HORIZON BANCORP INC /IN/
Form 10-Q
August 07, 2018
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UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

WASHINGTON, D.C. 20549

FORM 10-Q

QUARTERLY REPORT UNDER SECTION 13 OR 15 (d) OF THE SECURITIES EXCHANGE ACT OF 1934
For the quarterly period ended June 30, 2018

Commission file number 0-10792

HORIZON BANCORP, INC.

(Exact name of registrant as specified in its charter)

Indiana	**35-1562417**
(State or other jurisdiction of incorporation or organization)	**(I.R.S. Employer Identification No.)**

515 Franklin Street, Michigan City, Indiana	**46360**
(Address of principal executive offices)	**(Zip Code)**

Registrant s telephone number, including area code: (219) 879-0211

Former name, former address and former fiscal year, if changed since last report: N/A

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 (or for such shorter period that the Registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes No

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T 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, smaller reporting company, or an emerging growth company. See the definitions of large accelerated filer, accelerated filer, smaller reporting company and emerging growth company in Rule 12b-2 of the Exchange Act.

Large Accelerated Filer		Accelerated Filer
Non-accelerated Filer	(Do not check if smaller reporting company)	Smaller Reporting Company

Emerging growth company

If an emerging growth company, indicate by check mark if the registrant has elected not to use the extended transition period for complying with any new or revised financial accounting standards provided pursuant to Section 13 (a) of the Exchange Act.

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

Indicate the number of shares outstanding of each of the issuer s classes of common stock, as of the latest practicable date: 38,362,640 shares of Common Stock, no par value, at August 6, 2018.

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HORIZON BANCORP, INC.

FORM 10-Q

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PART 1 FINANCIAL INFORMATION

ITEM 1. FINANCIAL STATEMENTS

HORIZON BANCORP, INC. AND SUBSIDIARIES

Condensed Consolidated Balance Sheets

(Dollar Amounts in Thousands)

	June 30 2018 (Unaudited)	December 31 2017
Assets		
Cash and due from banks	**$ 69,018**	$ 76,441
Investment securities, available for sale	**526,195**	509,665
Investment securities, held to maturity (fair value of $206,730 and $201,085)	**209,767**	200,448
Loans held for sale	**3,000**	3,094
Loans, net of allowance for loan losses of $17,071 and $16,394	**2,907,445**	2,815,601
Premises and equipment, net	**75,063**	75,529
Federal Home Loan Bank stock	**18,105**	18,105
Goodwill	**119,880**	119,880
Other intangible assets	**11,359**	12,402
Interest receivable	**12,993**	16,244
Cash value of life insurance	**76,576**	75,931
Other assets	**47,210**	40,963
Total assets	**$ 4,076,611**	$ 3,964,303
Liabilities		
Deposits		
Non-interest bearing	**$ 615,018**	$ 601,805
Interest bearing	**2,401,145**	2,279,198
Total deposits	3,016,163	2,881,003
Borrowings	**524,846**	564,157
Subordinated debentures	**37,745**	37,653
Interest payable	**1,441**	886
Other liabilities	**25,881**	23,526
Total liabilities	**3,606,076**	3,507,225
Commitments and contingent liabilities		
Stockholders Equity		
Preferred stock, Authorized, 1,000,000 shares, Issued 0 shares		

Common stock, no par value, Authorized 99,000,000 shares (Restated - See Note 1)		
Issued 38,387,709 and 38,323,604 shares (Restated - See Note 1), Outstanding 38,362,640 and 38,294,729 shares (Restated - See Note 1)		
Additional paid-in capital	**275,587**	275,059
Retained earnings	**205,535**	185,570
Accumulated other comprehensive loss	**(10,587)**	(3,551)
Total stockholders equity	**470,535**	457,078
Total liabilities and stockholders equity	**$ 4,076,611**	$ 3,964,303

See notes to condensed consolidated financial statements

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HORIZON BANCORP, INC. AND SUBSIDIARIES

Condensed Consolidated Statements of Income

(Unaudited)

(Dollar Amounts in Thousands, Except Per Share Data)

	Three Months Ended June 30		Six Months Ended June 30	
	2018	**2017**	**2018**	**2017**
Interest Income				
Loans receivable	**$ 36,308**	$ 26,795	**$ 71,439**	$ 51,586
Investment securities				
Taxable	**2,563**	2,244	**4,993**	4,650
Tax exempt	**1,870**	1,766	**3,735**	3,403
Total interest income	**40,741**	30,805	**80,167**	59,639
Interest Expense				
Deposits	**3,920**	1,721	**6,791**	3,474
Borrowed funds	**2,679**	1,338	**5,251**	2,275
Subordinated debentures	**592**	548	**1,164**	1,124
Total interest expense	**7,191**	3,607	**13,206**	6,873
Net Interest Income	**33,550**	27,198	**66,961**	52,766
Provision for loan losses	**635**	330	**1,202**	660
Net Interest Income after Provision for Loan Losses	**32,915**	26,868	**65,759**	52,106
Non-interest Income				
Service charges on deposit accounts	**1,907**	1,566	**3,795**	2,966
Wire transfer fees	**180**	178	**330**	328
Interchange fees	**1,555**	1,382	**2,883**	2,558
Fiduciary activities	**1,818**	1,943	**3,743**	3,865
Gains on sale of investment securities (includes $0 and $(3) for the three months ended June 30, 2018 and 2017, respectively, and $11 and $32 for the six months ended June 30, 2018 and 2017, respectively, related to accumulated other comprehensive earnings reclassifications)		(3)	**11**	32
Gain on sale of mortgage loans	**1,896**	2,054	**3,319**	3,968
Mortgage servicing income net of impairment	**511**	359	**860**	806
Increase in cash value of bank owned life insurance	**442**	408	**877**	872
Death benefit on bank owned life insurance	**154**		**154**	
Other income	**469**	325	**1,278**	376

Total non-interest income	**8,932**	8,212	**17,250**	15,771
Non-interest Expense				
Salaries and employee benefits	**13,809**	12,466	**28,182**	24,175
Net occupancy expenses	**2,520**	2,196	**5,486**	4,648
Data processing	**1,607**	1,502	**3,303**	2,809
Professional fees	**376**	535	**877**	1,148
Outside services and consultants	**1,267**	1,265	**2,531**	2,487
Loan expense	**1,525**	1,250	**2,782**	2,357
FDIC insurance expense	**345**	243	**655**	506
Other losses	**269**	78	**415**	128
Other expense	**3,224**	2,953	**6,548**	5,751
Total non-interest expense	**24,942**	22,488	**50,779**	44,009
Income Before Income Taxes	**16,905**	12,592	**32,230**	23,868
Income tax expense (includes $0 and $(1) for the three months ended June 30, 2018 and 2017, respectively, and $2 and $11 for the six months ended June 30, 2018 and 2017, respectively, related to income tax expense from reclassification items)	**2,790**	3,520	**5,311**	6,572
Net Income	**$ 14,115**	$ 9,072	**$ 26,919**	$ 17,296
Basic Earnings Per Share (Restated - See Note 1)	**$ 0.37**	$ 0.27	**$ 0.70**	$ 0.52
Diluted Earnings Per Share (Restated - See Note 1)	**0.37**	0.27	**0.70**	0.51

See notes to condensed consolidated financial statements

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HORIZON BANCORP, INC. AND SUBSIDIARIES

Condensed Consolidated Statements of Comprehensive Income

(Unaudited)

(Dollar Amounts in Thousands)

	Three Months Ended June 30		Six Months Ended June 30	
	2018	**2017**	**2018**	**2017**
Net Income	**$ 14,115**	$ 9,072	**$ 26,919**	$ 17,296
Other Comprehensive Income (Loss)				
Change in fair value of derivative instruments:				
Change in fair value of derivative instruments for the period	**354**	46	**1,113**	446
Income tax effect	**(75)**	(16)	**(234)**	(156)
Changes from derivative instruments	**279**	30	**879**	290
Change in securities:				
Unrealized appreciation (depreciation) for the period on AFS securities	**(829)**	3,638	**(8,943)**	6,235
Amortization from transfer of securities from available for sale to held to maturity securities	**(46)**	(58)	**(98)**	(146)
Reclassification adjustment for securities (gains) losses realized in income		3	**(11)**	(32)
Income tax effect	**187**	(1,252)	**1,903**	(2,119)
Unrealized gains (losses) on securities	**(688)**	2,331	**(7,149)**	3,938
Other Comprehensive Income (Loss), Net of Tax	**(409)**	2,361	**(6,270)**	4,228
Comprehensive Income	**$ 13,706**	$ 11,433	**$ 20,649**	$ 21,524

See notes to condensed consolidated financial statements

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HORIZON BANCORP, INC. AND SUBSIDIARIES

Condensed Consolidated Statement of Stockholders Equity

(Unaudited)

(Dollar Amounts in Thousands, Except Per Share Data)

	Preferred Stock	Additional Paid-in Capital	Retained Earnings	Accumulated Other Comprehensive Loss	Total
Balances, January 1, 2018	**$**	**$ 275,059**	**$ 185,570**	**$ (3,551)**	**$ 457,078**
Net income			26,919		26,919
Other comprehensive loss, net of tax				(6,270)	(6,270)
Amortization of unearned compensation		(79)			(79)
Exercise of stock options		444			444
Stock option expense		163			163
Reclassification of tax adjustment on accumulated other comprehensive loss			766	(766)	
Cash dividends on common stock ($0.20 per share)			(7,720)		(7,720)
Balances, June 30, 2018	**$**	**$ 275,587**	**$ 205,535**	**$ (10,587)**	**$ 470,535**

See notes to condensed consolidated financial statements

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HORIZON BANCORP, INC. AND SUBSIDIARIES

Condensed Consolidated Statements of Cash Flows

(Unaudited)

(Dollar Amounts in Thousands)

	Six Months Ended June 30	
	2018	**2017**
Operating Activities		
Net income	**$ 26,919**	$ 17,296
Items not requiring (providing) cash		
Provision for loan losses	**1,202**	660
Depreciation and amortization	**3,300**	2,820
Share based compensation	**163**	158
Mortgage servicing rights, net impairment	**24**	23
Premium amortization on securities, net	**2,985**	2,945
Gain on sale of investment securities	**(11)**	(32)
Gain on sale of mortgage loans	**(3,319)**	(3,968)
Proceeds from sales of loans	**95,218**	113,382
Loans originated for sale	**(86,812)**	(107,473)
Change in cash value life insurance	**(877)**	(872)
Death benefit on bank owned life insurance	**(154)**	
(Gain)/loss on sale of other real estate owned	**(55)**	83
Net change in:		
Interest receivable	**3,251**	(584)
Interest payable	**555**	81
Other assets	**(4,220)**	3,714
Other liabilities	**7,211**	(1,794)
Net cash provided by operating activities	**45,380**	26,439
Investing Activities		
Purchases of securities available for sale	**(84,909)**	(97,482)
Proceeds from sales, maturities, calls and principal repayments of securities available for sale	**55,723**	44,223
Purchases of securities held to maturity	**(14,207)**	(19,948)
Proceeds from maturities of securities held to maturity	**5,517**	4,853
Change in Federal Reserve and FHLB stock		8,987
Net change in loans	**(102,516)**	(128,271)
Proceeds on the sale of OREO and repossessed assets	**794**	1,057
Change in premises and equipment, net	**(1,870)**	(1,052)
Net cash received in acquisition of branch		11,000

Net cash used in investing activities	**(141,468)**	(176,633)
Financing Activities		
Net change in:		
Deposits	**135,160**	(67,254)
Borrowings	**(39,219)**	217,921
Proceeds from issuance of stock	**444**	34
Dividends paid on common stock	**(7,720)**	(5,346)
Net cash provided by financing activities	**88,665**	145,355
Net Change in Cash and Cash Equivalents	**(7,423)**	(4,839)
Cash and Cash Equivalents, Beginning of Period	**76,441**	70,832
Cash and Cash Equivalents, End of Period	**$ 69,018**	$ 65,993
Additional Supplemental Information		
Interest paid	**$ 12,651**	$ 6,786
Income taxes paid	**3,966**	6,350
Transfer of loans to other real estate	**733**	1,416
Acquisition of LaPorte, measurement period adjustments		704

See notes to condensed consolidated financial statements

HORIZON BANCORP, INC. AND SUBSIDIARIES

Notes to Condensed Consolidated Financial Statements

(Unaudited)

(Table Dollar Amounts in Thousands, Except Per Share Data)

Note 1 Accounting Policies

The accompanying unaudited condensed consolidated financial statements include the accounts of Horizon Bancorp, Inc. (Horizon or the Company) and its wholly-owned subsidiaries, including Horizon Bank (Horizon Bank or the Bank). Horizon Bank (formerly known as Horizon Bank, N.A.) was a national association until its conversion to an Indiana commercial bank effective June 23, 2017. All inter-company balances and transactions have been eliminated. The results of operations for the periods ended June 30, 2018 and June 30, 2017 are not necessarily indicative of the operating results for the full year of 2018 or 2017. The accompanying unaudited condensed consolidated financial statements reflect all adjustments that are, in the opinion of Horizon s management, necessary to fairly present the financial position, results of operations and cash flows of Horizon for the periods presented. Those adjustments consist only of normal recurring adjustments.

Certain information and note disclosures normally included in Horizon s annual financial statements prepared in accordance with accounting principles generally accepted in the United States of America have been condensed or omitted. These condensed consolidated financial statements should be read in conjunction with the consolidated financial statements and notes thereto included in Horizon s Annual Report on Form 10-K for 2017 filed with the Securities and Exchange Commission on February 28, 2018. The condensed consolidated balance sheet of Horizon as of December 31, 2017 has been derived from the audited balance sheet as of that date.

On May 15, 2018, the Board of Directors of the Company approved a three-for-two stock split of the Company s authorized common stock, no par value. All share and per share amounts in the condensed consolidated financial statements and notes thereto have been retroactively adjusted, where necessary, to reflect this three-for-two stock split. The effect of the three-for-two stock split on the outstanding common shares is that shareholders of record as of the close of business on May 31, 2018, the record date, received an additional half share of common stock held, with shareholders receiving cash in lieu of any fractional shares. The additional shares issued in the stock split were payable and issued on June 15, 2018, and the common shares began trading on a split-adjusted basis on June 19, 2018.

Basic earnings per share is computed by dividing net income available to common shareholders (net income less dividend requirements for preferred stock and accretion of preferred stock discount) by the weighted-average number of common shares outstanding. Diluted earnings per share reflect the potential dilution that could occur if securities or other contracts to issue common stock were exercised or converted into common stock.

