514
Consumer and other	9	9	—	9	—	9
Total	\$ 19,320	\$ 6,283	\$ 7,544	\$ 13,827	\$ 1,755	\$ 18,644

December 31, 2016

Edgar Filing: ENTERPRISE FINANCIAL SERVICES CORP - Form 10-Q

(in thousands)	Unpaid Contractual Principal Balance	Recorded Investment With No Allowance	Recorded Investment With Allowance	Total Recorded Investment	Related Allowance	Average Recorded Investment
Commercial and industrial	\$12,341	\$ 566	\$ 11,791	\$ 12,357	\$ 2,909	\$ 4,489
Real estate:						
Commercial - investor owned	525	435	—	435	—	668
Commercial - owner occupied	225	231	—	231	—	227
Construction and land development	1,904	1,947	359	2,306	155	1,918
Residential	62	62	—	62	—	64
Consumer and other	—	—	—	—	—	—
Total	\$15,057	\$ 3,241	\$ 12,150	\$ 15,391	\$ 3,064	\$ 7,366

The following table presents details for past due and impaired loans:

(in thousands)	Three months ended June 30,		Six months ended June 30,	
	2017	2016	2017	2016
Total interest income that would have been recognized under original terms	\$340	\$329	\$655	\$477
Total cash received and recognized as interest income on non-accrual loans	16	44	39	50
Total interest income recognized on impaired loans	14	25	47	31

There were no loans over 90 days past due and still accruing interest at June 30, 2017 or December 31, 2016.

The recorded investment in impaired loans by category at June 30, 2017 and December 31, 2016, is as follows:

(in thousands)	June 30, 2017		
	Non-accrued	Restructured	Total
Commercial and industrial	\$9,608	\$ 677	\$10,285
Real estate:			
Commercial - investor owned	288	—	288
Commercial - owner occupied	—	—	—
Construction and land development	1,935	—	1,935
Residential	1,310	—	1,310
Consumer and other	9	—	9
Total	\$13,150	\$ 677	\$13,827

(in thousands)	December 31, 2016		
	Non-accrued	Restructured	Total
Commercial and industrial	\$10,046	\$ 2,311	\$12,357
Real estate:			
Commercial - investor owned	435	—	435
Commercial - owner occupied	231	—	231
Construction and land development	2,286	20	2,306
Residential	62	—	62
Consumer and other	—	—	—
Total	\$13,060	\$ 2,331	\$15,391

Edgar Filing: ENTERPRISE FINANCIAL SERVICES CORP - Form 10-Q

The recorded investment by category for the Portfolio loans that have been restructured during the three and six months ended June 30, 2017 and 2016, is as follows:

(in thousands, except for number of loans)	Three months ended June 30, 2017		Three months ended June 30, 2016	
	Pre-Modification Number of Outstanding Recorded loans Balance	Post-Modification Outstanding Recorded Balance	Pre-Modification Number of Outstanding Recorded loans Balance	Post-Modification Outstanding Recorded Balance
Commercial and industrial	1 \$ 676	\$ 676	1 \$ 2,300	\$ 2,300
Real estate:				
Commercial - investor owned	—	—	—	—
Commercial - owner occupied	—	—	—	—
Construction and land development	—	—	1 20	20
Residential	—	—	—	—
Consumer and other	—	—	—	—
Total	1 \$ 676	\$ 676	2 \$ 2,320	\$ 2,320

(in thousands, except for number of loans)	Six months ended June 30, 2017		Six months ended June 30, 2016	
	Pre-Modification Number of Outstanding Recorded loans Balance	Post-Modification Outstanding Recorded Balance	Pre-Modification Number of Outstanding Recorded loans Balance	Post-Modification Outstanding Recorded Balance
Commercial and industrial	1 \$ 676	\$ 676	2 \$ 2,341	\$ 2,341
Real estate:				
Commercial - investor owned	—	—	1 248	248
Commercial - owner occupied	—	—	—	—
Construction and land development	—	—	1 20	20
Residential	—	—	—	—
Consumer and other	—	—	—	—
Total	1 \$ 676	\$ 676	4 \$ 2,609	\$ 2,609

As of June 30, 2017, the Company had \$0.7 million specific reserves allocated to loans that have been restructured. During the three and six months ended June 30, 2016, there were no portfolio loans that subsequently defaulted. Portfolio loans restructured that subsequently defaulted during the three and six months ended June 30, 2017, are as follows:

(in thousands, except for number of loans)	Three months ended June 30, 2017	Six months ended June 30, 2017
	Number of Recorded loans Balance	Number of Recorded loans Balance
Commercial and industrial	2 \$ 343	2 \$ 343
Real estate:		
Commercial - investor owned	—	—
Commercial - owner occupied	—	—
Construction and land development	—	—
Residential	1 5	1 5

Consumer and other	_____	_____
Total	3 \$ 348	3 \$ 348

Edgar Filing: ENTERPRISE FINANCIAL SERVICES CORP - Form 10-Q

The aging of the recorded investment in past due loans by portfolio class and category at June 30, 2017 and December 31, 2016 is shown below.

(in thousands)	June 30, 2017				
	30-89 Days Past Due	90 or More Days Past Due	Total Past Due	Current	Total
Commercial and industrial	\$936	\$—	\$936	\$1,794,731	\$1,795,667
Real estate:					
Commercial - investor owned	205	—	205	711,497	711,702
Commercial - owner occupied	—	—	—	523,185	523,185
Construction and land development	47	1,489	1,536	281,690	283,226
Residential	836	621	1,457	344,438	345,895
Consumer and other	11	9	20	150,775	150,795
Total	\$2,035	\$2,119	\$4,154	\$3,806,316	\$3,810,470

(in thousands)	December 31, 2016				
	30-89 Days Past Due	90 or More Days Past Due	Total Past Due	Current	Total
Commercial and industrial	\$334	\$171	\$505	\$1,632,209	\$1,632,714
Real estate:					
Commercial - investor owned	—	175	175	544,633	544,808
Commercial - owner occupied	212	225	437	349,711	350,148
Construction and land development	355	1,528	1,883	192,659	194,542
Residential	91	—	91	240,669	240,760
Consumer and other	7	—	7	155,413	155,420
Total	\$999	\$2,099	\$3,098	\$3,115,294	\$3,118,392

The Company categorizes loans into risk categories based on relevant information about the ability of borrowers to service their debt, such as current financial information, payment experience, credit documentation, and current economic factors among other factors. This analysis is performed on a quarterly basis. The Company uses the following definitions for risk ratings:

Grades 1, 2, and 3 – Includes loans to borrowers with a continuous record of strong earnings, sound balance sheet condition and capitalization, ample liquidity with solid cash flow, and whose management team has experience and depth within their industry.

Grade 4 – Includes loans to borrowers with positive trends in profitability, satisfactory capitalization and balance sheet condition, and sufficient liquidity and cash flow.

Grade 5 – Includes loans to borrowers that may display fluctuating trends in sales, profitability, capitalization, liquidity, and cash flow.

Grade 6 – Includes loans to borrowers where an adverse change or perceived weakness has occurred, but may be correctable in the near future. Alternatively, this rating category may also include circumstances where the borrower is starting to reverse a negative trend or condition, or has recently been upgraded from a 7, 8, or 9 rating.

Grade 7 – Watch credits are borrowers that have experienced financial setback of a nature that is not determined to be severe or influence ‘ongoing concern’ expectations. Although possible, no loss is anticipated, due to strong collateral

and/or guarantor support.

17

Grade 8 – Substandard credits will include those borrowers characterized by significant losses and sustained downward trends in balance sheet condition, liquidity, and cash flow. Repayment reliance may have shifted to secondary sources. Collateral exposure may exist and additional reserves may be warranted.

Grade 9 – Doubtful credits include borrowers that may show deteriorating trends that are unlikely to be corrected.

Collateral values may appear insufficient for full recovery, therefore requiring a partial charge-off, or debt renegotiation with the borrower. The borrower may have declared bankruptcy or bankruptcy is likely in the near term. All doubtful rated credits will be on non-accrual.

The recorded investment by risk category of the loans by portfolio class and category at June 30, 2017, which is based upon the most recent analysis performed, and December 31, 2016 is as follows:

(in thousands)	June 30, 2017				Total
	Pass (1-6)	Watch (7)	Substandard (8)	Doubtful (9)	
Commercial and industrial	\$1,656,173	\$67,262	\$ 72,232	\$	—\$1,795,667
Real estate:					
Commercial - investor owned	692,743	14,955	4,004	—	711,702
Commercial - owner occupied	483,183	32,800	7,202	—	523,185
Construction and land development	278,365	2,730	2,131	—	283,226
Residential	335,818	2,743	7,334	—	345,895
Consumer and other	149,060	375	1,360	—	150,795
Total	\$3,595,342	\$120,865	\$ 94,263	\$	—\$3,810,470

(in thousands)	December 31, 2016				Total
	Pass (1-6)	Watch (7)	Substandard (8)	Doubtful (9)	
Commercial and industrial	\$1,499,114	\$57,416	\$ 76,184	\$	—\$1,632,714
Real estate:					
Commercial - investor owned	530,494	10,449	3,865	—	544,808
Commercial - owner occupied	306,658	39,249	4,241	—	350,148
Construction and land development	185,505	6,575	2,462	—	194,542
Residential	233,479	2,997	4,284	—	240,760
Consumer and other	153,984	—	1,436	—	155,420
Total	\$2,909,234	\$116,686	\$ 92,472	\$	—\$3,118,392

The following tables refer to loans accounted for using ASC 310-30 (purchased credit impaired loans):

Below is a summary of PCI loans by category at June 30, 2017 and December 31, 2016:

(in thousands)	June 30, 2017		December 31, 2016	
	Weighted-Average Risk Rating ¹	Recorded Investment PCI Loans	Weighted-Average Risk Rating ¹	Recorded Investment PCI Loans
Commercial and industrial	6.02	\$ 4,059	5.87	\$ 3,523
Real estate:				
Commercial - investor owned	7.35	46,180	6.95	8,162
Commercial - owner occupied	6.55	12,743	6.39	11,863
Construction and land development	5.84	7,883	5.80	4,365
Residential	6.15	13,370	5.64	11,792
Total real estate loans		80,176		36,182
Consumer and other	2.81	65	1.64	64
Purchased credit impaired loans		\$ 84,300		\$ 39,769

¹Risk ratings are based on the borrower's contractual obligation, which is not reflective of the purchase discount.

The aging of the recorded investment in past due PCI loans by portfolio class and category at June 30, 2017 and December 31, 2016 is shown below:

(in thousands)	June 30, 2017				
	30-89 Days Past Due	90 or More Days Past Due	Total Past Due	Current	Total
Commercial and industrial	\$—	\$50	\$50	\$4,009	\$4,059
Real estate:					
Commercial - investor owned	4,052	—	4,052	42,128	46,180
Commercial - owner occupied	653	401	1,054	11,689	12,743
Construction and land development	—	366	366	7,517	7,883
Residential	400	1,303	1,703	11,667	13,370
Consumer and other	—	—	—	65	65
Total	\$5,105	\$2,120	\$7,225	\$77,075	\$84,300

(in thousands)	December 31, 2016				
	30-89 Days Past Due	90 or More Days Past Due	Total Past Due	Current	Total
Commercial and industrial	\$—	\$—	\$—	\$3,523	\$3,523
Real estate:					
Commercial - investor owned	—	—	—	8,162	8,162
Commercial - owner occupied	—	—	—	11,863	11,863
Construction and land development	—	—	—	4,365	4,365

Edgar Filing: ENTERPRISE FINANCIAL SERVICES CORP - Form 10-Q

Residential	169	51	220	11,572	11,792
Consumer and other	—	—	—	64	64
Total	\$169	\$ 51	\$220	\$39,549	\$39,769

19

The following table is a rollforward of PCI loans, net of the allowance for loan losses, for the six months ended June 30, 2017 and 2016.