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HORIZON BANCORP, INC. AND SUBSIDIARIES

Notes to Condensed Consolidated Financial Statements

(Unaudited)

(Table Dollar Amounts in Thousands, Except Per Share Data)

The following table shows computation of basic and diluted earnings per share.

	Three Months Ended June 30		Six Months Ended June 30	
	2018	**2017**	**2018**	**2017**
Basic earnings per share				
Net income	**$ 14,115**	$ 9,072	**$ 26,919**	$ 17,296
Weighted average common shares outstanding[1]	38,347,612	33,264,697	38,327,118	33,263,997
Basic earnings per share	**$ 0.37**	$ 0.27	**$ 0.70**	$ 0.52
Diluted earnings per share				
Net income available to common shareholders	**$ 14,115**	$ 9,072	**$ 26,919**	$ 17,296
Weighted average common shares outstanding[1]	**38,347,612**	33,264,697	**38,327,118**	33,263,997
Effect of dilutive securities:				
Restricted stock	**47,307**	45,136	**37,383**	49,807
Stock options	**124,482**	173,751	**119,820**	172,975
Weighted average common shares outstanding	**38,519,401**	33,483,584	**38,484,321**	33,486,779
	$ 0.37	$ 0.27	**$ 0.70**	$ 0.51

[1] adjusted for 3:2 stock split on June 15, 2018

There were zero shares for the three months ended June 30, 2018 and 2017, respectively, which were not included in the computation of diluted earnings per share because they were non-dilutive. There were 67,575 and zero shares for the six months ended June 30, 2018 and 2017, respectively, which were not included in the computation of diluted earnings per share because they were non-dilutive.

Horizon has share-based employee compensation plans, which are described in the notes to the financial statements included in the December 31, 2017 Annual Report on Form 10-K.

Adoption of New Accounting Standards

Financial Accounting Standards Board (FASB) Accounting Standards Update (ASU) No. 2018-02, ***Income Statement Reporting Comprehensive Income (Topic 220): Reclassification of Certain Tax Effects from Accumulated Other Comprehensive Income***

The FASB has issued ASU No. 2018-02, *Income Statement Reporting Comprehensive Income (Topic 220): Reclassification of Certain Tax Effects from Accumulated Other Comprehensive Income*. The amendments in this ASU allow a reclassification from accumulated other comprehensive income (AOCI) to retained earnings for stranded tax effects resulting from the Tax Cuts and Jobs Act. Consequently, the amendments eliminate the stranded tax effects resulting from the Tax Cuts and Jobs Act and will improve the usefulness of information reported to financial statement users. The amendments in this ASU also require certain disclosures about stranded tax effects. The amendments in this ASU are effective for all entities for fiscal years beginning after December 15, 2018, and interim periods within those fiscal years. Early adoption of the amendments in this ASU is permitted, including adoption in any interim period, (1) for public business entities for reporting periods for which financial statements have not yet been issued and (2) for all other entities for reporting periods for which financial statements have not yet been made available for issuance. The amendments in this ASU should be applied either in the period of adoption or retrospectively to each period (or periods) in which the effect of the change in the U.S. federal corporate income tax rate in the Tax Cuts and Jobs Act is recognized. The Company early adopted ASU 2018-02 on January 1, 2018 through a $766,000 cumulative-effect adjustment from AOCI to increase retained earnings related to unrealized gains and losses on available for sale securities and derivative instruments.

FASB ASU No. 2016-01, ***Financial Instruments Overall*** **(Subtopic 825-10):** ***Recognition and Measurement of Financial Assets and Financial Liabilities***

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HORIZON BANCORP, INC. AND SUBSIDIARIES

Notes to Condensed Consolidated Financial Statements

(Unaudited)

(Table Dollar Amounts in Thousands, Except Per Share Data)

The FASB has issued ASU No. 2016-01, *Financial Instruments Overall (Subtopic 825-10): Recognition and Measurement of Financial Assets and Financial Liabilities.* The new guidance is intended to improve the recognition and measurement of financial instruments. The ASU affects public and private companies, not-for-profit organizations, and employee benefit plans that hold financial assets or owe financial liabilities.

The new guidance makes targeted improvements to existing U.S. GAAP by:

Requiring equity investments (except those accounted for under the equity method of accounting, or those that result in consolidation of the investee) to be measured at fair value with changes in fair value recognized in net income;

Requiring public business entities to use the exit price notion when measuring the fair value of financial instruments for disclosure purposes;

Requiring separate presentation of financial assets and financial liabilities by measurement category and form of financial asset (i.e., securities or loans and receivables) on the balance sheet or the accompanying notes to the financial statements;

Eliminating the requirement to disclose the fair value of financial instruments measured at amortized cost for organizations that are not public business entities;

Eliminating the requirement for public business entities to disclose the method(s) and significant assumptions used to estimate the fair value that is required to be disclosed for financial instruments measured at amortized cost on the balance sheet; and

Requiring a reporting organization to present separately in other comprehensive income the portion of the total change in the fair value of a liability resulting from a change in the instrument-specific credit risk (also referred to as own credit) when the organization has elected to measure the liability at fair value in accordance with the fair value option for financial instruments.

The new guidance is effective for public companies for fiscal years beginning after December 15, 2017, including interim periods within those fiscal years. The new guidance permits early adoption of the own credit provision. In

addition, the new guidance permits early adoption of the provision that exempts private companies and not-for-profit organizations from having to disclose fair value information about financial instruments measured at amortized cost. The Company adopted ASU 2016-01 on January 1, 2018, and it did not have a material effect on its accounting for equity investments, fair value disclosures and other disclosure requirements.

FASB ASU No. 2014-09, ***Revenue from Contracts with Customers*** **(Topic 606)**

The FASB has issued ASU No. 2014-09 creating, *Revenue from Contracts with Customers (Topic 606).* The guidance in this update affects any entity that either enters into contracts with customers to transfer goods or services or enters into contracts for the transfer of nonfinancial assets unless those contracts are within the scope of other standards (for example, insurance contracts or lease contracts). The core principle of the guidance is that an entity should recognize 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. The guidance provides steps to follow to achieve the core principle. An entity should disclose sufficient information to enable users of financial statements to understand the nature, amount, timing and uncertainty of revenue and cash flows arising from contracts with customers. The amendments in this update become effective for annual periods and interim periods within those annual periods beginning after December 15, 2017. The Company adopted ASU 2014-09 on January 1, 2018 and did not identify any significant changes in the timing of revenue recognition when considering the amended accounting guidance. Additional disclosures related to revenue recognition appear in Note 1 Accounting Policies.

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HORIZON BANCORP, INC. AND SUBSIDIARIES

Notes to Condensed Consolidated Financial Statements

(Unaudited)

(Table Dollar Amounts in Thousands, Except Per Share Data)

In May 2016, the FASB issued ASU No. 2016-12, *Revenue from Contracts with Customers (Topic 606): Narrow-Scope Improvements and Practical Expedients*. The amendments do not change the core revenue recognition principle in Topic 606. The amendments provide clarifying guidance in certain narrow areas and some practical expedients.

In December 2016, the FASB issued ASU No. 2016-20, *Revenue from Contracts with Customers (Topic 606): Technical Corrections and Improvements*. The FASB board decided to issue a separate update for technical corrections and improvements to Topic 606 and other Topics amended by ASU No. 2014-09 to increase awareness of the proposals and to expedite improvements to ASU No. 2014-09. The amendment affects narrow aspects of the guidance issued in ASU No. 2014-09.

Revenue Recognition

Accounting Standards Codification 606, *Revenue from Contracts with Customers* (ASC 606) provides that an entity should recognize 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. The guidance enumerates five steps that entities should follow in achieving this core principle. Revenue generated from financial instruments, including loans and investment securities, are not included in the scope of ASC 606. The adoption of ASC 606 did not result in a change to the accounting for any of the Company s revenue streams that are within the scope of the amendments. Revenue-generating activities that are within the scope of ASC 606 and that are presented as non-interest income in the Company s consolidated statements of income include:

- Service charges and fees on deposit accounts these include general service fees charged for deposit account maintenance and activity and transaction-based fees charged for certain services, such as debit card, wire transfer or overdraft activities. Revenue is recognized when the performance obligation is completed, which is generally after a transaction is completed or monthly for account maintenance services.

- Fiduciary activities this includes periodic fees due from trust and wealth management customers for managing the customers financial assets. Fees are charged based on a standard agreement and are recognized as they are earned.

Reclassifications

Certain reclassifications have been made to the 2017 condensed consolidated financial statements to be comparable to 2018. These reclassifications had no effect on net income.

Note 2 Acquisitions

Wolverine Bancorp, Inc.

On October 17, 2017, Horizon completed the acquisition of Wolverine Bancorp, Inc., a Maryland corporation (Wolverine) and Horizon Bank s acquisition of Wolverine Bank, a federally chartered savings bank and wholly-owned subsidiary of Wolverine, through mergers effective October 17, 2017. Under the terms of the Merger Agreement, shareholders of Wolverine received 1.5228 shares of Horizon common stock and $14.00 in cash for each outstanding share of Wolverine common stock. Wolverine shares outstanding at the closing to be exchanged were 2,129,331, and the shares of Horizon common stock issued to Wolverine shareholders totaled 3,241,045. Based upon the October 16, 2017 closing price of $19.37 per share of Horizon common stock immediately prior to the effectiveness of the merger, less the consideration used to pay off Wolverine Bancorp s ESOP loan receivable, the transaction has an implied valuation of approximately $93.8 million. The Company incurred approximately $1.9 million in costs related to the acquisition. These expenses are classified in the non-interest expense section of the income statement and are primarily located in the salaries and employee benefits, professional services and other expense line items. As a result of the acquisition, the Company was able to increase its deposit base and reduce transaction costs. The Company also expects to reduce costs through economies of scale.

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HORIZON BANCORP, INC. AND SUBSIDIARIES

Notes to Condensed Consolidated Financial Statements

(Unaudited)

(Table Dollar Amounts in Thousands, Except Per Share Data)

Under the acquisition method of accounting, the total purchase price is allocated to net tangible and intangible assets based on their current estimated fair values on the date of the acquisition. Based on preliminary valuations of the fair value of tangible and intangible assets acquired and liabilities assumed, which are based on estimates and assumptions that are subject to change, the final purchase price for the Wolverine acquisition is allocated as follows:

Assets		**Liabilities**	
Cash and due from banks	$ 44,450	Deposits	
		Non-interest bearing	$ 25,221
Loans		NOW accounts	8,026
Commercial	276,167	Savings and money market	129,044
Residential mortgage	30,603	Certificates of deposit	94,688
Consumer	3,897	Total deposits	256,979
Total loans	310,667		
Premises and equipment, net	2,941	Borrowings	36,970
FRB and FHLB stock	2,700	Interest payable	214
Goodwill	26,827	Other liabilities	6,154
Core deposit intangible	2,024		
Interest receivable	584		
Other assets	3,897		
Total assets purchased	$ 394,090	Total liabilities assumed	$ 300,317
Common shares issued	$ 62,111		
Cash paid	31,662		
Total estimated purchase price	$ 93,773		

Of the total purchase price of $93.8 million, $2.0 million has been allocated to core deposit intangible. Additionally, $26.8 million has been allocated to goodwill and none of the purchase price is deductible. The core deposit intangible is being amortized over 10 years on a straight line basis.

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

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

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(Table Dollar Amounts in Thousands, Except Per Share Data)

The following table details the acquired loans that are accounted for in accordance with ASC 310-30 as of October 17, 2017.

Contractually required principal and interest at acquisition	$ 21,912
Contractual cash flows not expected to be collected (nonaccretable differences)	1,832
Expected cash flows at acquisition	20,080
Interest component of expected cash flows (accretable discount)	2,267
Fair value of acquired loans accounted for under ASC 310-30	$ 17,813

Final estimates of certain loans, those for which specific credit-related deterioration, since origination, are recorded at fair value, reflecting the present value of the amounts expected to be collected. Income recognition of these loans is based on reasonable expectation about the timing and amount of cash flows to be collected.

Lafayette Community Bancorp

On September 1, 2017, Horizon completed the acquisition of Lafayette Community Bancorp, an Indiana corporation (Lafayette) and Horizon Bank s acquisition of Lafayette Community Bank, a state-chartered bank and wholly-owned subsidiary of Lafayette, through mergers effective September 1, 2017. Under the terms of the Merger Agreement, shareholders of Lafayette received 0.8817 shares of Horizon common stock and $1.73 in cash for each outstanding share of Lafayette common stock. Lafayette shareholders owning fewer than 100 shares of common stock received $17.25 in cash for each common share. Lafayette shares outstanding at the closing to be exchanged were 1,856,679, and the shares of Horizon common stock issued to Lafayette shareholders totaled 1,636,888. Based upon the August 31, 2017 closing price of $17.45 per share of Horizon common stock immediately prior to the effectiveness of the merger, the transaction has an implied valuation of approximately $34.5 million. The Company incurred approximately $1.7 million in costs related to the acquisition. These expenses are classified in the non-interest expense section of the income statement and are primarily located in the salaries and employee benefits, professional services and other expense line items. As a result of the acquisition, the Company was able to increase its deposit base and reduce transaction costs. The Company also expects to reduce costs through economies of scale.

Horizon held 5% ownership in Lafayette immediately preceding the merger date. In accordance with ASC 805-10 Business Combinations, Horizon was required to remeasure the equity interest in Lafayette s common stock and recognize the resulting gain or loss, if any, in earnings. Since Lafayette was traded in the OTC market, the remeasurement was based on the closing price of Lafayette s common stock immediately prior to the acquisition

announcement and immediately prior to Horizon taking control of Lafayette. This remeasurement resulted in a gain of $530,000 which was recorded during the fourth quarter of 2017.

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Under the acquisition method of accounting, the total purchase price is allocated to net tangible and intangible assets based on their current estimated fair values on the date of the acquisition. Based on preliminary valuations of the fair value of tangible and intangible assets acquired and liabilities assumed, which are based on assumptions that are subject to change, the purchase price for the Lafayette acquisition is detailed in the following table.

Assets		**Liabilities**	
Cash and due from banks	$ 24,846	Deposits	
Investment securities, available for sale	6	Non-interest bearing	$ 34,990
		NOW accounts	30,174
Loans		Savings and money market	53,663
Commercial	116,258	Certificates of deposit	32,520
Residential mortgage	12,761	Total deposits	151,347
Consumer	5,280		
Total loans	134,299		
Premises and equipment, net	7,818	Interest payable	42
FHLB stock	395	Other liabilities	990
Goodwill	15,408		
Core deposit intangible	2,085		
Interest receivable	338		
Other assets	1,649		
Total assets purchased	$ 186,844	Total liabilities assumed	$ 152,379
Common shares issued	$ 30,044[1]		
Cash paid	4,421		
Total estimated purchase price	$ 34,465		

[1] This includes $955,000 of common shares previously held by Horizone.

Of the total estimated purchase price of $34.5 million, $2.1 million has been allocated to core deposit intangible. Additionally, $15.4 million has been allocated to goodwill and none of the purchase price is deductible. The core

deposit intangible will be amortized over 10 years on a straight-line basis.

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

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

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The following table details an estimate of the acquired loans that are accounted for in accordance with ASC 310-30 as of September 1, 2017.

Contractually required principal and interest at acquisition	$ 6,128
Contractual cash flows not expected to be collected (nonaccretable differences)	1,326
Expected cash flows at acquisition	4,802
Interest component of expected cash flows (accretable discount)	933
Fair value of acquired loans accounted for under ASC 310-30	$ 3,869

Final estimates of certain loans, those for which specific credit-related deterioration, since origination, are recorded at fair value, reflecting the present value of the amounts expected to be collected. Income recognition of these loans is based on reasonable expectation about the timing and amount of cash flows to be collected.

Bargersville Branch Purchase

On February 3, 2017, Horizon completed the purchase and assumption of certain assets and liabilities of a single branch of First Farmers Bank & Trust Company, in Bargersville, Indiana. Net cash of $11.0 million was received in the transaction, representing the deposit balances assumed at closing, net of amounts paid for loans acquired in the transaction of $3.4 million and a 3.0% premium on deposits. Customer deposit balances were recorded at $14.8 million and a core deposit intangible of $452,000 was recorded in the transaction, which will be amortized over 10 years on a straight line basis. There was no goodwill generated in the transaction.

The results of operations of Wolverine and Lafayette have been included in the Company s consolidated financial statements since the acquisition dates. The following schedule includes pro-forma results for the three and six months ended June 30, 2017 as if the Wolverine and Lafayette acquisitions had occurred as of the beginning of the comparable prior reporting period, which was January 1, 2016.

	Three Months Ended June 30 2017	**Six Months Ended June 30 2017**
Summary of Operations:		

Net Interest Income	$	32,038	$	62,164
Provision for Loan Losses		(1,090)		(1,337)
Net Interest Income after Provision for Loan Losses		33,128		63,501
Non-interest Income		8,662		16,565
Non-interest Expense		26,714		51,398
Income before Income Taxes		15,076		28,668
Income Tax Expense		4,549		8,412
Net Income		10,527		20,256
Net Income Available to Common Shareholders	$	10,527	$	20,256
Basic Earnings per Share	$	0.32	$	0.61
Diluted Earnings per Share	$	0.31	$	0.60

The pro-forma information includes adjustments for interest income on loans, amortization of intangibles arising from the transaction, interest expense on deposits acquired, premises expense for the banking centers acquired and the related income tax effects.

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

Note 3 Securities

The fair value of securities is as follows:

	June 30, 2018			
	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
Available for sale				
U.S. Treasury and federal agencies	$ 24,654	$	$ (435)	$ 24,219
State and municipal	136,732	300	(2,051)	134,981
Federal agency collateralized mortgage obligations	168,382	112	(4,360)	164,134
Federal agency mortgage-backed pools	203,593	28	(6,626)	196,995
Private labeled mortgage-backed pools				
Corporate notes	5,725	145	(4)	5,866
Total available for sale investment securities	$ 539,086	$ 585	$ (13,476)	$ 526,195
Held to maturity				
State and municipal	$ 190,079	$ 1,610	$ (4,309)	$ 187,380
Federal agency collateralized mortgage obligations	5,409	8	(157)	5,260
Federal agency mortgage-backed pools	14,279	55	(244)	14,090
Total held to maturity investment securities	$ 209,767	$ 1,673	$ (4,710)	$ 206,730

	December 31, 2017			
	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value

Available for sale				
U.S. Treasury and federal agencies	$ 19,277	$	$ (225)	$ 19,052
State and municipal	148,045	2,189	(670)	149,564
Federal agency collateralized mortgage obligations	132,871	45	(2,551)	130,365
Federal agency mortgage-backed pools	211,487	155	(2,985)	208,657
Private labeled mortgage-backed pools	1,650		(8)	1,642
Corporate notes	272	113		385
Total available for sale investment securities	$ 513,602	$ 2,502	$ (6,439)	$ 509,665
Held to maturity				
State and municipal	$ 179,836	$ 3,493	$ (2,932)	$ 180,397
Federal agency collateralized mortgage obligations	5,734	17	(69)	5,682
Federal agency mortgage-backed pools	14,878	216	(88)	15,006
Total held to maturity investment securities	$ 200,448	$ 3,726	$ (3,089)	$ 201,085

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Based on evaluation of available evidence, including recent changes in market interest rates, credit rating information, and information obtained from regulatory filings, management believes the declines in fair value for these securities are temporary. While these securities are held in the available for sale portfolio and held-to-maturity, Horizon intends, and has the ability, to hold them until the earlier of a recovery in fair value or maturity.

Should the impairment of any of these securities become other than temporary, the cost basis of the investment will be reduced and the resulting loss recognized in net income in the period the other-than-temporary impairment is identified. At June 30, 2018, no individual investment security had an unrealized loss that was determined to be other-than-temporary.

The unrealized losses on the Company s investments in securities of state and municipal governmental agencies, U.S. Treasury and federal agencies, federal agency collateralized mortgage obligations, and federal agency mortgage-backed pools were caused by interest rate volatility and not a decline in credit quality. The contractual terms of those investments do not permit the issuer to settle the securities at a price less than the amortized cost basis of the investments. The Company expects to recover the amortized cost basis over the term of the securities. Because the Company does not intend to sell the investments and it is not likely that the Company will be required to sell the investments before recovery of their amortized cost basis, which may be at maturity, the Company did not consider those investments to be other-than-temporarily impaired at June 30, 2018.

The amortized cost and fair value of securities available for sale and held to maturity at June 30, 2018 and December 31, 2017, by contractual maturity, are shown below. Expected maturities will differ from contractual maturities because issuers may have the right to call or prepay obligations with or without call or prepayment penalties.

	June 30, 2018		December 31, 2017	
	Amortized Cost	**Fair Value**	**Amortized Cost**	**Fair Value**
Available for sale				
Within one year	$ 10,054	$ 10,013	$ 13,347	$ 13,326
One to five years	29,238	28,739	40,468	40,193
Five to ten years	80,973	79,937	50,473	51,156
After ten years	46,846	46,377	63,306	64,326
	167,111	165,066	167,594	169,001
Federal agency collateralized mortgage obligations	168,382	164,134	132,871	130,365
Federal agency mortgage-backed pools	203,593	196,995	211,487	208,657

Private labeled mortgage-backed pools			1,650	1,642
Total available for sale investment securities	$ 539,086	$ 526,195	$ 513,602	$ 509,665
Held to maturity				
Within one year	$ 5,578	$ 5,546	$ 1,948	$ 1,934
One to five years	43,825	44,383	40,603	41,531
Five to ten years	103,804	103,252	89,801	91,249
After ten years	36,872	34,199	47,484	45,683
	190,079	187,380	179,836	180,397
Federal agency collateralized mortgage obligations	5,409	5,260	5,734	5,682
Federal agency mortgage-backed pools	14,279	14,090	14,878	15,006
Total held to maturity investment securities	$ 209,767	$ 206,730	$ 200,448	$ 201,085

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The following table shows the gross unrealized losses and the fair value of the Company s investments, aggregated by investment category and length of time that individual securities have been in a continuous unrealized loss position.

	June 30, 2018					
	Less than 12 Months		12 Months or More		Total	
	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses
Available for sale						
U.S. Treasury and federal agencies	$ 20,387	$ (352)	$ 3,832	$ (83)	$ 24,219	$ (435)
State and municipal	149,412	(4,495)	37,546	(1,865)	186,958	(6,360)
Federal agency collateralized mortgage obligations	67,216	(1,507)	67,923	(3,010)	135,139	(4,517)
Federal agency mortgage-backed pools	119,369	(3,073)	84,772	(3,797)	204,141	(6,870)
Private labeled mortgage-backed pools						
Corporate notes	971	(4)			971	(4)
Total temporarily impaired securities	$ 357,355	$ (9,431)	$ 194,073	$ (8,755)	$ 551,428	$ (18,186)

	December 31, 2017					
	Less than 12 Months		12 Months or More		Total	
	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses
Available for sale						
U.S. Treasury and federal agencies	$ 15,882	$ (180)	$ 2,870	$ (45)	$ 18,752	$ (225)
State and municipal	54,312	(2,758)	30,691	(844)	85,003	(3,602)
Federal agency collateralized mortgage obligations	54,006	(589)	73,462	(2,031)	127,468	(2,620)
Federal agency mortgage-backed pools	103,926	(1,019)	86,846	(2,054)	190,772	(3,073)
Private labeled mortgage-backed pools	1,642	(8)			1,642	(8)
Total temporarily impaired securities	$ 229,768	$ (4,554)	$ 193,869	$ (4,974)	$ 423,637	$ (9,528)

Information regarding security proceeds, gross gains and gross losses are presented below.

	Three Months Ended June 30		Six Months Ended June 30	
	2018	2017	2018	2017
Sales of securities available for sale				
Proceeds	$	$ 3,013	$ 9,836	$ 5,103
Gross gains		110	37	145
Gross losses		(113)	(26)	(113)

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Note 4 Loans

	June 30 2018	December 31 2017
Commercial		
Working capital and equipment	**$ 744,842**	$ 720,477
Real estate, including agriculture	**857,336**	880,861
Tax exempt	**36,857**	36,324
Other	**33,963**	32,066
Total	**1,672,998**	1,669,728
Real estate		
1-4 family	**627,137**	599,217
Other	**7,499**	7,543
Total	**634,636**	606,760
Consumer		
Auto	**289,361**	244,003
Recreation	**13,158**	8,728
Real estate/home improvement	**38,096**	37,052
Home equity	**161,047**	165,240
Unsecured	**3,996**	3,479
Other	**2,208**	2,497
Total	**507,866**	460,999
Mortgage warehouse	**109,016**	94,508
Total loans	**2,924,516**	2,831,995
Allowance for loan losses	**(17,071)**	(16,394)
Loans, net	**$ 2,907,445**	$ 2,815,601

Commercial

Commercial loans are primarily based on the identified cash flows of the borrower and secondarily on the underlying collateral provided by the borrower. The cash flows of borrowers, however, may not be as expected, and the collateral

securing these loans may fluctuate in value. Most commercial loans are secured by the assets being financed or other business assets such as accounts receivable or inventory and may incorporate a personal guarantee; however, some short-term loans may be made on an unsecured basis. In the case of loans secured by accounts receivable, the availability of funds for the repayment of these loans may be substantially dependent on the ability of the borrower to collect amounts due from its customers.

Commercial real estate loans are viewed primarily as cash flow loans and secondarily as loans secured by real estate. Commercial real estate lending typically involves larger loan principal amounts and the repayment of these loans is generally dependent on the successful operation of the property securing the loan or the business conducted on the property securing the loan. Commercial real estate loans may be more adversely affected by conditions in the real estate markets, the general economy or fluctuations in interest rates. The properties securing the Company s commercial real estate portfolio are diverse in terms of property type, and are monitored for concentrations of credit. Management monitors and evaluates commercial real estate loans based on collateral, cash flow and risk grade criteria. As a general rule, the Company avoids financing single purpose projects unless other underwriting factors are present to help mitigate risk. In addition, management tracks the level of owner-occupied commercial real estate loans versus non-owner occupied loans.

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Real Estate and Consumer

With respect to residential loans that are secured by 1-4 family residences and are generally owner occupied, the Company generally establishes a maximum loan-to-value ratio and requires private mortgage insurance if that ratio is exceeded. Home equity loans are typically secured by a subordinate interest in 1-4 family residences, and consumer loans are secured by consumer assets such as automobiles or recreational vehicles. Some consumer loans are unsecured such as small installment loans and certain lines of credit. Repayment of these loans is primarily dependent on the personal income of the borrowers, which can be impacted by economic conditions in their market areas such as unemployment levels. Repayment can also be impacted by changes in property values on residential properties. Risk is mitigated by the fact that the loans are of smaller individual amounts and spread over a large number of borrowers.

Mortgage Warehousing

Horizon s mortgage warehouse lending has specific mortgage companies as customers of Horizon Bank. Individual mortgage loans originated by these mortgage companies are funded as a secured borrowing with a pledge of collateral under Horizon s agreement with the mortgage company. Each mortgage loan funded by Horizon undergoes an underwriting review by Horizon to the end investor guidelines and is assigned to Horizon until the loan is sold to the secondary market by the mortgage company. In addition, Horizon takes possession of each original note and forwards such note to the end investor once the mortgage company has sold the loan. At the time a loan is transferred to the secondary market, the mortgage company reacquires the loan under its option within the agreement. Due to the reacquire feature contained in the agreement, the transaction does not qualify as a sale and therefore is accounted for as a secured borrowing with a pledge of collateral pursuant to the agreement with the mortgage company. When the individual loan is sold to the end investor by the mortgage company, the proceeds from the sale of the loan are received by Horizon and used to pay off the loan balance with Horizon along with any accrued interest and any related fees. The remaining balance from the sale is forwarded to the mortgage company. These individual loans typically are sold by the mortgage company within 30 days and are seldom held more than 90 days. Interest income is accrued during this period and collected at the time each loan is sold. Fee income for each loan sold is collected when the loan is sold, and no costs are deferred due to the term between each loan funding and related payoff, which is typically less than 30 days.

Based on the agreements with each mortgage company, at any time a mortgage company can reacquire from Horizon its outstanding loan balance on an individual mortgage and regain possession of the original note. Horizon also has the option to request that the mortgage company reacquire an individual mortgage. Should this occur, Horizon would return the original note and reassign the assignment of the mortgage to the mortgage company. Also, in the event that the end investor would not be able to honor the purchase commitment and the mortgage company would not be able to reacquire its loan on an individual mortgage, Horizon would be able to exercise its rights under the agreement.

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The following table shows the recorded investment of individual loan categories.