(in thousands)	Contractual Cashflows	Non-accretable Difference	Accretable Yield	Carrying Amount
Balance December 31, 2016	\$ 66,003	\$ 18,902	\$ 13,176	\$ 33,925
Acquisitions	68,763	14,296	5,312	49,155
Principal reductions and interest payments	(10,781)	—	—	(10,781)
Accretion of loan discount	—	—	(3,534)	3,534
Changes in contractual and expected cash flows due to remeasurement	5,641	(1,383)	1,328	5,696
Reductions due to disposals	(5,070)	(1,317)	(1,398)	(2,355)
Balance June 30, 2017	\$ 124,556	\$ 30,498	\$ 14,884	\$ 79,174
Balance December 31, 2015	\$ 116,689	\$ 26,765	\$ 25,341	\$ 64,583
Principal reductions and interest payments	(11,768)	—	—	(11,768)
Accretion of loan discount	—	—	(3,431)	3,431
Changes in contractual and expected cash flows due to remeasurement	6,144	1,522	(788)	5,410
Reductions due to disposals	(21,663)	(4,912)	(3,073)	(13,678)
Balance June 30, 2016	\$ 89,402	\$ 23,375	\$ 18,049	\$ 47,978

The accretable yield is recognized in interest income over the estimated life of the acquired loans using the effective yield method. Outstanding customer balances on PCI loans were \$112.6 million and \$54.6 million as of June 30, 2017, and December 31, 2016, respectively.

NOTE 6 - COMMITMENTS AND CONTINGENCIES

The Company issues financial instruments with off balance sheet risk in the normal course of the business of meeting the financing needs of its customers. These financial instruments include commitments to extend credit and standby letters of credit. These instruments may involve, to varying degrees, elements of credit and interest rate risk in excess of the amounts recognized in the consolidated balance sheets.

The Company's extent of involvement and maximum potential exposure to credit loss in the event of nonperformance by the other party to the financial instrument for commitments to extend credit and standby letters of credit is represented by the contractual amount of these instruments.

The Company uses the same credit policies in making commitments and conditional obligations as it does for financial instruments included on its consolidated balance sheets. At June 30, 2017, the amount of unadvanced commitments on impaired loans was insignificant.

The contractual amounts of off-balance-sheet financial instruments as of June 30, 2017, and December 31, 2016, are as follows:

(in thousands)	June 30, 2017	December 31, 2016
Commitments to extend credit	\$ 1,232,326	\$ 1,075,170
Letters of credit	81,154	78,954

Commitments to extend credit are agreements to lend to a customer as long as there is no violation of any condition established in the contract. Commitments usually have fixed expiration dates or other termination clauses, may have significant usage restrictions, and may require payment of a fee. Of the total commitments to extend credit at June 30, 2017, and December 31, 2016, approximately \$119 million and \$90 million, respectively, represent fixed rate loan commitments. Since certain of the commitments may expire without being drawn upon or may be revoked, the total commitment amounts do not necessarily represent future cash requirements. The Company evaluates each customer's credit worthiness on a case-by-case basis. The amount of collateral obtained, if deemed necessary by the Company upon extension of credit, is based on management's credit evaluation of the borrower. Collateral held varies, but may include accounts receivable, inventory, premises and equipment, and real estate. Other liabilities include \$0.3 million for estimated losses attributable to the unadvanced commitments at June 30, 2017, and December 31, 2016.

Standby letters of credit are conditional commitments issued by the Company to guarantee the performance or payment of a customer to a third party. These standby letters of credit are issued to support contractual obligations of the Company's customers. The credit risk involved in issuing letters of credit is essentially the same as the risk involved in extending loans to customers. As of June 30, 2017, the approximate remaining term of standby letters of credit range from 1 month to 4 years and 3 months.

Contingencies

The Company and its subsidiaries are, from time to time, parties to various legal proceedings arising out of their businesses. Management believes there are no such proceedings pending or threatened against the Company or its subsidiaries which, if determined adversely, would have a material adverse effect on the business, consolidated financial condition, results of operations or cash flows of the Company or any of its subsidiaries.

NOTE 7 - DERIVATIVE FINANCIAL INSTRUMENTS

The Company is a party to various derivative financial instruments that are used in the normal course of business to meet the needs of its clients and as part of its risk management activities. These instruments include interest rate swaps and option contracts and foreign exchange forward contracts. The Company does not enter into derivative financial instruments for trading purposes.

Risk Management Instruments. At June 30, 2017, the company has no derivative contracts used to manage risk.

Client-Related Derivative Instruments. The Company enters into interest rate swaps to allow customers to hedge changes in fair value of certain loans while maintaining a variable rate loan on its own books. The Company also enters into foreign exchange forward contracts with clients, and enters into offsetting foreign exchange forward contracts with established financial institution counterparties. The table below summarizes the notional amounts and fair values of the client-related derivative instruments:

(in thousands)	Notional Amount		Asset Derivatives (Other Assets)		Liability Derivatives (Other Liabilities)	
			Fair Value		Fair Value	
	June 30, 2017	December 31, 2016	June 30, 2017	December 31, 2016	June 30, 2017	December 31, 2016
Non-designated hedging instruments						
Interest rate swap contracts	\$ 229,238	\$ 124,322	\$ 1,951	\$ 982	\$ 1,951	\$ 982
Foreign exchange forward contracts	1,625	3,034	1,625	3,034	1,625	3,034

Changes in the fair value of client-related derivative instruments are recognized currently in operations. For the three and six months ended June 30, 2017 and 2016, the gains and losses offset each other due to the Company's hedging of the client swaps and foreign exchange contracts with other bank counterparties.

NOTE 8 - FAIR VALUE MEASUREMENTS

Below is a description of certain assets and liabilities measured at fair value.

The following table summarizes financial instruments measured at fair value on a recurring basis as of June 30, 2017 and December 31, 2016, segregated by the level of the valuation inputs within the fair value hierarchy utilized to measure fair value:

(in thousands)	June 30, 2017			Total Fair Value
	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)	
Assets				
Securities available for sale				
Obligations of U.S. Government-sponsored enterprises	\$-100,235	\$ —		\$100,235
Obligations of states and political subdivisions	—35,084	—		35,084
Residential mortgage-backed securities	—488,538	—		488,538
Total securities available for sale	\$-623,857	\$ —		\$623,857
State tax credits held for sale	—	1,274		1,274
Derivative financial instruments	—3,577	—		3,577
Total assets	\$-627,434	\$ 1,274		\$628,708
Liabilities				
Derivative financial instruments	\$-3,577	\$ —		\$3,577
Total liabilities	\$-3,577	\$ —		\$3,577
December 31, 2016				
(in thousands)	December 31, 2016			Total Fair Value
	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)	
Assets				
Securities available for sale				
Obligations of U.S. Government-sponsored enterprises	\$-107,660	\$ —		\$107,660
Obligations of states and political subdivisions	—33,542	3,089		36,631

Edgar Filing: ENTERPRISE FINANCIAL SERVICES CORP - Form 10-Q

Residential mortgage-backed securities	—316,506	—	316,506
Total securities available for sale	\$-457,708	\$ 3,089	\$460,797
State tax credits held for sale	—	3,585	3,585
Derivative financial instruments	—4,016	—	4,016
Total assets	\$-461,724	\$ 6,674	\$468,398
Liabilities			
Derivative financial instruments	\$-4,016	\$ —	\$4,016
Total liabilities	\$-4,016	\$ —	\$4,016

Securities available for sale. Securities classified as available for sale are reported at fair value utilizing Level 2 and Level 3 inputs. Fair values for Level 2 securities are based upon dealer quotes, market spreads, the U.S. Treasury yield curve, trade execution data, market consensus prepayment speeds, credit information and the

bond's terms and conditions at the security level. At June 30, 2017, there were no Level 3 Auction Rate Securities. Auction Rate Securities at June 30, 2017 were valued using a Level 2 pricing source similar to our other securities available for sale.

State tax credits held for sale. At June 30, 2017, of the \$35.2 million of state tax credits held for sale on the condensed consolidated balance sheet, approximately \$1.3 million were carried at fair value. The remaining \$34.0 million of state tax credits were accounted for at cost.

The Company is not aware of an active market that exists for the 10-year streams of state tax credit financial instruments. However, the Company's principal market for these tax credits consists of Missouri state residents who buy these credits and local and regional accounting firms who broker them. As such, the Company employed a discounted cash flow analysis (income approach) to determine the fair value.

The fair value measurement is calculated using an internal valuation model with market data including discounted cash flows based upon the terms and conditions of the tax credits. If the underlying project remains in compliance with the various federal and state rules governing the tax credit program, each project will generate about 10 years of tax credits. The inputs to the discounted cash flow calculation include: the amount of tax credits generated each year, the anticipated sale price of the tax credit, the timing of the sale and a discount rate. The discount rate is estimated using the LIBOR swap curve at a point equal to the remaining life in years of credits plus a 205 basis point spread. With the exception of the discount rate, the other inputs to the fair value calculation are observable and readily available. The discount rate is considered a Level 3 input because it is an "unobservable input" and is based on the Company's assumptions. An increase in the discount rate utilized would generally result in a lower estimated fair value of the tax credits. Alternatively, a decrease in the discount rate utilized would generally result in a higher estimated fair value of the tax credits. The remaining state tax credits carried at fair value are expected to be sold within the next several quarters. The state tax credit assets are reported as Level 3 assets.

Derivatives. Derivatives are reported at fair value utilizing Level 2 inputs. The Company obtains counterparty quotations to value its interest rate swaps. In addition, the Company validates the counterparty quotations with third party valuation sources. Derivatives with negative fair values are included in Other liabilities in the consolidated balance sheets. Derivatives with positive fair value are included in Other assets in the consolidated balance sheets.

Level 3 financial instruments

The following table presents the changes in Level 3 financial instruments measured at fair value on a recurring basis as of June 30, 2017 and 2016.

Purchases, sales, issuances and settlements. There were no Level 3 purchases during the quarters ended June 30, 2017 or 2016.

Transfers in and/or out of Level 3. There was \$3.1 million in Level 3 transfers to Level 2 during the current quarter and none during the quarter ended June 30, 2016.

(in thousands)	Securities available for sale, at fair value			
	Three months ended June 30, 2017		Six months ended June 30, 2016	
Beginning balance	\$3,093	\$3,085	\$3,089	\$3,077
Total gains:				
Included in other comprehensive income	—	8	4	16
Purchases, sales, issuances and settlements:				
Purchases	—	—	—	—
Transfer in and/or out of Level 3	(3,093)	—	(3,093)	—
Ending balance	\$—	\$3,093	\$—	\$3,093
Change in unrealized gains relating to assets still held at the reporting date	\$—	\$8	\$—	\$16

(in thousands)	State tax credits held for sale			
	Three months ended June 30, 2017		Six months ended June 30, 2016	
Beginning balance	\$1,458	\$4,733	\$3,585	\$5,941
Total gains:				
Included in earnings	9	41	49	117
Purchases, sales, issuances and settlements:				
Sales	(193)	—	(2,360)	(1,284)
Ending balance	\$1,274	\$4,774	\$1,274	\$4,774
Change in unrealized gains (losses) relating to assets still held at the reporting date	\$(49)	\$41	\$(655)	\$(264)

From time to time, the Company measures certain assets at fair value on a nonrecurring basis. These include assets that are measured at the lower of cost or fair value that were recognized at fair value below cost at the end of the period. The following table presents financial instruments and non-financial assets measured at fair value on a non-recurring basis as of June 30, 2017.

(in thousands)	(1) Total Fair Value	(1) Quoted Prices in Active Markets for Identical Assets (Level 1)	(1) Significant Other Observable Inputs (Level 2)	(1) Significant Unobservable Inputs (Level 3)	Total losses for the three months ended June 30, 2017	Total losses for the six months ended June 30, 2017
Impaired loans	\$ 10,073	\$ —	—\$	—\$ 10,073	\$ 6,403	\$ 6,560
Other real estate	—	—	—	—	—	18
Total	\$ 10,073	\$ —	—\$	—\$ 10,073	\$ 6,403	\$ 6,578

(1) The amounts represent only balances measured at fair value during the period and still held as of the reporting date.

Impaired loans are reported at the fair value of the underlying collateral for collateral dependent loans. Fair values for impaired loans are obtained from current appraisals by qualified licensed appraisers or independent valuation specialists. Other real estate owned is adjusted to fair value upon foreclosure of the underlying loan. Subsequently, foreclosed assets are carried at the lower of carrying value or fair value less costs to sell. Fair value of other real estate is based upon the current appraised values of the properties as determined by qualified licensed appraisers and the Company's judgment of other relevant market conditions. Certain state tax credits are reported at cost.

Following is a summary of the carrying amounts and fair values of the Company's financial instruments on the consolidated balance sheets at June 30, 2017 and December 31, 2016.

(in thousands)	June 30, 2017		December 31, 2016	
	Carrying Amount	Estimated fair value	Carrying Amount	Estimated fair value
Balance sheet assets				
Cash and due from banks	\$77,815	\$ 77,815	\$54,288	\$ 54,288
Federal funds sold	912	912	446	446
Interest-bearing deposits	40,507	40,507	145,048	145,048
Securities available for sale	623,857	623,857	460,797	460,797
Securities held to maturity	77,641	77,831	80,463	79,639
Other investments, at cost	26,477	26,477	14,840	14,840
Loans held for sale	4,285	4,285	9,562	9,562
Derivative financial instruments	3,577	3,577	4,016	4,016
Loans, net	3,852,973	3,867,481	3,114,752	3,125,701
State tax credits, held for sale	35,247	36,857	38,071	41,264
Accrued interest receivable	11,923	11,923	11,117	11,117

Balance sheet liabilities

Edgar Filing: ENTERPRISE FINANCIAL SERVICES CORP - Form 10-Q

Deposits	3,921,253,919,379	3,233,363,232,414
Subordinated debentures and notes	118,080 99,873	105,540 86,052
Federal Home Loan Bank advances	200,992 201,397	— —
Other borrowings	217,180 217,077	276,980 276,905
Derivative financial instruments	3,577 3,577	4,016 4,016
Accrued interest payable	1,459 1,459	1,105 1,105

25

For information regarding the methods and assumptions used to estimate the fair value of each class of financial instruments for which it is practical to estimate such value, refer to Note 19 – Fair Value Measurements in the Company's Annual Report on Form 10-K for the year ended December 31, 2016.

The following table presents the level in the fair value hierarchy for the estimated fair values of only the Company's financial instruments that are not already presented on the condensed consolidated balance sheets at fair value at June 30, 2017, and December 31, 2016.

(in thousands)	Estimated Fair Value			Balance at June 30, 2017
	Measurement at Reporting Date Using Level 1	Level 2	Level 3	
Financial Assets:				
Securities held to maturity	\$-\$77,831	\$	—	\$ 77,831
Portfolio loans, net	—	3,867,481		3,867,481
State tax credits, held for sale	—	35,583		35,583
Financial Liabilities:				
Deposits	3,328,169	591,210		3,919,379
Subordinated debentures and notes	—99,873	—		99,873
Federal Home Loan Bank advances	—201,397	—		201,397
Other borrowings	—217,077	—		217,077

(in thousands)	Estimated Fair Value			Balance at December 31, 2016
	Measurement at Reporting Date Using Level 1	Level 2	Level 3	
Financial Assets:				
Securities held to maturity	\$-\$79,639	\$	—	\$ 79,639
Portfolio loans, net	—	3,125,701		3,125,701
State tax credits, held for sale	—	37,679		37,679
Financial Liabilities:				
Deposits	2,760,202	472,212		3,232,414
Subordinated debentures and notes	—86,052	—		86,052
Other borrowings	—276,905	—		276,905

NOTE 9 - NEW AUTHORITATIVE ACCOUNTING GUIDANCE

Financial Accounting Standards Board (the "FASB") Accounting Standards Update (the "ASU") 2017-09 "Compensation - Stock Compensation (Topic 718): Scope of Modification Accounting" In May 2017, the FASB issued ASU 2017-09, "Compensation - Stock Compensation (Topic 718): Scope of Modification Accounting" which amends the scope of modification accounting for share-based payment awards. The amendments provide guidance on the types of changes to the terms or conditions of share-based payment awards to which an entity would be required to apply modification accounting under ASC 718. The amendments are effective for public business entities for annual periods beginning after December 15, 2017, including interim periods within those annual periods, with early adoption being permitted. The Company is currently evaluating the new guidance and has not determined the impact this standard may have on its financial statements.

FASB ASU 2017-08 "Receivables - Nonrefundable Fees and Other Costs (Subtopic 310-20), Premium Amortization on Purchased Callable Debt Securities" In March 2017, the FASB issued ASU 2017-08, "Receivables - Nonrefundable Fees and Other Costs (Subtopic 310-20)" which shortens the amortization period of certain callable debt securities held at a premium to the earliest call date. The amendments are effective for public business entities for annual periods beginning after December 15, 2018, including interim periods within those annual periods, with early adoption being permitted. The Company is currently evaluating the new guidance and has not determined the impact this standard may have on its financial statements.

FASB ASU 2017-04 "Intangibles - Goodwill and Other (Topic 350): Simplifying the Test for Goodwill Impairment" In January 2017, the FASB issued ASU 2017-04 "Simplifying the Test for Goodwill Impairment" which simplifies the measurement of goodwill impairment by removing step two of the goodwill impairment test. The new guidance requires goodwill impairment to be measured as the amount by which a reporting unit's carrying value exceeds its fair value; however, the loss recognized should not exceed the total amount of goodwill allocated to that reporting unit. The amendments should be applied on a prospective basis. The guidance becomes effective for testing periods beginning after January 1, 2017. The new guidance will be applied in the Company's 2017 annual impairment testing and is expected to not have an impact on the Company's consolidated financial statements.

FASB ASU 2016-15 "Statement of Cash Flows (Topic 230): Classification of Certain Cash Receipts and Cash Payments" In August 2016, the FASB issued ASU 2016-15, "Statement of Cash Flows (Topic 230)" which addresses changes to reduce the presentation diversity of certain cash receipts and cash payments in the statement of cash flows, including debt prepayment or extinguishment costs, settlement of certain debt instruments, contingent consideration payments made after a business combination, proceeds from the settlement of insurance claims, and distributions received from equity method investees. The guidance becomes effective for fiscal years beginning after December 15, 2017, including interim periods within those fiscal years, with early adoption permitted. An entity that elects early adoption must adopt all of the amendments in the same period. The new standard will be applied retrospectively, but may be applied prospectively if retrospective application would be impracticable. The Company is currently evaluating the new guidance and has not determined the impact this standard may have on its consolidated statement of cash flows.

FASB ASU 2016-13 "Financial Instruments - Credit Losses (Topic 326): Measurement of Credit Losses on Financial Instruments" In June 2016, the FASB issued ASU 2016-13, "Financial Instruments (Topic 326)" which changes the methodology for evaluating impairment of most financial instruments. The ASU replaces the currently used incurred loss model with a forward-looking expected loss model, which will generally result in a more timely recognition of losses. The guidance becomes effective for fiscal years beginning after December 15, 2019, including interim periods within those fiscal years. Early adoption is permitted for fiscal years beginning after December 15, 2018, including interim periods within those fiscal years. The Company is currently evaluating the new guidance and has not determined the impact this standard may have on its financial statements.

FASB ASU 2016-02 "Leases (Topic 842)" In February 2016, the FASB issued ASU 2016-02, "Leases (Topic 842)" which requires organizations that lease assets ("lessees") to recognize the assets and liabilities for the rights and obligations created by leases with terms of more than 12 months. The recognition, measurement, and presentation of expenses and cash flows arising from a lease by a lessee remains dependent on its classification as a finance or operating lease. The criteria for determining whether a lease is a finance or operating lease has not been significantly changed by this ASU. The ASU also requires additional disclosure of the amount, timing, and uncertainty of cash flows arising from leases, including qualitative and quantitative requirements. The guidance becomes effective for periods beginning after December 15, 2018, including interim periods therein. Early adoption will be permitted. The Company is currently evaluating the new guidance and has not determined the impact this standard may have on its consolidated balance sheets.

FASB ASU 2016-01 "Financial Instruments-Overall (Subtopic 825-10): Recognition and Measurement of Financial Assets and Financial Liabilities" In January 2016, the FASB issued ASU 2016-01, "Financial Instruments-Overall (Subtopic 825-10): Recognition and Measurement of Financial Assets and Financial Liabilities." ASU 2016-01 requires equity investments to be measured at fair value through earnings, and eliminates the available-for-sale classification for equity securities with readily determinable fair values. For financial liabilities where the fair value option has been elected, changes in fair value due to instrument-specific credit risk must be recognized in other comprehensive income. When measuring the fair value of financial instruments at amortized cost, the exit price must

be used for disclosure purposes. The ASU also requires that financial assets and liabilities be presented separately in the notes to the financial statements. This ASU becomes effective for fiscal years beginning after December 15, 2017, including interim periods therein. Early adoption is permitted with some exceptions. The Company is currently evaluating the new guidance and has not determined the impact this standard may have on its financial statements.

FASB ASU 2014-09, "Revenue from Contracts with Customers" In May 2014, the FASB issued ASU 2014-09, "Revenue from Contracts with Customers". The objective of ASU 2014-09 is to establish a single comprehensive model for entities to use in accounting for revenue arising from contracts with customers and will supersede most of the existing revenue recognition guidance, including industry-specific guidance. The core principle of ASU 2014-09 is that an entity recognizes revenue to depict the transfer of promised goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods or services. In applying the new guidance, an entity will (1) identify the contract(s) with a customer; (2) identify the performance obligations in the contract; (3) determine the transaction price; (4) allocate the transaction price to the contract's performance obligations; and (5) recognize revenue when (or as) the entity satisfies a performance obligation. ASU 2014-09 applies to all contracts with customers except those that are within the scope of other topics in the FASB Accounting Standards Codification. The new guidance was originally effective for annual reporting periods (including interim periods within those periods) beginning after December 15, 2016 for public companies. In August 2015, the FASB issued ASU 2015-14, which defers the effective date of this guidance to annual reporting periods beginning after December 15, 2017 for public companies, and permits early adoption on a limited basis. The Company has conducted its initial assessment and is currently evaluating contracts to assess and quantify accounting methodology changes resulting from the adoption of ASU 2014-09. The majority of the Company's revenues are derived from loans which are excluded from the new standard; therefore, the new guidance is not expected to have a material impact on the Company's consolidated financial position, results of operations or cash flows. The Company has not decided upon the method of adoption. Entities have the option of using either a full retrospective or modified approach of adoption.

ITEM 2: MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

Safe Harbor Statement Under the Private Securities Litigation Reform Act of 1995

Some of the information in this report contains "forward-looking statements" within the meaning of and intended to be covered by the safe harbor provisions of the Private Securities Litigation Reform Act of 1995. Forward-looking statements typically are identified with use of terms such as "may," "might," "will," "should," "expect," "plan," "anticipate," "estimate," "predict," "potential," "could," "continue" and the negative of these terms and similar words, although some forward-looking statements may be expressed differently. Forward-looking statements also include, but are not limited to, statements regarding plans, objectives, expectations or consequences of statements about the future performance, operations products and services of the Company and its subsidiaries. Our ability to predict results or the actual effect of future plans or strategies is inherently uncertain. You should be aware that our actual results could differ materially from those contained in the forward-looking statements due to a number of factors, including, but not limited to: our ability to efficiently integrate acquisitions into our operations, retain the customers of these businesses and grow the acquired operations; credit risk; changes in the appraised valuation of real estate securing impaired loans; outcomes of litigation and other contingencies; exposure to general and local economic conditions; risks associated with rapid increases or decreases in prevailing interest rates; consolidation within the banking industry; competition from banks and other financial institutions; our ability to attract and retain relationship officers and other key personnel; burdens imposed by federal and state regulation; changes in regulatory requirements; changes in accounting regulation or standards applicable to banks; and other risks discussed under the caption "Risk Factors" of our most recently filed Form 10-K or within this Form 10-Q, all of which could cause the Company's actual results to differ from those set forth in the forward-looking statements.

Readers are cautioned not to place undue reliance on our forward-looking statements, which reflect management's analysis and expectations only as of the date of such statements. Forward-looking statements speak only as of the date they are made, and the Company does not intend, and undertakes no obligation, to publicly revise or update forward-looking statements after the date of this report, whether as a result of new information, future events or otherwise, except as required by federal securities law. You should understand that it is not possible to predict or identify all risk factors. Readers should carefully review all disclosures we file from time to time with the Securities and Exchange Commission which are available on our website at www.enterprisebank.com under "Investor Relations."

Introduction

The following discussion describes the significant changes to the financial condition of the Company that have occurred during the first six months of 2017 compared to the financial condition as of December 31, 2016. In addition, this discussion summarizes the significant factors affecting the results of operations, liquidity and cash flows of the Company for the three and six months ended June 30, 2017, compared to the same periods in 2016. This discussion should be read in conjunction with the accompanying condensed consolidated financial statements included in this report and our Annual Report on Form 10-K for the year ended December 31, 2016.

Executive Summary

The Company closed its acquisition of Jefferson County Bancshares, Inc. (JCB) on February 10, 2017. The results of operations of JCB are included in our consolidated results since this date. See Item 1-Note 2 - Acquisitions for more information.