	June 30, 2018			
	Loan Balance	Interest Due	Deferred Fees/ (Costs)	Recorded Investment
Owner occupied real estate	$ 591,273	$ 1,446	$ 2,000	$ 594,719
Non-owner occupied real estate	678,913	980	2,100	681,993
Residential spec homes	11,614	27	45	11,686
Development & spec land	34,384	97	28	34,509
Commercial and industrial	352,213	2,573	428	355,214
Total commercial	1,668,397	5,123	4,601	1,678,121
Residential mortgage	610,871	1,827	2,180	614,878
Residential construction	21,585	40		21,625
Mortgage warehouse	109,016	480		109,496
Total real estate	741,472	2,347	2,180	745,999
Direct installment	39,065	103	(576)	38,592
Indirect installment	276,317	607		276,924
Home equity	194,637	883	(1,577)	193,943
Total consumer	510,019	1,593	(2,153)	509,459
Total loans	2,919,888	9,063	4,628	2,933,579
Allowance for loan losses	(17,071)			(17,071)
Net loans	$ 2,902,817	$ 9,063	$ 4,628	$ 2,916,508

	December 31, 2017			
	Loan Balance	Interest Due	Deferred Fees/ (Costs)	Recorded Investment
Owner occupied real estate	$ 571,982	$ 1,511	$ 1,917	$ 575,410
Non-owner occupied real estate	678,945	1,138	2,478	682,561

Residential spec homes	16,431	63	80	16,574
Development & spec land	48,838	117	579	49,534
Commercial and industrial	347,871	2,572	607	351,050
Total commercial	1,664,067	5,401	5,661	1,675,129
Residential mortgage	588,358	1,776	2,375	592,509
Residential construction	16,027	39		16,066
Mortgage warehouse	94,508	480		94,988
Total real estate	698,893	2,295	2,375	703,563
Direct installment	37,841	113	(552)	37,402
Indirect installment	227,323	528	168	228,019
Home equity	197,578	889	(1,359)	197,108
Total consumer	462,742	1,530	(1,743)	462,529
Total loans	2,825,702	9,226	6,293	2,841,221
Allowance for loan losses	(16,394)			(16,394)
Net loans	$ 2,809,308	$ 9,226	$ 6,293	$ 2,824,827

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Note 5 Accounting for Certain Loans Acquired in a Transfer

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

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

The carrying amounts of those loans included in the balance sheet amounts of loans receivable are as follows:

	June 30, 2018					
	Commercial	Real Estate	Consumer	Outstanding Balance	Allowance for Loan Losses	Carrying Amount
Heartland	$ 254	$ 193	$	$ 447	$	$ 447
Summit	3,301	592		3,893		3,893
Peoples	296	112		408		408
Kosciusko	791	207		998		998
LaPorte	855	974	30	1,859		1,859
Lafayette	3,481			3,481		3,481
Wolverine	10,020			10,020		10,020
Total	$ 18,998	$ 2,078	$ 30	$ 21,106	$	$ 21,106

	December 31, 2017					
	Commercial	Real Estate	Consumer	Outstanding Balance	Allowance for	Carrying Amount

					Loan Losses	
Heartland	$ 390	$ 229	$	$ 619	$	$ 619
Summit	3,653	870		4,523		4,523
Peoples	315	126		441		441
Kosciusko	838	403		1,241		1,241
LaPorte	1,034	1,004	33	2,071		2,071
Lafayette	4,271			4,271		4,271
Wolverine	16,697			16,697		16,697
Total	$ 27,198	$ 2,632	$ 33	$ 29,863	$	$ 29,863

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Accretable yield, or income expected to be collected for the six months ended June 30, is as follows:

	Six Months Ended June 30, 2018					
	Beginning balance	Additions	Accretion	Reclassification from nonaccretable difference	Disposals	Ending balance
Heartland	$ 452	$	$ (68)	$	$ (193)	$ 191
Summit	147		(34)		(6)	107
Kosciusko	386		(40)			346
LaPorte	980		(75)		(7)	898
Lafayette	933		(176)		(2)	755
Wolverine	2,267		(538)		(680)	1,049
Total	$ 5,165	$	$ (931)	$	$ (888)	$ 3,346

	Six Months Ended June 30, 2017					
	Beginning balance	Additions	Accretion	Reclassification from nonaccretable difference	Disposals	Ending balance
Heartland	$ 557	$	$ (67)	$	$ (6)	$ 484
Summit	502		(182)		(2)	318
Peoples	389		(388)		(1)	
Kosciusko	530		(58)		(18)	454
LaPorte	1,479		(150)		(153)	1,176
Total	$ 3,457	$	$ (845)	$	$ (180)	$ 2,432

During the six months ended June 30, 2018 and 2017 the Company increased the allowance for loan losses on purchased loans by a charge to the income statement of $0 and $71,000, respectively.

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Note 6 Allowance for Loan Losses

The historical loss experience is determined by portfolio segment and is based on the actual loss history experienced by the Company over the prior one to five years. Management believes using the highest of the one, two or five-year historical loss experience is an appropriate methodology in the current economic environment, as it captures loss rates that are comparable to the current period being analyzed. The actual allowance for loan loss activity is provided below.

	Three Months Ended June 30		Six Months Ended June 30	
	2018 (Unaudited)	2017 (Unaudited)	2018 (Unaudited)	2017 (Unaudited)
Balance at beginning of the period	$ 16,474	$ 15,054	$ 16,394	$ 14,837
Loans charged-off:				
Commercial				
Owner occupied real estate			13	
Non-owner occupied real estate				
Residential spec homes				
Development & spec land		1		1
Commercial and industrial		254		259
Total commercial		255	13	260
Real estate				
Residential mortgage	3	1	15	52
Residential construction				
Mortgage warehouse				
Total real estate	3	1	15	52
Consumer				
Direct installment	49	9	104	29
Indirect installment	365	323	870	608
Home equity		21	131	71
Total consumer	414	353	1,105	708
Total loans charged-off	417	609	1,133	1,020

Recoveries of loans previously charged-off:				
Commercial				
Owner occupied real estate		1	12	1
Non-owner occupied real estate	12	3	17	25
Residential spec homes	2	2	4	4
Development & spec land				
Commercial and industrial	26	30	58	141
Total commercial	40	36	91	171
Real estate				
Residential mortgage	5	9	11	22
Residential construction				
Mortgage warehouse				
Total real estate	5	9	11	22
Consumer				
Direct installment	21	16	32	32
Indirect installment	132	152	271	265
Home equity	181	39	203	60
Total consumer	334	207	506	357
Total loan recoveries	379	252	608	550
Net loans charged-off	38	357	525	470
Provision charged to operating expense				
Commercial	985	41	(306)	928
Real estate	(117)	93	(369)	(474)
Consumer	(233)	196	1,877	206
Total provision charged to operating expense	635	330	1,202	660
Balance at the end of the period	$ 17,071	$ 15,027	$ 17,071	$ 15,027

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Certain loans are individually evaluated for impairment, and the Company s general practice is to proactively charge down impaired loans to the fair value of the underlying collateral, which is the appraised value less estimated selling costs.

Consistent with regulatory guidance, charge-offs on all loan segments are taken when specific loans, or portions thereof, are considered uncollectible. The Company s policy is to promptly charge these loans off in the period the uncollectible loss is reasonably determined.

For all loan portfolio segments except 1-4 family residential properties and consumer, the Company promptly charges-off loans, or portions thereof, when available information confirms that specific loans are uncollectible based on information that includes, but is not limited to, (1) the deteriorating financial condition of the borrower, (2) declining collateral values, and/or (3) legal action, including bankruptcy, that impairs the borrower s ability to adequately meet its obligations. For impaired loans that are considered to be solely collateral dependent, a partial charge-off is recorded when a loss has been confirmed by an updated appraisal or other appropriate valuation of the collateral.

The Company charges-off 1-4 family residential and consumer loans, or portions thereof, when the Company reasonably determines the amount of the loss. The Company adheres to timeframes established by applicable regulatory guidance which provides for the charge-down or specific allocation of 1-4 family first and junior lien mortgages to the net realizable value less costs to sell when the value is known but no later than when a loan is 180 days past due. Pursuant to such guidelines, the Company also charges-off unsecured open-end loans when the loan is contractually 90 days past due, and charges down to the net realizable value other secured loans when they are contractually 90 days past due. Loans at these respective delinquency thresholds for which the Company can clearly document that the loan is both well-secured and in the process of collection, such that collection in full will occur regardless of delinquency status, are not charged off.

The following table presents the balance in the allowance for loan losses and the recorded investment in loans by portfolio segment and based on impairment analysis:

	June 30, 2018				
	Commercial	Real Estate	Mortgage Warehousing	Consumer	Total
Allowance For Loan Losses					
Ending allowance balance attributable to loans:					
Individually evaluated for impairment	$ 184	$	$	$	$ 184

Collectively evaluated for impairment	8,681	1,761	1,084	5,361	16,887
Loans acquired with deteriorated credit quality					
Total ending allowance balance	$ 8,865	$ 1,761	$ 1,084	$ 5,361	$ 17,071
Loans:					
Individually evaluated for impairment	$ 8,999	$	$	$	$ 8,999
Collectively evaluated for impairment	1,669,122	636,503	109,496	509,459	2,924,580
Loans acquired with deteriorated credit quality					
Total ending loans balance	$ 1,678,121	$ 636,503	$ 109,496	$ 509,459	$ 2,933,579

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	December 31, 2017				
	Commercial	Real Estate	Mortgage Warehousing	Consumer	Total
Allowance For Loan Losses					
Ending allowance balance attributable to loans:					
Individually evaluated for impairment	$ 184	$	$	$	$ 184
Collectively evaluated for impairment	8,909	2,188	1,030	4,083	16,210
Loans acquired with deteriorated credit quality					
Total ending allowance balance	$ 9,093	$ 2,188	$ 1,030	$ 4,083	$ 16,394
Loans:					
Individually evaluated for impairment	$ 7,187	$	$	$	$ 7,187
Collectively evaluated for impairment	1,667,942	608,575	94,988	462,529	2,834,034
Loans acquired with deteriorated credit quality					
Total ending loans balance	$ 1,675,129	$ 608,575	$ 94,988	$ 462,529	$ 2,841,221

Note 7 Non-performing Loans and Impaired Loans

The following table presents the non-accrual, loans past due over 90 days still on accrual, and troubled debt restructured (TDRs) by class of loans:

	June 30, 2018				
	Non-accrual	Loans Past Due Over 90 Days Still Accruing	Non-peforming TDRs	Performing TDRs	Total Non-performing Loans
Commercial					
Owner occupied real estate	$ 5,629	$	$	$	$ 5,629
Non-owner occupied real estate	1,038		305		1,343
Residential spec homes					
Development & spec land	72				72
Commercial and industrial	1,943				1,943

Total commercial	8,682		305		8,987
Real estate					
Residential mortgage	1,823	11	440	1,641	3,915
Residential construction					
Mortgage warehouse					
Total real estate	1,823	11	440	1,641	3,915
Consumer					
Direct installment	54				54
Direct installment purchased					
Indirect installment	619	38			657
Home equity	1,377		149	270	1,796
Total consumer	2,050	38	149	270	2,507
Total	$ 12,555	$ 49	$ 894	$ 1,911	$ 15,409

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	December 31, 2017				
	Non-accrual	**Loans Past Due Over 90 Days Still Accruing**	**Non-peforming TDRs**	**Performing TDRs**	**Total Non-performing Loans**
Commercial					
Owner occupied real estate	$ 4,877	$	$ 11	$ 1	$ 4,889
Non-owner occupied real estate	115		440		555
Residential spec homes					
Development & spec land	176				176
Commercial and industrial	1,734				1,734
Total commercial	6,902		451	1	7,354
Real estate					
Residential mortgage	3,693		351	1,450	5,494
Residential construction				222	222
Mortgage warehouse					
Total real estate	3,693		351	1,672	5,716
Consumer					
Direct installment	160				160
Direct installment purchased					
Indirect installment	1,041	167			1,208
Home equity	1,480		211	285	1,976
Total consumer	2,681	167	211	285	3,344
Total	$ 13,276	$ 167	$ 1,013	$ 1,958	$ 16,414

Included in the $12.6 million of non-accrual loans and the $894,000 of non-performing TDRs at June 30, 2018 were $2.0 million and $0, respectively, of loans acquired for which accretable yield was recognized.

From time to time, the Bank obtains information that may lead management to believe that the collection of payments may be doubtful on a particular loan. In recognition of this, it is management s policy to convert the loan from an earning asset to a non-accruing loan. The entire balance of a loan is considered delinquent if the minimum payment contractually required to be made is not received by the specified due date. Further, it is management s policy to generally place a loan on a non-accrual status when the payment is delinquent in excess of 90 days or the loan has had

the accrual of interest discontinued by management. The officer responsible for the loan and the Chief Commercial Banking Officer and/or the Chief Operations Officer must review all loans placed on non-accrual status. Subsequent payments on non-accrual loans are recorded as a reduction of principal, and interest income is recorded only after principal recovery is reasonably assured. Non-accrual loans are returned to accrual status when, in the opinion of management, the financial position of the borrower indicates there is no longer any reasonable doubt as to the timely collection of interest or principal in accordance with the loan terms. The Company requires a period of satisfactory performance of not less than six months before returning a non-accrual loan to accrual status.

A loan becomes impaired when, based on current information, it is probable that a creditor will be unable to collect all amounts due according to the contractual terms of the loan agreement. When a loan is classified as impaired, the degree of impairment must be recognized by estimating future cash flows from the debtor. The present value of these cash flows is computed at a discount rate based on the interest rate contained in the loan agreement. However, if a particular loan has a determinable market value for its collateral, the creditor may use that value. Also, if the loan is secured and considered collateral dependent, the creditor may use the fair value of the collateral. Interest income on loans individually classified as impaired is recognized on a cash basis after all past due and current principal payments have been made.

Smaller-balance, homogeneous loans are evaluated for impairment in total. Such loans include residential first mortgage loans secured by 1 4 family residences, residential construction loans, automobile, home equity, second mortgage loans and mortgage warehouse loans. Commercial loans and mortgage loans secured by other properties are evaluated individually for impairment. When analysis of borrower operating results and financial condition indicate that underlying cash flows of a borrower s business are not adequate to meet its debt service requirements, the loan is evaluated for impairment. Often this is associated with a delay or shortfall in payments of 30 days or more. Loans are generally moved to non-accrual status when they are 90 days or more past due. These loans are often considered impaired. Impaired loans, or portions thereof, are charged off when deemed uncollectible.

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Loans for which it is probable that the Company will not collect all principal and interest due according to contractual terms, including TDRs, are measured for impairment. Allowable methods for determining the amount of impairment include the three methods described above.