Below are highlights of our financial performance for the three and six months ended June 30, 2017, as compared to the linked quarter ended March 31, 2017, and prior year period.

(in thousands, except per share data)	For the Three Months ended/At			For the Six Months ended		
	June 30, 2017	March 31, 2017	June 30, 2016	June 30, 2017	June 30, 2016	
EARNINGS						
Total interest income	\$51,542	\$43,740	\$37,033	\$95,282	\$72,493	
Total interest expense	5,909	5,098	3,250	11,007	6,282	
Net interest income	45,633	38,642	33,783	84,275	66,211	
Provision for portfolio loans	3,623	1,533	716	5,156	1,549	
Provision reversal for PCI loans	(207)	(148)	(336)	(355)	(409)	
Net interest income after provision for loan losses	42,217	37,257	33,403	79,474	65,071	
Total noninterest income	7,934	6,976	7,049	14,910	13,054	
Total noninterest expense	32,651	26,736	21,353	59,387	42,115	
Income before income tax expense	17,500	17,497	19,099	34,997	36,010	
Income tax expense	5,545	5,106	6,747	10,651	12,633	
Net income	\$11,955	\$12,391	\$12,352	\$24,346	\$23,377	
Basic earnings per share	\$0.51	\$0.57	\$0.62	\$1.07	\$1.17	
Diluted earnings per share	0.50	0.56	0.61	1.06	1.16	
Return on average assets	0.96	% 1.10	% 1.33	% 1.02	% 1.27	%
Return on average common equity	8.78	% 10.65	% 13.57	% 9.64	% 13.02	%
Return on average tangible common equity	11.49	% 12.96	% 14.91	% 12.20	% 14.34	%
Net interest margin (fully tax equivalent)	3.98	% 3.73	% 3.93	% 3.86	% 3.90	%
Efficiency ratio	60.95	% 58.61	% 52.29	% 59.87	% 53.13	%
Tangible book value per common share	\$17.89	\$17.59	\$16.95			
ASSET QUALITY ⁽¹⁾						
Net charge-offs (recoveries)	\$6,104	\$(56)	\$(409)	\$6,048	\$(508)	
Nonperforming loans	13,081	13,847	12,813			
Classified assets	93,795	86,879	87,532			
Nonperforming loans to portfolio loans	0.34	% 0.36	% 0.44	%		
Nonperforming assets to total assets ⁽¹⁾	0.27	% 0.33	% 0.47	%		
Allowance for loan losses to portfolio loans	0.96	% 1.02	% 1.23	%		
Net charge-offs (recoveries) to average loans (annualized)	0.64	% (0.01)	% (0.06)	% 0.33	% (0.04)	%

(1) Excludes non-core acquired loans and related assets, except for their inclusion in total assets.

Below are highlights of the Company's Core performance measures, which we believe are important measures of financial performance, but are non-GAAP measures. Core performance measures include contractual interest on non-core acquired loans, but exclude incremental accretion on these loans, Gain or loss on the sale of other real estate from non-core acquired loans, and expenses directly related to non-core acquired loans and other assets formerly covered under FDIC loss share agreements. Core performance measures also exclude certain other income and expense items, such as executive separation costs, merger related expenses, facilities disposal, and the gain or loss on sale of investment securities, the Company believes to be not indicative of or useful to measure the Company's operating performance on an ongoing basis. A reconciliation of Core performance measures has been included in this MD&A section under the caption "Use of Non-GAAP Financial Measures".

(in thousands)	For the Three Months ended			For the Six Months ended		
	June 30, 2017	March 31, 2017	June 30, 2016	June 30, 2017	June 30, 2016	
CORE PERFORMANCE MEASURES (1)						
Net interest income	\$43,049	\$37,567	\$30,212	\$80,616	\$59,806	
Provision for portfolio loans	3,623	1,533	716	5,156	1,549	
Noninterest income	7,934	6,976	6,105	14,910	12,110	
Noninterest expense	27,798	24,946	20,446	52,744	40,881	
Income before income tax expense	19,562	18,064	15,155	37,626	29,486	
Income tax expense	6,329	4,916	5,237	11,245	10,134	
Net income	\$13,233	\$13,148	\$9,918	\$26,381	\$19,352	
Earnings per share	\$0.56	\$0.59	\$0.49	\$1.15	\$0.96	
Return on average assets	1.06	% 1.17	% 1.07	% 1.11	% 1.06	%
Return on average common equity	9.72	% 11.29	% 10.89	% 10.44	% 10.78	%
Return on average tangible common equity	12.72	% 13.75	% 11.98	% 13.22	% 11.87	%
Net interest margin (fully tax equivalent)	3.76	% 3.63	% 3.52	% 3.70	% 3.53	%
Efficiency ratio	54.52	% 56.01	% 56.30	% 55.21	% 56.85	%

(1) A non-GAAP measure. A reconciliation has been included in this MD&A section under the caption "Use of Non-GAAP Financial Measures."

For the six months ended June 30, 2017 compared to the six months ended June 30, 2016, the Company noted the following trends:

The Company reported net income of \$24.3 million, or \$1.06 per share, for the six months ended June 30, 2017, compared to \$23.4 million, or \$1.16 per share, for the same period in 2016. The 5% decrease in earnings per share primarily resulted from the impact of merger related expenses and higher provision for portfolio loan losses offset by increases in net interest income from core deposit-funded portfolio loan growth, growth in noninterest income, and the acquisition of JCB.

On a core basis¹, net income was \$26.4 million, or \$1.15 per share, for the six months ended June 30, 2017, compared to \$19.4 million, or \$0.96 per share, in the prior year period. The diluted earnings per share increase of \$0.19 was primarily due to higher levels of core net interest income from continued growth in earning asset balances combined with 17 basis points of core net interest margin expansion. The earnings per share contribution from this growth was partially offset by a higher provision for portfolio loan losses.

•

Net interest income for the first six months of 2017 increased \$18.1 million or 27%, from the prior year period due to strong portfolio loan growth, net interest margin expansion and the acquisition of JCB.

Net interest margin for the first six months of 2017 decreased four basis points to 3.86% when compared to the prior year period due to changes in incremental accretion of non-core acquired loans, as those results vary due to prepayment activity. Core net interest margin¹, for the first six months of 2017, excludes incremental accretion on non-core acquired loans, increased 17 basis points from the prior year primarily due to core deposit-funded portfolio loan growth improving the earning asset mix, increased yield on portfolio loans, controlled increases in deposit costs, and the acquisition of JCB.

Noninterest income for the first six months of 2017 increased \$1.9 million, or 14%, compared to the prior year period due primarily to the acquisition of JCB (\$2.2 million) as well as higher fees from customer swaps, card products, and wealth management. These increases were offset by a non-core Gain on sale of other real estate in the prior year.

Noninterest expenses were \$59.4 million for the six months ended June 30, 2017, compared to \$42.1 million for the six months ended June 30, 2016. Noninterest expenses for the six months included \$6.1 million of merger related expenses. Core noninterest expenses¹ were \$52.7 million for the six months ended June 30, 2017, compared to \$40.9 million for the prior year period due to the JCB acquisition and a full quarter of JCB's expense base.

Balance sheet highlights:

Loans – Portfolio loans increased to \$3.9 billion at June 30, 2017, increasing \$741 million when compared to December 31, 2016. Excluding the acquisition of JCB, portfolio loans organically grew by \$63 million in the first six months of 2017. On a year over year basis, portfolio loans increased \$975 million of which \$297 million was organic loan growth and \$678 million was from the acquisition of JCB. See Item 1, Note 5 – Portfolio Loans for more information.

Deposits – Total deposits at June 30, 2017 were \$3.9 billion, an increase of \$688 million, or 21% from December 31, 2016, and \$893 million, or 29%, from June 30, 2016. \$774 million of the increase in both periods is attributed to the acquisition of JCB. Core deposits, defined as total deposits excluding time deposits, were \$3.3 billion at June 30, 2017, a decrease of \$97 million, or 3% from the linked quarter, but an increase of \$822 million, or 33%, when compared to the prior year period. The trends in deposits reflect continued progress across our business lines, \$636 million of core deposits from JCB, and some seasonality.

Asset quality – Nonperforming loans were \$13.1 million at June 30, 2017, compared to \$14.9 million at December 31, 2016. Nonperforming loans represented 0.34% of portfolio loans at June 30, 2017 versus 0.48% at December 31, 2016. There were no portfolio loans that were over 90 days delinquent and still accruing at June 30, 2017 or December 31, 2016.

Provision for portfolio loan losses was \$5.2 million for the six months ended June 30, 2017, compared to \$1.5 million for the six months ended June 30, 2016. See Item 1, Note 5 – Portfolio Loans, and Provision and Allowance for Loan Losses in this section for more information.

RESULTS OF OPERATIONS

Net Interest Income

Average Balance Sheet

Non-core acquired loans were those acquired from the FDIC and were previously covered by shared-loss agreements. These loans continue to be accounted for as purchased credit impaired loans. Approximately \$48 million of loans acquired from JCB's portfolio are also accounted for as purchased credit impaired loans. However, all loans acquired from JCB are included in portfolio loans. The following table presents, for the periods indicated, certain information related to our average interest-earning assets and interest-bearing liabilities, as well as, the corresponding interest rates earned and paid, all on a tax equivalent basis.

(in thousands)	Three months ended June 30, 2017			2016		
	Average Balance	Interest Income/Expense	Average Yield/ Rate	Average Balance	Interest Income/Expense	Average Yield/ Rate
Assets						
Interest-earning assets:						
Taxable portfolio loans (1)	\$3,802,103	\$ 43,678	4.61 %	\$2,832,279	\$ 29,377	4.17 %
Tax-exempt portfolio loans (2)	42,157	712	6.77	42,253	628	5.98
Non-core acquired loans	36,767	3,189	34.79	59,110	4,419	30.07
Total loans	3,881,027	47,579	4.92	2,933,642	34,424	4.72
Taxable investments in debt and equity securities	623,305	3,697	2.38	479,844	2,464	2.07
Non-taxable investments in debt and equity securities (2)	44,476	489	4.41	48,276	531	4.42
Short-term investments	92,390	234	1.02	45,039	58	0.52
Total securities and short-term investments	760,171	4,420	2.33	573,159	3,053	2.14
Total interest-earning assets	4,641,198	51,999	4.49	3,506,801	37,477	4.30
Noninterest-earning assets:						
Cash and due from banks	76,355			56,662		
Other assets	345,167			214,880		
Allowance for loan losses	(45,507)			(44,151)		
Total assets	\$5,017,213			\$3,734,192		
Liabilities and Shareholders' Equity						
Interest-bearing liabilities:						
Interest-bearing transaction accounts	\$789,922	\$ 523	0.27 %	\$582,482	\$ 329	0.23 %
Money market accounts	1,309,864	1,938	0.59	1,029,122	1,013	0.40
Savings	200,405	125	0.25	103,564	63	0.24
Certificates of deposit	600,709	1,373	0.92	481,140	1,183	0.99
Total interest-bearing deposits	2,900,900	3,959	0.55	2,196,308	2,588	0.47
Subordinated debentures	118,072	1,288	4.37	56,807	361	2.56
Other borrowed funds	415,873	662	0.64	350,783	301	0.35
Total interest-bearing liabilities	3,434,845	5,909	0.69	2,603,898	3,250	0.50
Noninterest bearing liabilities:						
Demand deposits	1,008,700			735,580		
Other liabilities	27,386			28,582		
Total liabilities	4,470,931			3,368,060		
Shareholders' equity	546,282			366,132		
Total liabilities & shareholders' equity	\$5,017,213			\$3,734,192		

Edgar Filing: ENTERPRISE FINANCIAL SERVICES CORP - Form 10-Q

Net interest income	\$ 46,090		\$ 34,227
Net interest spread		3.80 %	3.80 %
Net interest margin		3.98 %	3.93 %

Average balances include non-accrual loans. The income on such loans is included in interest but is recognized only upon receipt. Loan fees, net of amortization of deferred loan origination fees and costs, included in interest income are approximately \$0.8 million and \$0.4 million for the three months ended June 30, 2017 and 2016 respectively.

(1) Non-taxable income is presented on a fully tax-equivalent basis using a 38.0% tax rate in 2017 and 2016. The tax-equivalent adjustments were \$0.5 million and \$0.4 million for the three months ended June 30, 2017 and 2016.

(in thousands)	Six months ended June 30, 2017			2016		
	Average Balance	Interest Income/Expense	Average Yield/ Rate	Average Balance	Interest Income/Expense	Average Yield/ Rate
Assets						
Interest-earning assets:						
Taxable portfolio loans (1)	\$3,635,296	\$ 81,505	4.52 %	\$2,786,733	\$ 57,687	4.16 %
Tax-exempt portfolio loans (2)	43,482	1,405	6.52	41,542	1,288	6.24
Non-core acquired loans	38,020	4,859	25.77	64,071	8,310	26.08
Total loans	3,716,798	87,769	4.76	2,892,346	67,285	4.68
Taxable investments in debt and equity securities	602,070	6,995	2.34	472,567	4,923	2.09
Non-taxable investments in debt and equity securities (2)	50,518	1,111	4.43	48,836	1,069	4.40
Short-term investments	81,867	364	0.90	46,547	119	0.51
Total securities and short-term investments	734,455	8,470	2.33	567,950	6,111	2.16
Total interest-earning assets	4,451,253	96,239	4.36	3,460,296	73,396	4.27
Noninterest-earning assets:						
Cash and due from banks	75,794			55,829		
Other assets	314,478			215,623		
Allowance for loan losses	(44,899)			(43,998)		
Total assets	\$4,796,626			\$3,687,750		
Liabilities and Shareholders' Equity						
Interest-bearing liabilities:						
Interest-bearing transaction accounts	\$777,731	\$ 1,198	0.31 %	\$567,083	\$ 635	0.23 %
Money market accounts	1,251,929	3,431	0.55	1,046,869	2,019	0.39
Savings	177,504	207	0.24	99,815	123	0.25
Certificates of deposit	574,850	2,588	0.91	432,616	2,202	1.02
Total interest-bearing deposits	2,782,014	7,424	0.54	2,146,383	4,979	0.47
Subordinated debentures	115,300	2,452	4.29	56,807	709	2.51
Other borrowed funds	403,478	1,131	0.57	366,616	594	0.33
Total interest-bearing liabilities	3,300,792	11,007	0.67	2,569,806	6,282	0.49
Noninterest bearing liabilities:						
Demand deposits	958,107			725,165		
Other liabilities	28,343			31,723		
Total liabilities	4,287,242			3,326,694		
Shareholders' equity	509,384			361,056		
Total liabilities & shareholders' equity	\$4,796,626			\$3,687,750		
Net interest income		\$ 85,232			\$ 67,114	
Net interest spread			3.69 %			3.78 %
Net interest margin			3.86 %			3.90 %

Average balances include non-accrual loans. The income on such loans is included in interest but is recognized only upon receipt. Loan fees, net of amortization of deferred loan origination fees and costs, included in interest (1) income are approximately \$1.6 million and \$0.8 million for the six months ended June 30, 2017 and 2016 respectively.

(2) Non-taxable income is presented on a fully tax-equivalent basis using a 38.0% tax rate in 2017 and 2016. The tax-equivalent adjustments were \$1.0 million and \$0.9 million for the six months ended June 30, 2017 and 2016.

Rate/Volume

The following table sets forth, on a tax-equivalent basis for the periods indicated, a summary of the changes in interest income and interest expense resulting from changes in yield/rates and volume.

34

(in thousands)	2017 compared to 2016					
	Three months ended June 30,			Six months ended June 30,		
	Increase (decrease) due to			Increase (decrease) due to		
	Volume(1)	Rate(2)	Net	Volume(1)	Rate(2)	Net
Interest earned on:						
Taxable portfolio loans	\$10,957	\$3,344	\$14,301	\$18,568	\$5,250	\$23,818
Tax-exempt portfolio loans (3)	(1)	85	84	59	58	117
Non-core acquired loans	(1,852)	622	(1,230)	(3,352)	(99)	(3,451)
Taxable investments in debt and equity securities	818	415	1,233	1,447	625	2,072
Non-taxable investments in debt and equity securities (3)	(40)	(2)	(42)	35	7	42
Short-term investments	92	84	176	124	121	245
Total interest-earning assets	\$9,974	\$4,548	\$14,522	\$16,881	\$5,962	\$22,843
Interest paid on:						
Interest-bearing transaction accounts	\$131	\$63	\$194	\$279	\$284	\$563
Money market accounts	327	598	925	445	967	1,412
Savings	61	1	62	90	(6)	84
Certificates of deposit	281	(91)	190	656	(270)	386
Subordinated debentures	560	367	927	1,037	706	1,743
Borrowed funds	65	296	361	65	472	537
Total interest-bearing liabilities	1,425	1,234	2,659	2,572	2,153	4,725
Net interest income	\$8,549	\$3,314	\$11,863	\$14,309	\$3,809	\$18,118

(1) Change in volume multiplied by yield/rate of prior period.

(2) Change in yield/rate multiplied by volume of prior period.

(3) Nontaxable income is presented on a fully-tax equivalent basis using the combined statutory federal and state income tax rate in effect for each tax year.

NOTE: The change in interest due to both rate and volume has been allocated to rate and volume changes in proportion to the relationship of the absolute dollar amounts of the change in each.

Net interest income (on a tax equivalent basis) was \$46.1 million for the three months ended June 30, 2017, compared to \$34.2 million for the same period of 2016, an increase of \$11.9 million, or 35%. The tax-equivalent net interest margin was 3.98% for the second quarter of 2017, compared to 3.73% for the first quarter of 2017, and 3.93% in the second quarter of 2016, and combined with the acquisition of JCB and portfolio loan growth, supported the \$14.5 million increase in interest income. The yield on taxable portfolio loans increased 44 basis points from the prior year period to 4.61% for the three months ended June 30, 2017. The increase was due to the impact of interest rate increases which increased yields on variable rate loans and an improved earning asset mix. The run-off of higher yielding non-core acquired loans continues to negatively impact net interest margin and resulted in a \$1.2 million decrease in interest income for the three months ended June 30, 2017.

Net interest income (on a tax equivalent basis) was \$85.2 million for the six months ended June 30, 2017, compared to \$67.1 million for the same period of 2016, an increase of \$18.1 million, or 27%. The tax-equivalent net interest margin was 3.86% for the six months ended June 30, 2017, compared to 3.90% for the prior year period. The yield on taxable portfolio loans increased 36 basis points from the prior year period to 4.52% for the six months ended June 30, 2017. The increase was due to the impact of interest rate increases which increased yields on variable rate loans and an improved earning asset mix.

Core net interest margin¹ expanded 17 basis points from the prior year to 3.70% for the six months ended June 30, 2017, primarily due to loan growth improving the earning asset mix, combined with increased yield on portfolio loans out-pacing the increase to borrowing costs. Core net interest margin also increased modestly from JCB purchase

accounting adjustments. The Company continues to manage its balance sheet to grow core net interest income and expects to increase or maintain core net interest margin over the coming quarters; however, pressure on funding costs could negate the expected trends in core net interest margin.

Non-Core Acquired Assets Contribution

The following table illustrates the non-core contribution of non-core acquired loans and related assets for the periods indicated.

(in thousands)	For the Three Months ended		For the Six Months ended	
	June 30, 2017	June 30, 2016	June 30, 2017	June 30, 2016
Accelerated cash flows and other incremental accretion	\$2,584	\$3,571	\$3,659	\$6,405
Provision reversal for non-core acquired loan losses	207	336	355	409
Gain (loss) on sale of other real estate	—	705	—	705
Other income from other real estate	—	239	—	239
Other (expenses) recovery	16	(325)	(107)	(652)
Non-core acquired assets income before income tax expense	\$2,807	\$4,526	\$3,907	\$7,106

Accelerated cash flows and other incremental accretion consists of the interest income on non-core acquired loans in excess of contractual interest on the loans. The contractual amount of interest is included in the Company's core results. At June 30, 2017, the remaining accretable yield on the remaining non-core acquired portfolio was estimated to be \$12 million and the non-accretable difference was approximately \$16 million. Accelerated cash flows and other incremental accretion from these was \$3.7 million for the six months ended June 30, 2017, and \$6.4 million for the same period in 2016. The Company estimates 2017 income from accelerated cash flows and other incremental accretion to be between \$6 million and \$8 million.

Noninterest Income

The following table presents a comparative summary of the major components of noninterest income for the periods indicated.

(in thousands)	Three months ended June 30,				
	2017	2016	Increase (decrease)		
Service charges on deposit accounts	\$2,816	\$2,188	\$628	29	%
Wealth management revenue	2,054	1,644	410	25	%
Other service charges and fee income	1,661	952	709	74	%
Gain on state tax credits, net	9	153	(144)	(94)	%
Gain on sale of other real estate - core	17	—	17	—	%
Miscellaneous income - core	1,377	1,168	209	18	%
Core noninterest income (1)	7,934	6,105	1,829	30	%
Gain (loss) on sale of other real estate from PCI loans	—	705	(705)	(100)	%
Other income from PCI assets	—	239	(239)	(100)	%
Total noninterest income	\$7,934	\$7,049	\$885	13	%

(1) A non-GAAP measure. A reconciliation has been included in this MD&A section under the caption "Use of Non-GAAP Financial Measures."

(in thousands)	Six months ended June 30,				
	2017	2016	Increase (decrease)		
Service charges on deposit accounts	\$5,326	\$4,231	\$1,095	26	%
Wealth management revenue	3,887	3,306	581	18	%
Other service charges and fee income	2,941	1,820	1,121	62	%
Gain on state tax credits, net	255	671	(416)	(62)	%
Gain on sale of other real estate - core	17	123	(106)	(86)	%
Miscellaneous income - core	2,484	1,959	525	27	%
Core noninterest income (1)	14,910	12,110	2,800	23	%
Gain (loss) on sale of other real estate from PCI loans	—	705	(705)	(100)	%
Other income from PCI assets	—	239	(239)	(100)	%
Total noninterest income	\$14,910	\$13,054	\$1,856	14	%

(1) A non-GAAP measure. A reconciliation has been included in this MD&A section under the caption "Use of Non-GAAP Financial Measures."

Noninterest income increased \$1.9 million, or 14% in the first six months of 2017 compared to the first six months of 2016. Core noninterest income¹ grew 23% in the first six months of 2017 due primarily to the JCB acquisition, approximately \$2.2 million. The Company's customer swap, card services and wealth management businesses all experienced growth in addition to JCB due to increased customer activity and new customer additions.

Noninterest Expense

The following table presents a comparative summary of the major components of noninterest expense for the periods indicated.

(in thousands)	Three months ended June 30,			
	2017	2016	Increase (decrease)	
Core expenses (1):				
Employee compensation and benefits - core	\$15,798	\$12,185	\$3,613	30 %
Occupancy - core	2,265	1,584	681	43 %
Data processing - core	1,806	1,172	634	54 %
FDIC and other insurance	650	738	(88)	(12) %
Professional fees - core	1,079	718	361	50 %
Loan, legal and other real estate expense - core	629	218	411	189 %
Other - core	5,571	3,831	1,740	45 %
Core noninterest expense (1)	27,798	20,446	7,352	36 %
Executive severance	—	332	(332)	(100) %
Merger related expenses	4,480	—	4,480	— %
Other non-core	389	250	139	56 %
Other expenses related to non-core acquired loans	(16)	325	(341)	(105) %
Total noninterest expense	\$32,651	\$21,353	\$11,298	53 %

(1) A non-GAAP measure. A reconciliation has been included in this MD&A section under the caption "Use of Non-GAAP Financial Measures."

(in thousands)	Six months ended June 30,			
	2017	2016	Increase (decrease)	
Core expenses (1):				
Employee compensation and benefits - core	\$31,006	\$24,650	\$6,356	26 %
Occupancy - core	4,194	3,241	953	29 %
Data processing - core	3,439	2,261	1,178	52 %
FDIC and other insurance	1,474	1,461	13	1 %
Professional fees - core	1,916	1,402	514	37 %
Loan, legal and other real estate expense - core	851	472	379	80 %
Other - core	9,864	7,394	2,470	33 %
Core noninterest expense (1)	52,744	40,881	11,863	29 %
Executive severance	—	332	(332)	(100) %
Merger related expenses	6,147	—	6,147	— %
Other non-core expenses	389	250	139	56 %
Other expenses related to non-core acquired loans	107	652	(545)	(84) %
Total noninterest expense	\$59,387	\$42,115	\$17,272	41 %

(1) A non-GAAP measure. A reconciliation has been included in this MD&A section under the caption "Use of Non-GAAP Financial Measures."