The Company s TDRs are considered impaired loans and included in the allowance methodology using the guidance for impaired loans. At June 30, 2018, the type of concessions the Company has made on restructured loans has been temporary rate reductions and/or reductions in monthly payments and there have been no restructured loans with modified recorded balances. Any modification to a loan that is a concession and is not in the normal course of lending is considered a restructured loan. A restructured loan is returned to accruing status after six consecutive payments but is still reported as TDR unless the loan bears interest at a market rate. As of June 30, 2018, the Company had $2.8 million in TDRs and $1.9 million were performing according to the restructured terms and $32,000 in TDRs were returned to accrual status during the first six months of 2018. There were $70,000 specific reserves allocated to TDRs at June 30, 2018 based on the discounted cash flows or when appropriate the fair value of the collateral.

The following table presents commercial loans individually evaluated for impairment by class of loan:

	June 30, 2018						
				Three Months Ended		Six Months Ended	
	Unpaid Principal Balance	Recorded Investment	Allowance for Loan Loss Allocated	Average Balance in Impaired Loans	Cash/Accrual Interest Income Recognized	Average Balance in Impaired Loans	Cash/Accrual Interest Income Recognized
With no recorded allowance							
Commercial							
Owner occupied real estate	$ 4,765	$ 4,762	$	$ 5,271	$ 59	$ 5,303	$ 96
Non-owner occupied real estate	1,344	1,360		1,591	5	1,559	10
Residential spec homes							
Development & spec land	72	70		71		73	
Commercial and industrial	1,943	1,943		1,916	7	1,886	7
Total commercial	8,124	8,135		8,849	71	8,821	113
With an allowance recorded							
Commercial							
Owner occupied real estate	864	864	184	871		885	
Non-owner occupied real estate							

Residential spec homes							
Development & spec land							
Commercial and industrial							
Total commercial	864	864	184	871		885	
Total	$ 8,988	$ 8,999	$ 184	$ 9,720	$ 71	$ 9,706	$ 113

				June 30, 2017			
				Three Months Ended		**Six Months Ended**	
	Unpaid Principal Balance	**Recorded Investment**	**Allowance for Loan Loss Allocated**	**Average Balance in Impaired Loans**	**Cash/Accrual Interest Income Recognized**	**Average Balance in Impaired Loans**	**Cash/Accrual Interest Income Recognized**
With no recorded allowance							
Commercial							
Owner occupied real estate	$ 1,591	$ 1,592	$	$ 1,538	$ 22	$ 1,233	$ 22
Non-owner occupied real estate	467	467		471	2	432	2
Residential spec homes							
Development & spec land	107	107		230		234	
Commercial and industrial	1,474	1,474		1,023	16	619	16
Total commercial	3,639	3,640		3,262	40	2,518	40
With an allowance recorded							
Commercial							
Owner occupied real estate							
Non-owner occupied real estate							
Residential spec homes							
Development & spec land							
Commercial and industrial							
Total commercial							
Total	$ 3,639	$ 3,640	$	$ 3,262	$ 40	$ 2,518	$ 40

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The following table presents the payment status by class of loan:

	June 30, 2018					
	30-59 Days Past Due	60-89 Days Past Due	90 Days or Greater Past Due	Total Past Due	Loans Not Past Due	Total
Commercial						
Owner occupied real estate	$ 897	$ 138	$	$ 1,035	$ 590,238	$ 591,273
Non-owner occupied real estate	42	895		937	677,976	678,913
Residential spec homes					11,614	11,614
Development & spec land					34,384	34,384
Commercial and industrial	175	966		1,141	351,072	352,213
Total commercial	1,114	1,999		3,113	1,665,284	1,668,397
Real estate						
Residential mortgage	822	302	11	1,135	609,736	610,871
Residential construction					21,585	21,585
Mortgage warehouse					109,016	109,016
Total real estate	822	302	11	1,135	740,337	741,472
Consumer						
Direct installment	78	26		104	38,961	39,065
Indirect installment	1,513	256	38	1,807	274,510	276,317
Home equity	451	30		481	194,156	194,637
Total consumer	2,042	312	38	2,392	507,627	510,019
Total	$ 3,978	$ 2,613	$ 49	$ 6,640	$ 2,913,248	$ 2,919,888
Percentage of total loans	0.14%	0.09%	0.00%	0.23%	99.77%	

	December 31, 2017					
	30-59 Days Past	60-89 Days Past	90 Days or Greater	Total Past Due	Loans Not Past Due	Total

	Due	Due	Past Due			
Commercial						
Owner occupied real estate	$ 1,613	$ 1,950	$	$ 3,563	$ 568,419	$ 571,982
Non-owner occupied real estate	512	122		634	678,311	678,945
Residential spec homes					16,431	16,431
Development & spec land	31			31	48,807	48,838
Commercial and industrial	520	1		521	347,350	347,871
Total commercial	2,676	2,073		4,749	1,659,318	1,664,067
Real estate						
Residential mortgage	1,248	49		1,297	587,061	588,358
Residential construction	63			63	15,964	16,027
Mortgage warehouse					94,508	94,508
Total real estate	1,311	49		1,360	697,533	698,893
Consumer						
Direct installment	78	10		88	37,753	37,841
Indirect installment	1,859	244	167	2,270	225,053	227,323
Home equity	502	527		1,029	196,549	197,578
Total consumer	2,439	781	167	3,387	459,355	462,742
Total	$ 6,426	$ 2,903	$ 167	$ 9,496	$ 2,816,206	$ 2,825,702
Percentage of total loans	0.23%	0.10%	0.01%	0.34%	99.66%	

The entire balance of a loan is considered delinquent if the minimum payment contractually required to be made is not received by the specified due date.

Horizon Bank s processes for determining credit quality differ slightly depending on whether a new loan or a renewed loan is being underwritten, or whether an existing loan is being re-evaluated for credit quality. The latter usually occurs upon receipt of current financial information or other pertinent data that would trigger a change in the loan grade.

For new and renewed commercial loans, the Bank s Credit Department, which acts independently of the loan officer, assigns the credit quality grade to the loan. Loan grades for loans with an aggregate credit exposure that exceeds the authorities in the respective markets (ranging from $1,000,000 to $3,500,000) are validated by the Loan Committee, which is chaired by the Chief Commercial Banking Officer (CCBO).

Commercial loan officers are responsible for reviewing their loan portfolios and reporting any adverse material change to the CCBO or Loan Committee. When circumstances warrant a change in the credit quality grade, loan officers are required to notify the CCBO and the Credit Department of the change in the loan grade. Downgrades are accepted immediately by the CCBO, however, lenders must present their factual information to either the Loan Committee or the CCBO when recommending an upgrade.

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The CCBO, or his designee, meets weekly with loan officers to discuss the status of past-due loans and classified loans. These meetings are also designed to give the loan officers an opportunity to identify an existing loan that should be downgraded to a classified grade.

Monthly, senior management meets with the Watch Committee, which reviews all of the past due, classified, and impaired loans and the relative trends of these assets. This committee also reviews the actions taken by management regarding foreclosure mitigation, loan extensions, troubled debt restructures, other real estate owned and personal property repossessions. The information reviewed in this meeting acts as a precursor for developing management s analysis of the adequacy of the Allowance for Loan and Lease Losses.

For residential real estate and consumer loans, Horizon uses a grading system based on delinquency. Loans that are 90 days or more past due, on non-accrual, or are classified as a TDR are graded Substandard. After being 90 to 120 days delinquent a loan is charged off unless it is well secured and in the process of collection. If the latter case exists, the loan is placed on non-accrual. Occasionally a mortgage loan may be graded as Special Mention. When this situation arises, it is because the characteristics of the loan and the borrower fit the definition of a Risk Grade 5 described below, which is normally used for grading commercial loans. Loans not graded Substandard are considered Pass.

Horizon Bank employs a nine-grade rating system to determine the credit quality of commercial loans. The first five grades represent acceptable quality, and the last four grades mirror the criticized and classified grades used by the bank regulatory agencies (special mention, substandard, doubtful, and loss). The loan grade definitions are detailed below.

Risk Grade 1: Excellent (Pass)

Loans secured by liquid collateral, such as certificates of deposit, reputable bank letters of credit, or other cash equivalents; loans that are guaranteed or otherwise backed by the full faith and credit of the United States government or an agency thereof, such as the Small Business Administration; or loans to any publicly held company with a current long-term debt rating of A or better.

Risk Grade 2: Good (Pass)

Loans to businesses that have strong financial statements containing an unqualified opinion from a CPA firm and at least three consecutive years of profits; loans supported by unaudited financial statements containing strong balance sheets, five consecutive years of profits, a five-year satisfactory relationship with the Bank, and key balance sheet and income statement trends that are either stable or positive; loans secured by publicly traded marketable securities where there is no impediment to liquidation; loans to individuals backed by liquid personal assets and unblemished credit history; or loans to publicly held companies with current long-term debt ratings of Baa or better.

Risk Grade 3: Satisfactory (Pass)

Loans supported by financial statements (audited or unaudited) that indicate average or slightly below average risk and having some deficiency or vulnerability to changing economic conditions; loans with some weakness but offsetting features of other support are readily available; loans that are meeting the terms of repayment, but which may be susceptible to deterioration if adverse factors are encountered. Loans may be graded Satisfactory when there is no recent information on which to base a current risk evaluation and the following conditions apply:

At inception, the loan was properly underwritten, did not possess an unwarranted level of credit risk, and the loan met the above criteria for a risk grade of Excellent, Good, or Satisfactory;

At inception, the loan was secured with collateral possessing a loan value adequate to protect the Bank from loss.

The loan has exhibited two or more years of satisfactory repayment with a reasonable reduction of the principal balance.

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During the period that the loan has been outstanding, there has been no evidence of any credit weakness. Some examples of weakness include slow payment, lack of cooperation by the borrower, breach of loan covenants, or the borrower is in an industry known to be experiencing problems. If any of these credit weaknesses is observed, a lower risk grade may be warranted.

Risk Grade 4 Satisfactory/Monitored:

Loans in this category are considered to be of acceptable credit quality, but contain greater credit risk than Satisfactory loans. Borrower displays acceptable liquidity, leverage, and earnings performance within the Bank s minimum underwriting guidelines. The level of risk is acceptable but conditioned on the proper level of loan officer supervision. Loans that normally fall into this grade include acquisition, construction and development loans and income producing properties that have not reached stabilization.

Risk Grade 4W Management Watch:

Loans in this category are considered to be of acceptable quality, but with above normal risk. Borrower displays potential indicators of weakness in the primary source of repayment resulting in a higher reliance on secondary sources of repayment. Balance sheet may exhibit weak liquidity and/or high leverage. There is inconsistent earnings performance without the ability to sustain adverse economic conditions. Borrower may be operating in a declining industry or the property type, as for a commercial real estate loan, may be unstablized, high risk or in decline. These loans require an increased level of loan officer supervision and monitoring to assure that any deterioration is addressed in a timely fashion.

Risk Grade 5: Special Mention

Loans which possess some credit deficiency or potential weakness which deserves close attention. Such loans pose an unwarranted financial risk that, if not corrected, could weaken the loan by adversely impacting the future repayment ability of the borrower. The key distinctions of a Special Mention classification are that (1) it is indicative of an unwarranted level of risk and (2) weaknesses are considered potential, not defined, impairments to the primary source of repayment. These loans may be to borrowers with adverse trends in financial performance, collateral value and/or marketability, or balance sheet strength.

Risk Grade 6: Substandard

One or more of the following characteristics may be exhibited in loans classified Substandard:

Loans which possess a defined credit weakness. The likelihood that a loan will be paid from the primary source of repayment is uncertain. Financial deterioration is under way and very close attention is warranted to ensure that the loan is collected without loss.

Loans are inadequately protected by the current net worth and paying capacity of the obligor.

The primary source of repayment is gone, and the Bank is forced to rely on a secondary source of repayment, such as collateral liquidation or guarantees.

Loans have a distinct possibility that the Bank will sustain some loss if deficiencies are not corrected.

Unusual courses of action are needed to maintain a high probability of repayment.

The borrower is not generating enough cash flow to repay loan principal; however, it continues to make interest payments.

The lender is forced into a subordinated or unsecured position due to flaws in documentation.

Loans have been restructured so that payment schedules, terms, and collateral represent concessions to the borrower when compared to the normal loan terms.

The lender is seriously contemplating foreclosure or legal action due to the apparent deterioration in the loan.

There is a significant deterioration in market conditions to which the borrower is highly vulnerable.

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Risk Grade 7: Doubtful

One or more of the following characteristics may be present in loans classified Doubtful:

Loans have all of the weaknesses of those classified as Substandard. However, based on existing conditions, these weaknesses make full collection of principal highly improbable.

The primary source of repayment is gone, and there is considerable doubt as to the quality of the secondary source of repayment.

The possibility of loss is high but because of certain important pending factors which may strengthen the loan, loss classification is deferred until the exact status of repayment is known.

Risk Grade 8: Loss

Loans are considered uncollectible and of such little value that continuing to carry them as assets is not feasible. Loans will be classified Loss when it is neither practical nor desirable to defer writing off or reserving all or a portion of a basically worthless asset, even though partial recovery may be possible at some time in the future.

The following table presents loans by credit grades.

	June 30, 2018				
	Pass	Special Mention	Substandard	Doubtful	Total
Commercial					
Owner occupied real estate	$ 569,089	$ 5,772	$ 16,412	$	$ 591,273
Non-owner occupied real estate	667,031	5,888	5,994		678,913
Residential spec homes	11,614				11,614
Development & spec land	34,168	144	72		34,384
Commercial and industrial	335,442	4,719	12,052		352,213
Total commercial	1,617,344	16,523	34,530		1,668,397
Real estate					

Residential mortgage	606,967		3,904		610,871
Residential construction	21,585				21,585
Mortgage warehouse	109,016				109,016
Total real estate	737,568		3,904		741,472
Consumer					
Direct installment	39,011		54		39,065
Indirect installment	275,660		657		276,317
Home equity	192,841		1,796		194,637
Total consumer	507,512		2,507		510,019
Total	$ 2,862,424	$ 16,523	$ 40,941	$	$ 2,919,888
Percentage of total loans	98.03%	0.57%	1.40%	0.00%	

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	December 31, 2017				
	Pass	Special Mention	Substandard	Doubtful	Total
Commercial					
Owner occupied real estate	$ 545,158	$ 8,622	$ 18,202	$	$ 571,982
Non-owner occupied real estate	670,074	3,864	5,007		678,945
Residential spec homes	16,431				16,431
Development & spec land	47,726	886	226		48,838
Commercial and industrial	326,756	7,448	13,667		347,871
Total commercial	1,606,145	20,820	37,102		1,664,067
Real estate					
Residential mortgage	582,864		5,494		588,358
Residential construction	15,805		222		16,027
Mortgage warehouse	94,508				94,508
Total real estate	693,177		5,716		698,893
Consumer					
Direct installment	37,681		160		37,841
Indirect installment	226,115		1,208		227,323
Home equity	195,602		1,976		197,578
Total consumer	459,398		3,344		462,742
Total	$ 2,758,720	$ 20,820	$ 46,162	$	$ 2,825,702
Percentage of total loans	97.63%	0.74%	1.63%	0.00%	

Note 8 Repurchase Agreements

The Company transfers various securities to customers in exchange for cash at the end of each business day and agrees to acquire the securities at the end of the next business day for the cash exchanged plus interest. The process is repeated at the end of each business day until the agreement is terminated. The securities underlying the agreement remained under the Bank s control.