Noninterest expenses were \$59.4 million for the six months ended June 30, 2017, compared to \$42.1 million for the six months ended June 30, 2016. The increase was primarily due to the acquisition of JCB including merger related expenses. Core noninterest expenses¹ increased \$11.9 million to \$52.7 million for the six months ended June 30, 2017, from \$40.9 million for the prior year period. Core expenses increased from the acquisition as well as increases in

Employee compensation and benefits from investments in revenue producing personnel.

38

The Company's Core efficiency ratio¹ improved to 55.2% for the six months ended June 30, 2017 from 56.9% for the prior year, and reflects overall expense management and revenue growth trends mitigated by the acquisition of JCB. The conversion of JCB's core systems was completed late in the second quarter. The Company expects to achieve additional cost savings from the JCB transaction throughout 2017 and expects to continue to leverage its expense base principally through revenue growth. The Company anticipates core expenses, which exclude merger related costs, to be between \$25 and \$28 million per quarter for the rest of 2017. Core efficiency ratio is a non-GAAP measure. A reconciliation of Core efficiency ratio has been included in this MD&A section under the caption "Use of Non-GAAP Financial Measures".

Income Taxes

The Company's income tax expense for the six months ended June 30, 2017, which includes both federal and state taxes, was \$5.5 million compared to \$6.7 million for the same period of 2016. The combined federal and state effective income tax rate for the six months ended June 30, 2017 was 30.4%, compared to 35.1% for the same period in 2016. The decrease in the effective tax rate over the prior year period was caused by a change in accounting guidance that requires recording excess tax benefits on equity compensation awards to the income statement. For additional discussion of this guidance, refer to Note 1, Summary of Significant Accounting Policies.

Summary Balance Sheet

(in thousands)	June 30, 2017	December 31, 2016	Increase (decrease)	
Total cash and cash equivalents	\$ 117,764	\$ 198,802	(81,038)	(40.8)%
Securities	701,498	541,260	160,238	29.6 %
Loans	3,894,770	3,158,161	736,609	23.3 %
Non-core acquired loans	35,807	39,769	(3,962)	(10.0)%
Total assets	5,038,696	4,081,328	957,368	23.5 %
Deposits	3,921,251	3,233,361	687,890	21.3 %
Total liabilities	4,489,943	3,694,230	795,713	21.5 %
Total shareholders' equity	548,753	387,098	161,655	41.8 %

Assets

Loans by Type

The Company has a diversified loan portfolio, with no particular concentration of credit in any one economic sector; however, a substantial portion of the portfolio is secured by real estate, including loans classified as C&I loans. The ability of the Company's borrowers to honor their contractual obligations is partially dependent upon the local economy and its effect on the real estate market. The following table summarizes the composition of the Company's loan portfolio:

(in thousands)	June 30, 2017	December 31, 2016	Increase (decrease)	
Commercial and industrial	\$1,796,342	\$1,632,714	\$163,628	10.0 %
Commercial real estate - investor owned	750,256	544,808	205,448	37.7 %
Commercial real estate - owner occupied	525,515	350,148	175,367	50.1 %
Construction and land development	287,360	194,542	92,818	47.7 %
Residential real estate	348,678	240,760	107,918	44.8 %
Consumer and other	150,812	155,420	(4,608)	(3.0)%
Portfolio loans	3,858,963	3,118,392	740,571	23.7 %
Non-core acquired loans	35,807	39,769	(3,962)	(10.0)%
Total loans	\$3,894,770	\$3,158,161	\$736,609	23.3 %

Portfolio loans grew by \$740.6 million, (\$675 million from JCB) to \$3.9 billion at June 30, 2017, when compared to December 31, 2016. Non-core acquired loans totaled \$35.8 million at June 30, 2017, a decrease of \$4.0 million, or 10%, from December 31, 2016, primarily as a result of principal paydowns and accelerated loan payoffs.

The following table illustrates portfolio loan growth with selected specialized lending detail:

(in thousands)	At the quarter ended			Increase (decrease)	
	June 30, 2017	December 31, 2016			
Enterprise value lending	\$433,766	\$388,798	\$44,968	11.6 %	
C&I - general	894,787	794,451	100,336	12.6 %	
Life insurance premium financing	317,848	305,779	12,069	3.9 %	
Tax credits	149,941	143,686	6,255	4.4 %	
CRE, Construction, and land development	1,563,131	1,089,498	473,633	43.5 %	
Residential	348,678	240,760	107,918	44.8 %	
Other	150,812	155,420	(4,608)	(3.0)%	
Portfolio loans	\$3,858,963	\$3,118,392	\$740,571	23.7 %	

Specialized lending products, especially Enterprise value lending, Life insurance premium financing, and Tax credits, consist of primarily C&I loans, and have contributed significantly to the Company's loan growth. These loans are sourced through relationships developed with estate planning firms and private equity funds, and are not bound geographically by our traditional three markets. These specialized loan products offer opportunities to expand and diversify geographically by entering into new markets. The Company continues to focus on originating high-quality C&I relationships as they typically have variable interest rates and allow for cross selling opportunities involving other banking products. C&I loan growth also supports our efforts to maintain the Company's asset sensitive interest rate risk position. The Company expects continued loan growth, excluding the acquisition of JCB, at or above 10% for 2017.

Provision and Allowance for Loan Losses

The following table summarizes changes in the allowance for loan losses arising from loans charged off and recoveries on loans previously charged off, by loan category, and additions to the allowance charged to expense.

(in thousands)	Three months ended June 30,		Six months ended June 30,	
	2017	2016	2017	2016
Allowance at beginning of period, for portfolio loans	\$39,148	\$34,373	\$37,565	\$33,441
Loans charged off:				
Commercial and industrial	(6,035)	(157)	(6,168)	(225)
Real estate:				
Commercial	(45)	—	(45)	—
Construction and land development	(5)	—	(5)	—
Residential	(265)	—	(274)	—
Consumer and other	(39)	(6)	(68)	(11)
Total loans charged off	(6,389)	(163)	(6,560)	(236)
Recoveries of loans previously charged off:				
Commercial and industrial	57	502	137	555
Real estate:				
Commercial	103	23	201	98
Construction and land development	49	8	58	14
Residential	62	36	87	70
Consumer and other	20	3	29	7
Total recoveries of loans	291	572	512	744
Net loan charge-offs	(6,098)	409	(6,048)	508
Provision for loan losses	3,623	716	5,156	1,549
Allowance at end of period, for portfolio loans (1)	\$36,673	\$35,498	\$36,673	\$35,498
Allowance at beginning of period, for purchased credit impaired loans	\$5,477	\$9,569	\$5,844	\$10,175
Loans charged off	(48)	(495)	(48)	(983)
Recoveries of loans	—	—	—	—
Other	(96)	(187)	(315)	(232)
Net loan charge-offs	(144)	(682)	(363)	(1,215)
Provision reversal for PCI loan losses	(207)	(336)	(355)	(409)
Allowance at end of period, for purchased credit impaired loans	\$5,126	\$8,551	\$5,126	\$8,551
Total allowance at end of period	\$41,799	\$44,049	\$41,799	\$44,049
Portfolio loans, average	\$3,839,266	\$2,874,532	\$3,673,012	\$2,483,488
Portfolio loans, ending (1)	3,810,470	2,883,909	3,810,470	2,883,909
Net charge-offs to average portfolio loans (1)	0.64	% (0.06)	% 0.33	% (0.04)
Allowance for portfolio loan losses to loans (1)	0.96	% 1.23	% 0.96	% 1.23

(1) Excludes PCI loans.

The provision for loan losses on portfolio loans for the six months ended June 30, 2017 was \$5.2 million, compared to \$1.5 million for the comparable 2016 period. The provision is reflective of a chargeoff and reserve increase on a single nonperforming relationship, growth in the portfolio, and maintaining a prudent credit risk posture.

There was \$0.4 million of provision reversal for loan losses on PCI loans for the six months ended June 30, 2017, compared to provision reversal of \$0.4 million for the comparable 2016 period.

The allowance for loan losses on portfolio loans was 0.96% (1.15% excluding loans acquired from JCB) of portfolio loans at June 30, 2017 compared to 1.23% at June 30, 2016. Management believes the allowance for loan losses is adequate to absorb inherent losses in the loan portfolio.

Nonperforming assets

The following table presents the categories of nonperforming assets and other ratios as of the dates indicated.

(in thousands)	June 30, 2017	December 31, 2016	June 30, 2016	
Non-accrual loans	\$12,405	\$12,585	\$10,493	
Restructured loans	676	2,320	2,320	
Total nonperforming loans (1)	13,081	14,905	12,813	
Other real estate from originated loans	283	740	2,741	
Other real estate from acquired loans	246	240	2,160	
Total nonperforming assets (1) (2)	\$13,610	\$15,885	\$17,714	
Total assets	\$5,038,696	\$4,081,328	\$3,761,665	
Portfolio loans (1)	3,810,470	3,158,161	2,883,909	
Portfolio loans plus other real estate (1)	3,810,999	3,159,141	2,888,810	
Nonperforming loans to portfolio loans (1)	0.34	% 0.47	% 0.44	%
Nonperforming assets to total loans plus other real estate (1) (2)	0.36	0.50	0.61	
Nonperforming assets to total assets (1) (2)	0.27	0.39	0.47	
Allowance for loans to nonperforming loans (1)	280	% 252	% 277	%

(1) Excludes PCI loans, except for their inclusion in total assets.

(2) Other real estate from PCI loans included in Nonperforming assets beginning with the year ended December 31, 2015 due to termination of all existing FDIC loss share agreements.

Nonperforming loans

Nonperforming loans exclude PCI loans that are accounted for on a pool basis, as the pools are considered to be performing. See Item 1, Note 5 – Loans for more information on these loans.

Nonperforming loans based on loan type were as follows:

(in thousands)	June 30, 2017	December 31, 2016	June 30, 2016
Commercial and industrial	\$10,003	\$12,284	\$4,748
Commercial real estate	287	655	248
Construction and land development	1,489	1,904	2,576
Residential real estate	1,293	62	670
Consumer and other	9	—	4,571
Total	\$13,081	\$14,905	\$12,813

The following table summarizes the changes in nonperforming loans:

(in thousands)	Six months ended June 30,	
	2017	2016
Nonperforming loans beginning of period	\$14,905	\$9,100
Additions to nonaccrual loans	6,111	7,555
Additions to restructured loans	676	2,320
Charge-offs	(6,508)	(35)
Other principal reductions	(1,820)	(4,932)
Moved to other real estate	(283)	(283)
Nonperforming loans end of period	\$13,081	\$12,813

Other real estate

Other real estate at June 30, 2017, was \$0.5 million, compared to \$4.9 million at June 30, 2016.

The following table summarizes the changes in Other real estate:

(in thousands)	Six months ended June 30,	
	2017	2016
Other real estate beginning of period	\$980	\$8,366
Additions and expenses capitalized to prepare property for sale	2,063	2,203
Writedowns in value	(18)	—
Sales	(2,496)	(5,668)
Other real estate end of period	\$529	\$4,901

Writedowns in fair value are recorded in Loan legal and other real estate expense based on current market activity shown in the appraisals.

Liabilities

Liabilities totaled \$4.5 billion at June 30, 2017, compared to \$3.7 billion at December 31, 2016. The increase in liabilities was largely due to a \$688 million increase in total deposits and a \$201 million increase in Federal Home Loan Bank advances, partially offset by a decrease of \$60 million in other borrowings.

Deposits

(in thousands)	June 30, 2017	December 31, 2016	Increase (decrease)	
Demand deposits	\$1,019,064	\$866,756	152,308	17.6%
Interest-bearing transaction accounts	803,104	731,539	71,565	9.8%
Money market accounts	1,306,051	1,050,472	255,579	24.3%
Savings	199,950	111,435	88,515	79.4%
Certificates of deposit:				
Brokered	133,606	117,145	16,461	14.1%
Other	459,476	356,014	103,462	29.1%
Total deposits	\$3,921,251	\$3,233,361	687,890	21.3%
Non-time deposits / total deposits	85	% 85		%
Demand deposits / total deposits	26	% 27		%

Total deposits at June 30, 2017 were \$3.9 billion, an increase of \$688 million, or 21%, from December 31, 2016, primarily from the acquisition of JCB (\$675 million). The composition of our noninterest bearing deposits remained relatively stable at 26% of total deposits at June 30, 2017 compared to 27% at December 31, 2016.

Shareholders' Equity

Shareholders' equity totaled \$549 million at June 30, 2017, an increase of \$161.7 million from December 31, 2016. Significant activity during the six months ended June 30, 2017 was as follows:

- Issuance of 3.3 million shares common stock for the JCB acquisition of \$141.7 million
- Net income of \$24.3 million,
- Dividends paid on common shares of \$5.2 million.

Liquidity and Capital Resources

Liquidity

The objective of liquidity management is to ensure we have the ability to generate sufficient cash or cash equivalents in a timely and cost-effective manner to meet our commitments as they become due. Typical demands on liquidity are run-off from demand deposits, maturing time deposits which are not renewed, and fundings under credit commitments to customers. Funds are available from a number of sources, such as from the core deposit base and from loans and securities repayments and maturities.

Additionally, liquidity is provided from sales of the securities portfolio, fed fund lines with correspondent banks, borrowings from the Federal Reserve and the FHLB, the ability to acquire large and brokered deposits, and the ability to sell loan participations to other banks. These alternatives are an important part of our liquidity plan and provide flexibility and efficient execution of the asset-liability management strategy.

The Bank's Asset-Liability Management Committee oversees our liquidity position, the parameters of which are approved by the Bank's Board of Directors. Our liquidity position is monitored monthly by producing a liquidity report, which measures the amount of liquid versus non-liquid assets and liabilities. Our liquidity management framework includes measurement of several key elements, such as the loan to deposit ratio, a liquidity ratio, and a dependency ratio. The Company's liquidity framework also incorporates contingency planning to assess the nature and

volatility of funding sources and to determine alternatives to these sources. While core deposits and loan and

44

investment repayments are principal sources of liquidity, funding diversification is another key element of liquidity management and is achieved by strategically varying depositor types, terms, funding markets, and instruments.

Parent Company liquidity

The parent company's liquidity is managed to provide the funds necessary to pay dividends to shareholders, service debt, invest in subsidiaries as necessary, and satisfy other operating requirements. The parent company's primary funding sources to meet its liquidity requirements are dividends and payments from the Bank and proceeds from the issuance of equity (i.e. stock option exercises, stock offerings). Another source of funding for the parent company includes the issuance of subordinated debentures and other debt instruments.

The Company has an effective shelf registration statement on Form S-3 registering up to \$100 million of common stock, preferred stock, debt securities, and various other securities, including combinations of such securities. The Company's ability to offer securities pursuant to the registration statement depends on market conditions and the Company's continuing eligibility to use the Form S-3 under rules of the SEC.

On November 1, 2016, the Company issued \$50 million aggregate principal amount of 4.75% fixed-to-floating rate subordinated notes with a maturity date of November 1, 2026. The subordinated notes will initially bear an annual interest rate of 4.75%, with interest payable semiannually. The notes were registered pursuant to a Form S-3 which was declared effective in August 2014. Beginning November 1, 2021, the interest rate resets quarterly to the three-month LIBOR rate plus a spread of 338.7 basis points, payable quarterly. The Company used a portion of the proceeds from the issuance to pay the cash consideration at the closing of the acquisition of JCB. Regulatory guidance allows for this subordinated debt to be treated as tier 2 regulatory capital for the first five years of its term, subject to certain limitations, and then phased out of tier 2 capital pro rata over the next five years.

The Company has a senior unsecured revolving credit agreement (the "Revolving Agreement") with another bank allowing for borrowings up to \$20 million which is renewed through February 2018. The proceeds can be used for general corporate purposes. The Revolving Agreement is subject to ongoing compliance with a number of customary affirmative and negative covenants as well as specified financial covenants. As of June 30, 2017, there were no outstanding balances under the Revolving Agreement.

As of June 30, 2017, the Company had \$69.3 million of outstanding subordinated debentures as part of ten Trust Preferred Securities Pools. These securities are classified as debt but are included in regulatory capital and the related interest expense is tax-deductible, which makes them an attractive source of funding.

Bank liquidity

The Bank has a variety of funding sources available to increase financial flexibility. In addition to amounts currently borrowed, at June 30, 2017 the Bank has borrowing capacity of \$229.1 million from the FHLB of Des Moines under blanket loan pledges, and has an additional \$917.2 million available from the Federal Reserve Bank under a pledged loan agreement. The Bank has unsecured federal funds lines with six correspondent banks totaling \$85.0 million.

Investment securities are another important tool to the Bank's liquidity objectives. Of the \$623.9 million of the securities available for sale at June 30, 2017, \$418.9 million was pledged as collateral for deposits of public institutions, treasury, loan notes, and other requirements. The remaining \$204.9 million could be pledged or sold to enhance liquidity, if necessary.

In the normal course of business, the Bank enters into certain forms of off-balance sheet transactions, including unfunded loan commitments and letters of credit. These transactions are managed through the Bank's various risk management processes. Management considers both on-balance sheet and off-balance sheet transactions in its evaluation of the Company's liquidity. The Bank has \$1.3 billion in unused commitments as of June 30, 2017. While

this commitment level would exhaust the majority the Company's current liquidity resources, the nature of these commitments is such that the likelihood of funding them in the aggregate at any one time is low.

Capital Resources

45

The Company and the Bank are subject to various regulatory capital requirements administered by the Federal banking agencies. Failure to meet minimum capital requirements can initiate certain mandatory and possible additional discretionary actions by regulators that, if undertaken, could have a direct material effect on the financial statements. Under capital adequacy guidelines and the regulatory framework for prompt corrective action, the Company and its bank affiliate must meet specific capital guidelines that involve quantitative measures of assets, liabilities, and certain off-balance-sheet items as calculated under regulatory accounting practices. The banking affiliate's capital amounts and classification are also subject to qualitative judgments by the regulators about components, risk weightings and other factors.

Quantitative measures established by regulation to ensure capital adequacy require the Company and the Bank to maintain minimum amounts and ratios (set forth in the following table) of total, Tier 1, and Common equity tier 1 capital to risk-weighted assets, and of Tier 1 capital to average assets. To be categorized as "well capitalized", banks must maintain minimum total risk-based (10%), Tier 1 risk-based (8%), Common equity tier 1 risk-based (6.5%), and Tier 1 leverage ratios (5%). As of June 30, 2017, and December 31, 2016, the Company and the Bank met all capital adequacy requirements to which they are subject.

The Bank continues to exceed regulatory standards and met the definition of "well-capitalized" (the highest category) at June 30, 2017. The Company adopted the Regulatory Capital Framework (Basel III) in 2015, and has implemented the necessary processes and procedures to comply.

The following table summarizes the Company's various capital ratios at the dates indicated:

(in thousands)	June 30, 2017	December 31, 2016	Well Capitalized Minimum %	%	%
Total capital to risk-weighted assets	12.84	% 13.48	% 10.00	%	%
Tier 1 capital to risk-weighted assets	10.82	% 10.99	% 8.00	%	%
Common equity tier 1 capital to risk-weighted assets	9.34	% 9.52	% 6.50	%	%
Leverage ratio (Tier 1 capital to average assets)	10.09	% 10.42	% 5.00	%	%
Tangible common equity to tangible assets ¹	8.56	% 8.76	% N/A		
Tier 1 capital	\$493,719	\$412,865			
Total risk-based capital	585,593	506,349			

¹ Not a required regulatory capital ratio

The Company believes the tangible common equity ratio and the common equity tier 1 capital ratio are important measures of capital strength even though they are considered to be non-GAAP measures. The tables further within MD&A reconcile these ratios to U.S. GAAP.

Use of Non-GAAP Financial Measures:

The Company's accounting and reporting policies conform to generally accepted accounting principles in the United States ("GAAP") and the prevailing practices in the banking industry. However, the Company provides other financial measures, such as Core net income and net interest margin, and other Core performance measures, regulatory capital ratios, and the tangible common equity ratio, in this report that are considered "non-GAAP financial measures."

Generally, a non-GAAP financial measure is a numerical measure of a company's financial performance, financial position, or cash flows that exclude (or include) amounts that are included in (or excluded from) the most directly comparable measure calculated and presented in accordance with GAAP.

The Company considers its Core performance measures presented in this report and the included tables as important measures of financial performance, even though they are non-GAAP measures, as they provide supplemental information by which to evaluate the impact of non-core acquired loans and related income and expenses, the impact of certain non-comparable items, and the Company's operating performance on an ongoing basis. Core performance measures include contractual interest on non-core acquired loans, but exclude incremental accretion on these loans. Core performance measures also exclude the Change in FDIC receivable, Gain or loss on sale of other real estate from non-core acquired loans, and expenses directly related to non-core acquired loans and other assets formerly covered under FDIC loss share agreements. Core performance measures also exclude certain other income and expense items, such as executive separation costs, merger related expenses, facilities disposal and the gain or loss on sale of investment securities, the Company believes to be not indicative of or useful to measure the Company's operating performance on an ongoing basis. The Company believes that the tangible common equity ratio provides useful information to investors about the Company's capital strength even though it is considered to be a non-GAAP financial measure and is not part of the regulatory capital requirements to which the Company is subject.

The Company believes these non-GAAP measures and ratios, when taken together with the corresponding GAAP measures and ratios, provide meaningful supplemental information regarding the Company's performance and capital strength. The Company's management uses, and believes that investors benefit from referring to, these non-GAAP measures and ratios in assessing the Company's operating results and related trends and when forecasting future periods. However, these non-GAAP measures and ratios should be considered in addition to, and not as a substitute for or preferable to, ratios prepared in accordance with GAAP. In the following tables, the Company has provided a reconciliation of, where applicable, the most comparable GAAP financial measures and ratios to the non-GAAP financial measures and ratios, or a reconciliation of the non-GAAP calculation of the financial measure for the periods indicated.

Core Performance Measures

(in thousands)	For the Three Months ended			For the Six Months ended		
	June 30, 2017	March 31, 2017	June 30, 2016	June 30, 2017	June 30, 2016	
Net interest income	\$45,633	\$38,642	\$33,783	\$84,275	\$66,211	
Less: Incremental accretion income	2,584	1,075	3,571	3,659	6,405	
Core net interest income	43,049	37,567	30,212	80,616	59,806	
Total noninterest income	7,934	6,976	7,049	14,910	13,054	
Less: Gain (loss) on sale of other real estate from non-core acquired loans	—	—	705	—	705	
Less: Other income from non-core acquired assets	—	—	239	—	239	
Core noninterest income	7,934	6,976	6,105	14,910	12,110	
Total core revenue	50,983	44,543	36,317	95,526	71,916	
Provision for portfolio loans	3,623	1,533	716	5,156	1,549	
Total noninterest expense	32,651	26,736	21,353	59,387	42,115	
Less: Other expenses related to non-core acquired loans	(16)	123	325	107	652	
Less: Merger related expenses	4,480	1,667	—	6,147	—	
Less: Facilities disposal charge	389	—	—	389	—	
Less: Executive severance	—	—	332	—	332	
Less: Other non-core expenses	—	—	250	—	250	
Core noninterest expense	27,798	24,946	20,446	52,744	40,881	
Core income before income tax expense	19,562	18,064	15,155	37,626	29,486	
Total income tax expense	5,545	5,106	6,747	10,651	12,633	
Less: Non-core income tax expense ¹	(784)	190	1,510	(594)	2,499	
Core income tax expense	6,329	4,916	5,237	11,245	10,134	
Core net income	\$13,233	\$13,148	\$9,918	\$26,381	\$19,352	
Core diluted earnings per share	\$0.56	\$0.59	\$0.49	\$1.15	\$0.96	
Core return on average assets	1.06	% 1.17	% 1.07	% 1.11	% 1.06	%
Core return on average common equity	9.72	% 11.29	% 10.89	% 10.44	% 10.78	%
Core return on average tangible common equity	12.72	% 13.75	% 11.98	% 13.22	% 11.87	%
Core efficiency ratio	54.52	% 56.01	% 56.30	% 55.21	% 56.85	%

¹Non-core income tax expense calculated at 38% of non-core pretax income plus an estimate of taxes payable related to non-deductible JCB acquisition costs.