The following table shows repurchase agreements accounted for as secured borrowings:

	June 30, 2018 Remaining Contractual Maturity of the Agreements						
	Overnight and Continuous	Up to one year	One to three years	Three to five years	Five to ten years	Beyond ten years	Total
Repurchase Agreements and repurchase-to-maturity transactions							
Repurchase Agreements	$ 43,702	$	$	$	$	$	$ 43,702
Securities pledged for Repurchase Agreements							
Federal agency collateralized mortgage obligations	$ 34,344	$	$	$	$	$	$ 34,344
Federal agency mortgage-backed pools	31,208						31,208
Total	$ 65,552	$	$	$	$	$	$ 65,552

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Note 9 Derivative Financial Instruments

Cash Flow Hedges

As a strategy to maintain acceptable levels of exposure to the risk of changes in future cash flow due to interest rate fluctuations, the Company entered into interest rate swap agreements for a portion of its floating rate debt. The agreements provide for the Company to receive interest from the counterparty at three month LIBOR and to pay interest to the counterparty at a weighted average fixed rate of 5.81% on a notional amount of $30.5 million at June 30, 2018 and December 31, 2017. Under the agreements, the Company pays or receives the net interest amount monthly, with the monthly settlements included in interest expense.

The Company assumed additional interest rate swap agreements as the result of the LaPorte acquisition in July 2016. The agreements provide for the Company to receive interest from the counterparty at one month LIBOR and to pay interest to the counterparty at a weighted average fixed rate of 2.31% on a notional amount of $30.0 million at June 30, 2018 and December 31, 2017. Under the agreements, the Company pays or receives the net interest amount monthly, with the monthly settlements included in interest expense.

Management has designated the interest rate swap agreement as a cash flow hedging instrument. For derivative instruments that are designated and qualify as a cash flow hedge, the effective portion of the gain or loss on the derivative is reported as a component of other comprehensive income and reclassified into earnings in the same period or periods during which the hedged transaction affects earnings. Gains and losses on the derivative representing either hedge ineffectiveness or hedge components excluded from the assessment of effectiveness are recognized in current earnings. At June 30, 2018, the Company s cash flow hedge was effective and is not expected to have a significant impact on the Company s net income over the next 12 months.

Fair Value Hedges

Fair value hedges are intended to reduce the interest rate risk associated with the underlying hedged item. The Company enters into fixed rate loan agreements as part of its lending policy. To mitigate the risk of changes in fair value based on fluctuations in interest rates, the Company has entered into interest rate swap agreements on individual loans, converting the fixed rate loans to a variable rate. For derivative instruments that are designated and qualify as a fair value hedge, the gain or loss on the derivative as well as the offsetting gain or loss on the hedged item attributable to the hedged risk are recognized in current earnings. At June 30, 2018, the Company s fair value hedges were effective and are not expected to have a significant impact on the Company s net income over the next 12 months.

The change in fair value of both the hedge instruments and the underlying loan agreements are recorded as gains or losses in interest income. The fair value hedges are considered to be highly effective and any hedge ineffectiveness was deemed not material. The notional amounts of the loan agreements being hedged were $155.7 million at June 30,

2018 and $154.6 million at December 31, 2017.

Other Derivative Instruments

The Company enters into non-hedging derivatives in the form of mortgage loan forward sale commitments with investors and commitments to originate mortgage loans as part of its mortgage banking business. At June 30, 2018, the Company s fair value of these derivatives were recorded and over the next 12 months are not expected to have a significant impact on the Company s net income.

The change in fair value of both the forward sale commitments and commitments to originate mortgage loans were recorded and the net gains or losses included in the Company s gain on sale of loans.

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The following tables summarize the fair value of derivative financial instruments utilized by Horizon:

	Asset Derivatives June 30, 2018		Liability Derivatives June 30, 2018	
	Balance Sheet Location	Fair Value	Balance Sheet Location	Fair Value
Derivatives designated as hedging instruments				
Interest rate contracts	Loans	$	Other liabilities	$ 3,579
Interest rate contracts	Other Assets	3,579	Other liabilities	969
Total derivatives desginated as hedging instruments		3,579		4,548
Derivatives not designated as hedging instruments				
Mortgage loan contracts	Other assets	257	Other liabilities	4
Total derivatives not designated as hedging instruments		257		4
Total derivatives		$ 3,836		$ 4,552

	Asset Derivatives December 31, 2017		Liability Derivatives December 31, 2017	
	Balance Sheet Location	Fair Value	Balance Sheet Location	Fair Value
Derivatives designated as hedging instruments				
Interest rate contracts	Loans	$	Other liabilities	$ 811
Interest rate contracts	Other Assets	811	Other liabilities	1,728
Total derivatives desginated as hedging instruments		811		2,539

Derivatives not designated as hedging instruments				
Mortgage loan contracts	Other assets	143	Other liabilities	3
Total derivatives not designated as hedging instruments		143		3
Total derivatives		$ 954		$ 2,542

The effect of the derivative instruments on the condensed consolidated statements of income for the three and six-month periods ending June 30 is as follows:

	Amount of Loss Recognized in Other Comprehensive Income on Derivative (Effective Portion)			
	Three Months Ended		**Six Months Ended**	
	June 30, 2018	**June 30, 2017**	**June 30, 2018**	**June 30, 2017**
Derivatives in cash flow hedging relationship				
Interest rate contracts	$ 279	$ 30	$ 879	$ 290

FASB Accounting Standards Codification (ASC) Topic 820-10-20 defines fair value as the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. Topic 820-10-55 establishes a fair value hierarchy that emphasizes the use of observable inputs and minimizes the use of unobservable inputs when measuring fair value.

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	Location of gain (loss) recognized on derivative	Amount of Gain (Loss) Recognized on Derivative			
		Three Months Ended		Six Months Ended	
		June 30, 2018	June 30, 2017	June 30, 2018	June 30, 2017
Derivative in fair value hedging relationship					
Interest rate contracts	Interest income - loans	$ 2,768	$ 679	$ 574	$ 426
Interest rate contracts	Interest income - loans	(2,768)	(679)	(574)	(426)
Total		$	$	$	$

	Location of gain (loss) recognized on derivative	Amount of Gain (Loss) Recognized on Derivative			
		Three Months Ended		Six Months Ended	
		June 30, 2018	June 30, 2017	June 30, 2018	June 30, 2017
Derivative not designated as hedging relationship					
Mortgage contracts	Other income - gain on sale of loans	$ 112	$ (153)	$ 195	$ (212)

Note 10 Disclosures about Fair Value of Assets and Liabilities

The Fair Value Measurements topic of the FASB ASC defines fair value, establishes a framework for measuring fair value and expands disclosures about fair value measurements. There are three levels of inputs that may be used to measure fair value:

Level 1 Quoted prices in active markets for identical assets or liabilities

Level 2 Observable inputs other than Level 1 prices, such as quoted prices for similar assets or liabilities; quoted prices in markets that are not active; or other inputs that are observable or can be corroborated by observable market data for substantially the full term of the assets or liabilities

Level 3 Unobservable inputs that are supported by little or no market activity and that are significant to the fair value of the assets or liabilities

Following is a description of the valuation methodologies used for instruments measured at fair value on a recurring basis and recognized in the accompanying condensed consolidated financial statements, as well as the general classification of such instruments pursuant to the valuation hierarchy. There have been no significant changes in the valuation techniques during the period ended June 30, 2018. For assets classified within Level 3 of the fair value hierarchy, the process used to develop the reported fair value is described below.

Available for sale securities

When quoted market prices are available in an active market, securities are classified within Level 1 of the valuation hierarchy. If quoted market prices are not available, then fair values are estimated by using pricing models, quoted prices of securities with similar characteristics or discounted cash flows. Level 2 securities include U.S. Treasury and federal agency securities, state and municipal securities, federal agency collateralized mortgage obligations and mortgage-backed pools and corporate notes. Level 2 securities are valued by a third party pricing service commonly used in the banking industry utilizing observable inputs. Observable inputs include dealer quotes, market spreads, cash flow analysis, the U.S. Treasury yield curve, trade execution data, market consensus prepayment spreads and available credit information and the bond s terms and conditions. The pricing provider utilizes evaluated pricing models that vary based on asset class. These models incorporate available market information including quoted prices of securities with similar characteristics and, because many fixed-income securities do not trade on a daily basis, apply available information through processes such as benchmark curves, benchmarking of like securities, sector grouping, and matrix pricing. In addition, model processes, such as an option adjusted spread model, is used to develop prepayment and interest rate scenarios for securities with prepayment features.

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Hedged loans

Certain fixed rate loans have been converted to variable rate loans by entering into interest rate swap agreements. The fair value of those fixed rate loans is based on discounting the estimated cash flows using interest rates determined by the respective interest rate swap agreement. Loans are classified within Level 2 of the valuation hierarchy based on the unobservable inputs used.

Interest rate swap agreements

The fair value of the Company s interest rate swap agreements is estimated by a third party using inputs that are primarily unobservable including a yield curve, adjusted for liquidity and credit risk, contracted terms and discounted cash flow analysis, and therefore, are classified within Level 2 of the valuation hierarchy.

The following table presents the fair value measurements of assets and liabilities recognized in the accompanying condensed consolidated financial statements measured at fair value on a recurring basis and the level within the FASB ASC fair value hierarchy in which the fair value measurements fall at the following:

	June 30, 2018			
	Fair Value	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
Available for sale securities				
U.S. Treasury and federal agencies	$ 24,219	$	$ 24,219	$
State and municipal	134,981		134,981	
Federal agency collateralized mortgage obligations	164,134		164,134	
Federal agency mortgage-backed pools	196,995		196,995	
Private labeled mortgage-backed pools				
Corporate notes	5,866		5,866	
Total available for sale securities	526,195		526,195	
Hedged loans	155,742		155,742	

Forward sale commitments	344	344
Interest rate swap agreements	3,939	3,939
Commitments to originate loans	(21)	(21)

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	December 31, 2017			
	Fair Value	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
Available for sale securities				
U.S. Treasury and federal agencies	$ 19,052	$	$ 19,052	$
State and municipal	149,564		149,564	
Federal agency collateralized mortgage obligations	130,365		130,365	
Federal agency mortgage-backed pools	208,657		208,657	
Private labeled mortgage-backed pools	1,642		1,642	
Corporate notes	385		385	
Total available for sale securities	509,665		509,665	
Hedged loans	154,575		154,575	
Forward sale commitments	143		143	
Interest rate swap agreements	(917)		(917)	
Commitments to originate loans	(3)		(3)	

Realized gains and losses included in net income for the periods are reported in the condensed consolidated statements of income as follows:

Non-interest Income	Three Months Ended		Six Months Ended	
	June 30, 2018	June 30, 2017	June 30, 2018	June 30, 2017
Total gains and losses from:				
Hedged loans	$ 976	$ 679	$ 3,744	$ 426
Fair value interest rate swap agreements	(976)	(679)	(3,744)	(426)
Derivative loan commitments	71	(153)	183	(212)
	$ 71	$ (153)	$ 183	$ (212)

Certain other assets are measured at fair value on a non-recurring basis in the ordinary course of business and are subject to fair value adjustments in certain circumstances (for example, when there is evidence of impairment):

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	Fair Value	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
June 30, 2018				
Impaired loans	$ 8,804	$	$	$ 8,804
Mortgage servicing rights	11,670			11,670
December 31, 2017				
Impaired loans	$ 6,957	$	$	$ 6,957
Mortgage servicing rights	11,602			11,602

Impaired (collateral dependent): Loans for which it is probable that the Company will not collect all principal and interest due according to contractual terms are measured for impairment. Allowable methods for determining the amount of impairment include estimating fair value using the fair value of the collateral for collateral-dependent loans.

If the impaired loan is identified as collateral dependent, then the fair value method of measuring the amount of impairment is utilized. This method requires obtaining a current independent appraisal of the collateral and applying a discount factor to the value.

Impaired loans that are collateral dependent are classified within Level 3 of the fair value hierarchy when impairment is determined using the fair value method.

Mortgage Servicing Rights (MSRs): MSRs do not trade in an active market with readily observable prices. Accordingly, the fair value of these assets is classified as Level 3. The Company determines the fair value of MSRs using an income approach model based upon the Company s month-end interest rate curve and prepayment assumptions. The model utilizes assumptions to estimate future net servicing income cash flows, including estimates of time decay, payoffs and changes in valuation inputs and assumptions. The Company reviews the valuation assumptions against this market data for reasonableness and adjusts the assumptions if deemed appropriate. The carrying amount of the MSRs fair value due to impairment decreased by $24,000 during the first six months of 2018 and decreased by $23,000 during the first six months of 2017.

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The following table presents qualitative information about unobservable inputs used in recurring and non-recurring Level 3 fair value measurements, other than goodwill.

	June 30, 2018			
	Fair Value	**Valuation Technique**	**Unobservable Inputs**	**Range (Weighted Average)**
Impaired loans	$ 8,804	Collateral based measurement	Discount to reflect current market conditions and ultimate collectability	0%-54.8% (2.0%)
Mortgage servicing rights	11,670	Discounted cash flows	Discount rate, Constant prepayment rate, Probability of default	10.3%-11.3% (10.3%), 8.3%-16.5% (8.6%), 0.1%-1.7% (0.6%)

	December 31, 2017			
	Fair Value	**Valuation Technique**	**Unobservable Inputs**	**Range (Weighted Average)**
Impaired loans	$ 6,957	Collateral based measurement	Discount to reflect current market conditions and ultimate collectability	0%-46.8% (2.6%)
Mortgage servicing rights	11,602	Discounted cash flows	Discount rate, Constant prepayment rate, Probability of default	9.6%-10.8% (9.7%), 9.2%-27.7% (10.5%), 0%-1.5% (0.2%)

Note 11 Fair Value of Financial Instruments

The estimated fair value amounts of the Company s financial instruments were determined using available market information, current pricing information applicable to Horizon and various valuation methodologies. Where market quotations were not available, considerable management judgment was involved in the determination of estimated fair values. Therefore, the estimated fair value of financial instruments shown below may not be representative of the amounts at which they could be exchanged in a current or future transaction. Due to the inherent uncertainties of expected cash flows of financial instruments, the use of alternate valuation assumptions and methods could have a significant effect on the estimated fair value amounts.

The estimated fair values of financial instruments, as shown below, are not intended to reflect the estimated liquidation or market value of Horizon taken as a whole. The disclosed fair value estimates are limited to Horizon s significant financial instruments at June 30, 2018 and December 31, 2017. These include financial instruments

recognized as assets and liabilities on the condensed consolidated balance sheet as well as certain off-balance sheet financial instruments. The estimated fair values shown below do not include any valuation of assets and liabilities, which are not financial instruments as defined by the FASB ASC fair value hierarchy.

The following methods and assumptions were used to estimate the fair value of each class of financial instrument:

Cash and Due from Banks The carrying amounts approximate fair value.

Held-to-Maturity Securities For debt securities held to maturity, fair values are based on quoted market prices or dealer quotes. For those securities where a quoted market price is not available, carrying amount is a reasonable estimate of fair value based upon comparison with similar securities.

Loans Held for Sale The carrying amounts approximate fair value.

Net Loans At June 30, 2018, the fair value of net loans are estimated on an exit price basis incorporating discounts for credit, liquidity and marketability factors. This is not comparable with the fair values disclosed at December 31, 2017, which were based on an entrance price basis. At December 31, 2017, the fair value of portfolio loans were estimated by discounting the future cash flows using the current rates at which similar loans would be made to borrowers with similar credit ratings and for the same remaining maturities.

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FHLB and FRB Stock Fair value of FHLB and FRB stock is based on the price at which it may be resold to the FHLB and FRB.

Interest Receivable/Payable The carrying amounts approximate fair value.

Deposits The fair value of demand deposits, savings accounts, interest-bearing checking accounts and money market deposits is the amount payable on demand at the reporting date. The fair value of fixed maturity certificates of deposit is estimated by discounting the future cash flows using rates currently offered for deposits of similar remaining maturity.

Borrowings Rates currently available to Horizon for debt with similar terms and remaining maturities are used to estimate fair values of existing borrowings.

Subordinated Debentures Rates currently available for debentures with similar terms and remaining maturities are used to estimate fair values of existing debentures.

Commitments to Extend Credit and Standby Letters of Credit The fair value of commitments is estimated using the fees currently charged to enter into similar agreements, taking into account the remaining terms of the agreements and the present creditworthiness of the counterparties. For fixed-rate loan commitments, fair value also considers the difference between current levels of interest rates and the committed rates. The fair value of letters of credit is based on fees currently charged for similar agreements or on the estimated cost to terminate them or otherwise settle the obligations with the counterparties at the reporting date. Due to the short-term nature of these agreements, carrying amounts approximate fair value.

The following table presents estimated fair values of the Company s financial instruments and the level within the fair value hierarchy in which the fair value measurements fall (unaudited).

	June 30, 2018			
	Carrying Amount	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
Assets				
Cash and due from banks	$ 69,018	$ 69,018	$	$

Investment securities, held to maturity	209,767		206,730	
Loans held for sale	3,000			3,000
Loans (excluding loan level hedges), net	2,751,703			2,585,501
Stock in FHLB	18,105		18,105	
Interest receivable	12,993		12,993	
Liabilities				
Non-interest bearing deposits	$ 615,018	$ 615,018	$	$
Interest bearing deposits	2,401,145		2,263,817	
Borrowings	524,846		520,701	
Subordinated debentures	37,745		35,682	
Interest payable	1,441		1,441	

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	December 31, 2017			
	Carrying Amount	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
Assets				
Cash and due from banks	$ 76,441	$ 76,441	$	$
Investment securities, held to maturity	200,448		201,085	
Loans held for sale	3,094			3,094
Loans (excluding loan level hedges), net	2,661,026			2,585,879
Stock in FHLB	18,105		18,105	
Interest receivable	16,244		16,244	
Liabilities				
Non-interest bearing deposits	$ 601,805	$ 601,805	$	$
Interest bearing deposits	2,279,198		2,156,487	
Borrowings	564,157		560,057	
Subordinated debentures	37,653		35,994	
Interest payable	886		886	

Note 12 Accumulated Other Comprehensive Income

	June 30 2018	December 31 2017
Unrealized loss on securities available for sale	$ (12,891)	$ (3,937)
Unamortized gain on securities held to maturity, previously transferred from AFS	102	200
Unrealized loss on derivative instruments	(615)	(1,728)
Tax effect	2,817	1,914
Total accumulated other comprehensive loss	$ (10,587)	$ (3,551)

Note 13 Regulatory Capital

Horizon and the Bank are subject to various regulatory capital requirements administered by the federal banking agencies and are assigned to a capital category. Failure to meet the minimum regulatory capital requirements can initiate certain mandatory and possible additional discretionary actions by regulators, which if undertaken, could have a direct material effect on the Bank s financial statements. Under capital adequacy guidelines and the regulatory framework for prompt corrective actions, the Bank must meet specific capital guidelines involving quantitative measures of the Bank s assets, liabilities, and certain off-balance-sheet items as calculated under regulatory accounting practices. The Bank 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 Bank to maintain minimum amounts and ratios of total and Tier I capital (as defined in the regulations) to risk-weighted assets (as defined), and of Tier I capital (as defined) to average assets (as defined), or leverage ratio. For June 30, 2018, Basel III rules require the Bank to maintain minimum amounts and ratios of common equity Tier I capital (as defined in the regulation) to risk-weighted assets (as defined). Additionally, under Basel III rules, the decision was made to opt-out of including accumulated other comprehensive income in regulatory capital.

To be categorized as well capitalized, the Bank must maintain minimum Total risk-based, Tier I risk-based, common equity Tier I risk-based and Tier I leverage ratios as set forth in the table below. As of June 30, 2018 and December 31, 2017, the Bank met all capital adequacy requirements to be considered well capitalized. There have been no conditions or events since the end of the first quarter of 2018 that management believes have changed the Bank s classification as well capitalized. There is no threshold for well-capitalized status for bank holding companies.

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Horizon and the Bank s actual and required capital ratios as of June 30, 2018 and December 31, 2017 were as follows:

	Actual		Required for Capital[1] Adequacy Purposes		Required For Capital[1] Adequacy Purposes with Capital Buffer		Well Capitalized Under Prompt[1] Corrective Action Provisions	
	Amount	Ratio	Amount	Ratio	Amount	Ratio	Amount	Ratio
June 30, 2018								
Total capital[1] (to risk-weighted assets)								
Consolidated	$ 403,480	13.07%	246,952	8.00%	285,539	9.25%	N/A	N/A
Bank	392,814	12.77%	246,109	8.00%	284,563	9.25%	$ 307,636	10.00%
Tier 1 capital[1] (to risk-weighted assets)								
Consolidated	386,409	12.52%	185,214	6.00%	223,800	7.25%	N/A	N/A
Bank	375,684	12.21%	184,581	6.00%	223,035	7.25%	246,108	8.00%
Common equity tier 1 capital[1] (to risk-weighted assets)								
Consolidated	347,946	11.27%	138,910	4.50%	177,497	5.75%	N/A	N/A
Bank	375,684	12.21%	138,436	4.50%	176,890	5.75%	199,963	6.50%
Tier 1 capital[1] (to average assets)								
Consolidated	386,409	9.94%	155,556	4.00%	155,556	4.00%	N/A	N/A
Bank	375,684	9.65%	155,805	4.00%	155,805	4.00%	194,756	5.00%
December 31, 2017								
Total capital[1] (to risk-weighted assets)								
Consolidated	$ 384,800	12.91%	$ 238,543	8.00%	$ 275,816	9.25%	N/A	N/A
Bank	382,788	12.85%	238,386	8.00%	275,634	9.25%	$ 297,982	10.00%
Tier 1 capital[1] (to risk-weighted assets)								
Consolidated	368,355	12.35%	178,907	6.00%	216,180	7.25%	N/A	N/A
Bank	366,343	12.29%	178,790	6.00%	216,038	7.25%	238,386	8.00%
Common equity tier 1 capital[1] (to risk-weighted								

assets)								
Consolidated	329,892	11.06%	134,181	4.50%	171,454	5.75%	N/A	N/A
Bank	366,343	12.29%	134,092	4.50%	171,340	5.75%	193,689	6.50%
Tier 1 capital[1] (to average assets)								
Consolidated	368,355	9.92%	148,503	4.00%	148,503	4.00%	N/A	N/A
Bank	366,343	9.89%	148,116	4.00%	148,116	4.00%	185,145	5.00%

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Note 14 Future Accounting Matters

Financial Accounting Standards Board (FASB) Accounting Standards Update (ASU) No. 2017-12, *Derivatives and Hedging (Topic 815), Targeted Improvements to Accounting for Hedging Activities*

The FASB has issued ASU No. 2017-12, *Derivatives and Hedging (Topic 815), Targeted Improvements to Accounting for Hedging Activities*. The new guidance improves the financial reporting of hedging relationships to better portray the economic results of an entity s risk management activities in its financial statements. The amendments in this ASU also make certain targeted improvements to simplify the application of the hedge accounting guidance in current GAAP. For public entities, the new guidance will be effective for fiscal years beginning after December 15, 2018, and interim periods within those fiscal years. For all other entities, the amendments are effective for fiscal years beginning after December 15, 2019, and interim periods beginning after December 15, 2020. Early application is permitted in any interim period after issuance of the ASU. All transition requirements and elections should be applied to hedging relationships existing (that is, hedging relationships in which the hedging instrument has not expired, been sold, terminated, or exercised or the entity has not removed the designation of the hedging relationship) on the date of adoption. The effect of adoption should be reflected as of the beginning of the fiscal year of adoption (that is, the initial application date). We are currently evaluating the impact of adopting the new guidance on the consolidated financial statements, but it is not expected to have a material impact.

FASB ASU No. 2017-04, *Intangibles Goodwill and Other* (Topic 350): *Simplifying the Test for Goodwill Impairment*

The FASB has issued ASU No. 2017-04, *Intangibles Goodwill and Other (Topic 350): Simplifying the Test for Goodwill Impairment.* The new guidance is intended to simplify the subsequent measurement of goodwill by eliminating Step 2 from the goodwill impairment test. The annual, or interim, goodwill impairment test is performed by comparing the fair value of a reporting unit with its carrying amount. An impairment charge should be recognized for the amount by which the carrying amount exceeds the reporting unit s fair value; however, the loss recognized should not exceed the total amount of goodwill allocated to that reporting unit. In addition, the income tax effects of tax deductible goodwill on the carrying amount of the reporting unit should be considered when measuring the goodwill impairment loss, if applicable. The amendments also eliminate the requirements for any reporting unit with a zero or negative carrying amount to perform Step 2 of the goodwill impairment test. An entity still has the option to perform the qualitative assessment for a reporting unit to determine if the qualitative impairment test is necessary. The amendments should be applied on a prospective basis. The nature of and reason for the change in accounting principle should be disclosed upon transition. The amendments in this update should be adopted for annual or any interim goodwill impairment tests in fiscal years beginning after December 15, 2019. Early adoption is permitted on testing dates after January 1, 2017. We are currently evaluating the impact of adopting the new guidance on the consolidated financial statements, but it is not expected to have a material impact.

FASB ASU No. 2016-13, *Financial Instruments Credit Losses* (Topic 326): *Measurement of Credit Losses on Financial Instruments*

The FASB has issued ASU No. 2016-13, *Financial Instruments Credit Losses (Topic 326): Measurement of Credit Losses on Financial Instruments.* The main objective of this amendment is to provide financial statement users with more decision-useful information about the expected credit losses on financial instruments and other commitments to extend credit held by a reporting entity at each reporting date. The amendment requires the measurement of all expected credit losses for financial assets held at the reporting date based on historical experience, current conditions, and reasonable and supportable forecasts. Financial institutions and other organizations will now use forward-looking information to enhance their credit loss estimates. The amendment requires enhanced disclosures to help investors and other financial statement users better understand significant estimates and judgments used in estimating credit losses, as well as the credit quality and underwriting standards of an organization s portfolio. In addition, the ASU amends the accounting for credit losses on available-for-sale debt securities and purchased financial assets with credit deterioration. The

HORIZON BANCORP, INC. AND SUBSIDIARIES

Notes to Condensed Consolidated Financial Statements

(Unaudited)

(Table Dollar Amounts in Thousands, Except Per Share Data)

amendments in this update become effective for annual periods and interim periods within those annual periods beginning after December 15, 2019. Early adoption will be permitted beginning after December 15, 2018. We have formed a cross functional committee that is assessing our data and system needs and are evaluating the impact of adopting the new guidance. This committee has developed a timeline associated with the Company s adoption of this ASU. We expect to recognize a one-time cumulative effect adjustment to the allowance for loan losses as of the beginning of the first reporting period in which the new standard is effective, but cannot yet determine the magnitude of any such one-time adjustment or the overall impact of the new guidance on the consolidated financial statements.

FASB Accounting Standards Updates No. 2016-02, *Leases* (Topic 842)

The FASB has issued Accounting Standards Update (ASU) No. 2016-02, *Leases.* Under the new guidance, lessees will be required to recognize the following for all leases, with the exception of short-term leases, at the commencement date: (1) a lease liability, which is a lessee s obligation to make lease payments arising from a lease, measured on a discounted basis; and (2) a right-of-use asset, which is an asset that represents the lessee s right to use, or control the use of, a specified asset for the lease term. Under the new guidance, lessor accounting is largely unchanged. The amendments in this update become effective for annual periods and interim periods within those annual periods beginning after December 15, 2018. Based on leases outstanding as of December 31, 2017, we do not expect the new standard to have a material impact on our balance sheet or income statement.

Note 15 General Litigation

The Company is subject to claims and lawsuits that arise primarily in the ordinary course of business. It is the opinion of management that the disposition or ultimate resolution of such claims and lawsuits will not have a material adverse effect on the consolidated financial position, results of operation and cash flows of the Company.

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

Forward Looking Statements

This report contains certain forward-looking statements within the meaning of Section 27A of the Securities Act of 1933, as amended, and Section 21E of the Securities Exchange Act of 1934, as amended, with respect to Horizon Bancorp, Inc. (Horizon or the Company) and Horizon Bank (the Bank). Horizon intends such forward-looking statements to be covered by the safe harbor provisions for forward-looking statements contained in the Private Securities Reform Act of 1995, and is including this statement for the purposes of these safe harbor provisions. Statements in this report should be considered in conjunction with the other information available about Horizon, including the information in the other filings we make with the Securities and Exchange Commission. The forward-looking statements are based on management s expectations and are subject to a number of risks and uncertainties. We have tried, wherever possible, to identify such statements by using words such as anticipate, expect, estimate, project, intend, plan, believe, could, will and similar expressions in connection with any discussi operating or financial performance. Although management believes that the expectations reflected in such forward-looking statements are reasonable, actual results may differ materially from those expressed or implied in such statements.