Net Interest Margin to Core Net Interest Margin (fully tax equivalent)

(in thousands)	Three months ended June 30,		Six months ended June 30,		
	2017	2016	2017	2016	
Net interest income	\$46,096	\$34,227	\$85,243	\$67,114	
Less: Incremental accretion income	2,584	3,571	3,659	6,405	
Core net interest income	\$43,512	\$30,656	\$81,584	\$60,709	
Average earning assets	\$4,641,198	\$3,506,801	\$4,451,253	\$3,460,296	
Reported net interest margin	3.98	% 3.93	% 3.86	% 3.90	%
Core net interest margin	3.76	% 3.52	% 3.70	% 3.53	%

Tangible common equity ratio

(in thousands)	June 30, 2017	December 31, 2016	
Total shareholders' equity	\$548,753	\$387,098	
Less: Goodwill	116,186	30,334	
Less: Intangible assets	12,458	2,151	
Tangible common equity	\$420,109	\$354,613	
Total assets	\$5,038,696	\$4,081,328	
Less: Goodwill	116,186	30,334	
Less: Intangible assets	12,458	2,151	
Tangible assets	\$4,910,052	\$4,048,843	
Tangible common equity to tangible assets	8.56	% 8.76	%

Regulatory Capital to Risk-Weighted Assets

(in thousands)	June 30, 2017	December 31, 2016		
Total shareholders' equity	\$548,753	\$387,098		
Less: Goodwill	116,186	30,334		
Less: Intangible assets, net of deferred tax liabilities	6,179	800		
Less: Unrealized gains	329	(1,741))
Plus: Other	12	24		
Common equity Tier 1 capital	426,071	357,729		
Plus: Qualifying trust preferred securities	67,600	55,100		
Plus: Other	48	36		
Tier 1 capital	493,719	412,865		
Plus: Tier 2 capital	91,874	93,484		
Total risk-based capital	585,593	506,349		
Total risk-weighted assets determined in accordance with prescribed regulatory requirements	\$4,562,322	\$3,757,161		
Common equity tier 1 to risk-weighted assets	9.34	% 9.52		%
Tier 1 capital to risk-weighted assets	10.82	% 10.99		%
Total risk-based capital to risk-weighted assets	12.84	% 13.48		%

Critical Accounting Policies

The impact and any associated risks related to the Company's critical accounting policies on business operations are described throughout "Management's Discussion and Analysis of Financial Condition and Results of Operations," where such policies affect our reported and expected financial results. For a detailed description on the application of these and other accounting policies, see below under caption Acquisitions, as well as, the Company's Annual Report on Form 10-K for the year ended December 31, 2016.

Acquisitions

Acquisitions and Business Combinations are accounted for using the acquisition method of accounting. The assets and liabilities of the acquired entities have been recorded at their estimated fair values at the date of acquisition. Goodwill represents the excess of the purchase price over the fair value of net assets acquired, including the amount assigned to identifiable intangible assets.

The purchase price allocation process requires an estimation of the fair values of the assets acquired and the liabilities assumed. When a business combination agreement provides for an adjustment to the cost of the combination contingent on future events, the Company includes an estimate of the acquisition-date fair value as part of the cost of the combination. To determine the fair values, the Company relies on third party valuations, such as appraisals, or internal valuations based on discounted cash flow analyses or other valuation techniques. The results of operations of the acquired business are included in the Company's consolidated financial statements from the respective date of acquisition. Merger-related costs are costs the Company incurs to effect a business combination. In 2017, the Company changed its presentation of Merger related expenses as a separate component of Noninterest expenses on the Condensed Consolidated Statements of Operations. Merger related expenses include costs directly related to merger or acquisition activity and include legal and professional fees, system consolidation and conversion costs, and compensation costs such as severance and retention incentives for employees impacted by acquisition activity. The

Company accounts for merger-related costs as expenses in the periods in which the costs are incurred and the services are received.

Purchased Credit Impaired ("PCI") Loans

50

Purchased credit impaired ("PCI") loans were acquired in a business combination or transaction that have evidence of deterioration of credit quality since origination and for which it is probable, at acquisition, that the Company will be unable to collect all contractually required payments receivable. PCI loans were initially recorded at fair value (as determined by the present value of expected future cash flows) with no valuation allowance. The difference between the undiscounted cash flows expected at acquisition and the investment in the loans, or the "accretable yield," is recognized as interest income on a level-yield method over the life of the loans. Contractually required payments for interest and principal that exceed the undiscounted cash flows expected at acquisition, or the "nonaccretable difference," are not recognized as a yield adjustment or as a loss accrual or a valuation allowance. The Company aggregates individual loans with common risk characteristics into pools of loans. Increases in expected cash flows subsequent to the initial investment are recognized prospectively through adjustment of the yield on the loans over their remaining lives. Decreases in expected cash flows due to an inability to collect contractual cash flows are recognized as impairment through the provision for loan losses account. Any allowance for loan loss on these pools reflect only losses incurred after the acquisition. Disposals of loans, including sales of loans, paydowns, payments in full or foreclosures result in the removal or reduction of the loan from the loan pool.

PCI loans are generally considered accruing and performing, as the loans accrete income over the estimated life of the loan, in circumstances where cash flows are reasonably estimable by management. Accordingly, PCI loans that could be contractually past due could be considered to be accruing and performing. If the timing and amount of future cash flows is not reasonably estimable or is less than the carrying value, the loans may be classified as nonaccrual loans and the purchase price discount on those loans is not recorded as interest income until the timing and amount of future cash flows can be reasonably estimable.

Allowance for Loan Losses on PCI Loans

The Company updates its cash flow projections for purchased credit-impaired loans on a periodic basis. Assumptions utilized in this process include projections related to probability of default, loss severity, prepayment, extensions and recovery lag. Projections related to probability of default and prepayment are calculated utilizing a loan migration analysis and management's assessment of loss exposure including the fair value of underlying collateral. The loan migration analysis is a matrix that specifies the probability of a loan pool transitioning into a particular delinquency or liquidation state given its current performance at the measurement date. Loss severity factors are based upon industry data and historical experience.

Any decreases in expected cash flows after the acquisition date and subsequent measurement periods are recognized by recording an impairment in allowance for loan losses through a provision for loan losses.

ITEM 3: QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

The disclosures set forth in this item are qualified by the section captioned “Safe Harbor Statement Under the Private Securities Litigation Reform Act of 1995” included in Item 2 – Management’s Discussion and Analysis of Financial Condition and Results of Operations of this report and other cautionary statements set forth elsewhere in this report.

Interest Rate Risk

Our interest rate risk management practices are aimed at optimizing net interest income, while guarding against deterioration that could be caused by certain interest rate scenarios. Interest rate sensitivity varies with different types of interest-earning assets and interest-bearing liabilities. We attempt to maintain interest-earning assets, comprised primarily of both loans and investments, and interest-bearing liabilities, comprised primarily of deposits, maturing or repricing in similar time horizons in order to minimize or eliminate any impact from market interest rate changes. In order to measure earnings sensitivity to changing rates, the Company uses an earnings simulation model.

The Company determines the sensitivity of its short-term future earnings to a hypothetical plus or minus 100 to 300 basis point parallel rate shock through the use of simulation modeling. The simulation of earnings includes the modeling of the balance sheet as an ongoing entity. Future business assumptions involving administered rate products, prepayments for future rate-sensitive balances, and the reinvestment of maturing assets and liabilities are included. These items are then modeled to project net interest income based on a hypothetical change in interest rates. The resulting net interest income for the next 12-month period is compared to the net interest income amount calculated using flat rates. This difference represents the Company's earnings sensitivity to a plus or minus 100 basis points parallel rate shock.

The following table summarizes the expected impact of interest rate shocks on net interest income (due to the current level of interest rates, the 200 and 300 basis point downward shock scenarios are not shown):

Rate Shock	Annual % change in net interest income
+ 300 bp	4.6%
+ 200 bp	3.2%
+ 100 bp	1.6%
- 100 bp	-7.2%

The Company occasionally uses interest rate derivative financial instruments as an asset/liability management tool to hedge mismatches in interest rate exposure indicated by the net interest income simulation described above. They are used to modify the Company's exposures to interest rate fluctuations and provide more stable spreads between loan yields and the rate on their funding sources.

ITEM 4: CONTROLS AND PROCEDURES

Evaluation of Disclosure Controls and Procedures

Under the supervision and with the participation of the Company's Chief Executive Officer (CEO) and the Chief Financial Officer (CFO), management has evaluated the effectiveness of the design and operation of the Company's disclosure controls and procedures pursuant to Exchange Act Rule 13a-15, as of June 30, 2017. Disclosure controls and procedures include without limitation, controls and procedures designed to ensure that information required to be disclosed by an issuer in the reports that it files or submits under the Securities Exchange Act of 1934, as amended, is accumulated and communicated to the issuer's management, including its principal executive and principal financial officers, or persons performing similar functions, as appropriate to allow timely decisions regarding required disclosure.

Based on that evaluation, the CEO and CFO concluded the Company's disclosure controls and procedures were effective as of June 30, 2017 to provide reasonable assurance of the achievement of the objectives described above.

Changes to Internal Controls

There were no changes during the period covered by this Quarterly Report on Form 10-Q in the Company's internal controls over financial reporting that have materially affected, or are reasonably likely to materially affect, those controls.

PART II - OTHER INFORMATION

ITEM 1: LEGAL PROCEEDINGS

The Company and its subsidiaries are, from time to time, parties to various legal proceedings arising out of their businesses. Management believes there are no such proceedings pending or threatened against the Company or its subsidiaries which, if determined adversely, would have a material adverse effect on the business, consolidated financial condition, results of operations or cash flows of the Company or any of its subsidiaries.

ITEM 1A: RISK FACTORS

For information regarding risk factors affecting the Company, please see the cautionary language regarding forward-looking statements in the introduction to Item 2 of Part I of this Report on Form 10-Q, and Part I, Item 1A of our Report on Form 10-K for the fiscal year ended December 31, 2016. There have been no material changes to the risk factors described in such Annual Report on Form 10-K.

ITEM 2: UNREGISTERED SALES OF EQUITY SECURITIES AND USE OF PROCEEDS

Issuer Purchases of Equity Securities

There were no repurchases of common stock by the Company during the quarter ended June 30, 2017.

ITEM 6: EXHIBITS

Exhibit No. Description

Registrant hereby agrees to furnish to the Commission, upon request, the instruments defining the rights of holders of each issue of long-term debt of Registrant and its consolidated subsidiaries.

10.1 Executive Employment Agreement by and between Enterprise Financial Services Corp and James B. Lally, dated May 2, 2017. (1)

*12.1 Computation of Ratio of Earnings to Fixed Charges and Preferred Dividends.

*31.1 Chief Executive Officer's Certification required by Rule 13(a)-14(a).

*31.2 Chief Financial Officer's Certification required by Rule 13(a)-14(a).

**32.1 Chief Executive Officer Certification pursuant to 18 U.S.C. § 1350, as adopted pursuant to section § 906 of the Sarbanes-Oxley Act of 2002.

**32.2 Chief Financial Officer Certification pursuant to 18 U.S.C. § 1350, as adopted pursuant to section § 906 of the Sarbanes-Oxley Act of 2002.

Pursuant to Rule 405 of Regulation S-T, the following financial information from the Company's Quarterly Report on Form 10-Q for the period ended June 30, 2017, is formatted in XBRL interactive data files: (i) Consolidated Balance Sheet at June 30, 2017 and December 31, 2016; (ii) Consolidated Statement of Income for the three and six months ended June 30, 2017 and 2016; (iii) Consolidated Statement of Comprehensive Income for the three and six months ended June 30, 2017 and 2016; (iv) Consolidated Statement of Changes in Equity for the six months ended June 30, 2017 and 2016; (v) Consolidated Statement of Cash Flows for the six months ended June 30, 2017 and 2016; and (vi) Notes to Financial Statements.

(1) Incorporated by reference to Exhibit 10.1 to the Current Report on Form 8-K of Enterprise Financial Services Corp, filed with the Commission on June 6, 2017.

* Filed herewith

** Furnished herewith. Notwithstanding any incorporation of this Quarterly Statement on Form 10-Q in any other filing by the Registrant, Exhibits furnished herewith and designated with two (**) shall not be deemed incorporated by reference to any other filing unless specifically otherwise set forth herein or therein.

SIGNATURES

Pursuant to the requirements of the Securities Exchange Act of 1934, as amended, the Registrant has duly caused this report to be signed on its behalf by the undersigned, thereunto duly authorized, in the City of Clayton, State of Missouri on the day of July 28, 2017.

ENTERPRISE FINANCIAL
SERVICES CORP

By: /s/ James B. Lally
James B. Lally
Chief Executive Officer

By: /s/ Keene S. Turner
Keene S. Turner
Chief Financial Officer