Actual results may differ materially, adversely or positively, from the expectations of the Company that are expressed or implied by any forward-looking statement. Risks, uncertainties, and factors that could cause the Company s actual results to vary materially from those expressed or implied by any forward-looking statement include but are not limited to:

- economic conditions and their impact on Horizon and its customers;
- changes in the level and volatility of interest rates, spreads on earning assets and interest-bearing liabilities, and interest rate sensitivity;
- rising interest rates and their impact on mortgage loan volumes and the outflow of deposits;
- loss of key Horizon personnel;

increases in disintermediation, as new technologies allow consumers to complete financial transactions without the assistance of banks;

loss of fee income, including interchange fees, as new and emerging alternative payment platforms (e.g. Apple Pay or Bitcoin) take a greater market share of the payment systems;

estimates of fair value of certain of Horizon s assets and liabilities;

volatility and disruption in financial markets;

prepayment speeds, loan originations, credit losses and market values, collateral securing loans and other assets;

sources of liquidity;

potential risk of environmental liability related to lending activities;

changes in the competitive environment in Horizon s market areas and among other financial service providers;

legislation and/or regulation affecting the financial services industry as a whole, and Horizon and its subsidiaries in particular, including the effects resulting from the reforms enacted by the Dodd-Frank Wall Street Reform and Consumer Protection Act (the Dodd-Frank Act) and the adoption of regulations by regulatory bodies under the Dodd-Frank Act;

the possible impact of whole or partial dismantling of provisions of the Dodd-Frank Act under the current federal administration;

the potential for additional changes in tax laws, particularly corporate income tax reform, that may affect current returns, Horizon s deferred tax assets and liabilities, the ability to utilize federal and state net operating loss carryforwards, and the market s perception on overall value;

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- the impact of the Basel III capital rules;
- changes in regulatory supervision and oversight, including monetary policy and capital requirements;
- changes in accounting policies or procedures as may be adopted and required by regulatory agencies;
- rapid technological developments and changes;
- the risks presented by cyber terrorism and data security breaches, and the increasing costs of cybersecurity for the Company;
- containing costs and expenses;
- an economic slowdown and/or possible recession;
- the ability of the U.S. federal government to manage federal debt limits; and
- the risks of expansion through mergers and acquisitions, including unexpected credit quality problems with acquired loans, difficulty integrating acquired operations and material differences in the actual financial results of such transactions compared with Horizon s initial expectations, including the full realization of anticipated cost savings.

The foregoing list of important factors is not exclusive, and you are cautioned not to place undue reliance on these forward-looking statements, which speak only as of the date of this document or, in the case of documents incorporated by reference, the dates of those documents. We do not undertake to update any forward-looking statements, whether written or oral, that may be made from time to time by us or on our behalf. For a detailed discussion of the risks and uncertainties that may cause our actual results or performance to differ materially from the results or performance expressed or implied by forward-looking statements, see Risk Factors in Item 1A of Part I of our 2017 Annual Report on Form 10-K and in the subsequent reports we file with the SEC.

Overview

Horizon is a registered bank holding company incorporated in Indiana and headquartered in Michigan City, Indiana. Horizon provides a broad range of banking services in Northern and Central regions of Indiana and the Southern, Central and Great Lakes Bay regions of Michigan through its bank subsidiary. Horizon operates as a single segment, which is commercial banking. Horizon s common stock is traded on the NASDAQ Global Select Market under the symbol HBNC. The Bank was originally chartered as a national banking association in 1873 and has operated continuously since that time and converted to an Indiana state-chartered bank effective on June 23, 2017. The Bank is a full-service commercial bank offering commercial and retail banking services, corporate and individual trust and agency services, and other services incident to banking. Upon approval of a name change by Horizon s shareholders at the annual meeting on May 3, 2018, Horizon s full corporate name became Horizon Bancorp, Inc.

On October 17, 2017, Horizon completed the acquisition of Wolverine Bancorp, Inc., a Maryland corporation (Wolverine) and Horizon Bank s acquisition of Wolverine Bank, a federally-chartered savings bank and wholly-owned subsidiary of Wolverine, through mergers effective October 17, 2017. Under the terms of the Merger Agreement, shareholders of Wolverine received 1.5228 shares of Horizon common stock and $14.00 in cash for each outstanding share of Wolverine common stock. Wolverine shares outstanding at the closing to be exchanged were 2,129,331 and the shares of Horizon common stock issued to Wolverine shareholders totaled 3,241,045. Based upon the October 16, 2017 closing price of $19.37 per share of Horizon common stock immediately prior to the effectiveness of the merger, less the consideration used to pay off Wolverine Bancorp s ESOP loan receivable, the transaction has an implied valuation of approximately $93.8 million.

On September 1, 2017, Horizon completed the acquisition of Lafayette Community Bancorp, an Indiana corporation (Lafayette) and Horizon Bank s acquisition of Lafayette Community Bank, a state-chartered bank and wholly-owned subsidiary of Lafayette, through mergers effective September 1, 2017. Under the terms of the Merger Agreement, shareholders of Lafayette received 0.8817 shares of Horizon common stock and $1.73 in cash for each outstanding share of Lafayette common stock. Lafayette shareholders owning fewer than 100 shares of common stock received $17.25 in cash for each common share. Lafayette shares outstanding at the closing to be exchanged were 1,856,679, and the shares of Horizon common stock issued to Lafayette shareholders totaled 1,636,888. Based upon the August 31, 2017 closing price of $17.45 per share of Horizon common stock immediately prior to the effectiveness of the merger, the transaction has an implied valuation of approximately $34.5 million.

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On February 3, 2017, Horizon completed the purchase and assumption of certain assets and liabilities of a single branch of First Farmers Bank & Trust Company, located in Bargersville, Indiana. Net cash of $11.0 million was received in the transaction, representing the deposit balances assumed at closing, net of amounts paid for loans acquired in the transaction and a premium on deposits assumed in the transaction.

Following are some highlights of Horizon s financial performance through the first six months of 2018:

Net income for the quarter ended June 30, 2018 was $14.1 million, or $0.37 diluted earnings per share, compared to $9.1 million, or $0.27 diluted earnings per share, for the quarter ended June 30, 2017 resulting in a 37.0% increase in diluted earnings per share. This represents the highest quarterly net income and diluted earnings per share in the Company s 145-year history.

Net income for the first six months of 2018 was $26.9 million, or $0.70 diluted earnings per share, compared to $17.3 million, or $0.51 diluted earnings per share, for the first six months of 2017 resulting in a 37.3% increase in diluted earnings per share. This represents the highest year-to-date net income and diluted earnings per share as of June 30th in the Company s 145-year history.

Return on average assets was 1.41% for the second quarter of 2018 compared to 1.12% for the second quarter of 2017. Return on average assets for the first six months of 2018 was 1.36% compared to 1.10% for the first six months of 2017.

Return on average equity was 12.15% for the second quarter of 2018 compared to 10.24% for the second quarter of 2017. Return on average equity was 11.72% for the first six months of 2018 compared to 9.96% for the first six months of 2017.

Total loans increased by an annualized rate of 6.6%, or $92.4 million, during the first six months of 2018.

Consumer loans increased by an annualized rate of 20.5%, or $46.9 million, during the first six months of 2018.

Residential mortgage loans increased by an annualized rate of 9.3%, or $27.9 million, during the first six months of 2018.

Total deposits increased by an annualized rate of 9.5%, or $135.2 million, during the first six months of 2018.

Net interest income increased $6.4 million, or 23.4%, to $33.6 million for the three months ended June 30, 2018 compared to $27.2 million for the three months ended June 30, 2017. Net interest income increased $14.2 million, or 26.9%, to $67.0 million for the six months ended June 30, 2018 compared to $52.8 million for the six months ended June 30, 2017.

Net interest margin was 3.78% for the three months ended June 30, 2018 compared to 3.84% for the three months ended June 30, 2017. Net interest margin for the six months ended June 30, 2018 and 2017 was 3.81%.

Horizon s tangible book value per share increased to $8.84 at June 30, 2018 compared to $8.48 and $8.13 at December 31, 2017 and June 30, 2017, respectively. This represents the highest tangible book value per share in the Company s 145-year history.

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Critical Accounting Policies

The notes to the consolidated financial statements included in Item 8 of the Company s Annual Report on Form 10-K for 2017 contain a summary of the Company s significant accounting policies. Certain of these policies are important to the portrayal of the Company s financial condition, since they require management to make difficult, complex or subjective judgments, some of which may relate to matters that are inherently uncertain. Management has identified as critical accounting policies the allowance for loan losses, goodwill and intangible assets, mortgage servicing rights, hedge accounting and valuation measurements.

Allowance for Loan Losses

An allowance for loan losses is maintained to absorb probable incurred loan losses inherent in the loan portfolio. The determination of the allowance for loan losses is a critical accounting policy that involves management s ongoing quarterly assessments of the probable incurred losses inherent in the loan portfolio. The identification of loans that have probable incurred losses is subjective; therefore, a general reserve is maintained to cover all probable losses within the entire loan portfolio. Horizon utilizes a loan grading system that helps identify, monitor and address asset quality problems in an adequate and timely manner. Each quarter, various factors affecting the quality of the loan portfolio are reviewed. Large credits are reviewed on an individual basis for loss potential. Other loans are reviewed as a group based upon previous trends of loss experience. Horizon also reviews the current and anticipated economic conditions of its lending market as well as transaction risk to determine the effect they may have on the loss experience of the loan portfolio.

Goodwill and Intangible Assets

Management believes that the accounting for goodwill and other intangible assets also involves a higher degree of judgment than most other significant accounting policies. FASB ASC 350-10 establishes standards for the amortization of acquired intangible assets and impairment assessment of goodwill. At June 30, 2018, Horizon had core deposit intangibles of $11.4 million subject to amortization and $119.9 million of goodwill, which is not subject to amortization. Goodwill arising from business combinations represents the value attributable to unidentifiable intangible assets in the business acquired. Horizon s goodwill relates to the value inherent in the banking industry and that value is dependent upon the ability of Horizon to provide quality, cost effective banking services in a competitive marketplace. The goodwill value is supported by revenue that is in part driven by the volume of business transacted. A decrease in earnings resulting from a decline in the customer base or the inability to deliver cost effective services over sustained periods can lead to impairment of goodwill that could adversely affect earnings in future periods. FASB ASC 350-10 requires an annual evaluation of goodwill for impairment. The evaluation of goodwill for impairment requires the use of estimates and assumptions. Market price at the close of business on June 30, 2018 was $20.69 per share compared to a book value of $12.27 per common share.

Horizon has concluded that, based on its own internal evaluation, the recorded value of goodwill is not impaired.

Mortgage Servicing Rights

Servicing assets are recognized as separate assets when rights are acquired through purchase or through the sale of financial assets on a servicing-retained basis. Capitalized servicing rights are amortized into non-interest income in proportion to, and over the period of, the estimated future net servicing income of the underlying financial assets. Servicing assets are evaluated regularly for impairment based upon the fair value of the rights as compared to amortized cost. Impairment is determined by stratifying servicing rights by predominant characteristics, such as interest rates, original loan terms and whether the loans are fixed or adjustable rate mortgages. Fair value is determined using prices for similar assets with similar characteristics, when available, or based upon discounted cash flows using market-based assumptions. When the book value of an individual stratum exceeds its fair value, an impairment reserve is recognized so that each individual stratum is carried at the lower of its amortized book value or fair value. In periods of falling market interest rates, accelerated loan prepayment can adversely affect the fair value of these mortgage-servicing rights relative to their book value. In the event that the fair value of these assets was to increase in the future, Horizon can recognize the increased fair value to the extent of the impairment allowance but cannot recognize an asset in excess of

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its amortized book value. Future changes in management s assessment of the impairment of these servicing assets, as a result of changes in observable market data relating to market interest rates, loan prepayment speeds, and other factors, could impact Horizon s financial condition and results of operations either positively or negatively.

Generally, when market interest rates decline and other factors favorable to prepayments occur, there is a corresponding increase in prepayments as customers refinance existing mortgages under more favorable interest rate terms. When a mortgage loan is prepaid, the anticipated cash flows associated with servicing that loan are terminated, resulting in a reduction of the fair value of the capitalized mortgage servicing rights. To the extent that actual borrower prepayments do not react as anticipated by the prepayment model (i.e., the historical data observed in the model does not correspond to actual market activity), it is possible that the prepayment model could fail to accurately predict mortgage prepayments and could result in significant earnings volatility. To estimate prepayment speeds, Horizon utilizes a third-party prepayment model, which is based upon statistically derived data linked to certain key principal indicators involving historical borrower prepayment activity associated with mortgage loans in the secondary market, current market interest rates and other factors, including Horizon s own historical prepayment experience. For purposes of model valuation, estimates are made for each product type within the mortgage servicing rights portfolio on a monthly basis. In addition, on a quarterly basis Horizon engages a third party to independently test the value of its servicing asset.

Derivative Instruments

As part of the Company s asset/liability management program, Horizon utilizes, from time-to-time, interest rate floors, caps or swaps to reduce the Company s sensitivity to interest rate fluctuations. These are derivative instruments, which are recorded as assets or liabilities in the consolidated balance sheets at fair value. Changes in the fair values of derivatives are reported in the consolidated income statements or other comprehensive income (OCI) depending on the use of the derivative and whether the instrument qualifies for hedge accounting. The key criterion for the hedge accounting is that the hedged relationship must be highly effective in achieving offsetting changes in those cash flows that are attributable to the hedged risk, both at inception of the hedge and on an ongoing basis.

Horizon s accounting policies related to derivatives reflect the guidance in FASB ASC 815-10. Derivatives that qualify for the hedge accounting treatment are designated as either: a hedge of the fair value of the recognized asset or liability or of an unrecognized firm commitment (a fair value hedge) or a hedge of a forecasted transaction or the variability of cash flows to be received or paid related to a recognized asset or liability (a cash flow hedge). For fair value hedges, the cumulative change in fair value of both the hedge instruments and the underlying loans is recorded in non-interest income. For cash flow hedges, changes in the fair values of the derivative instruments are reported in OCI to the extent the hedge is effective. The gains and losses on derivative instruments that are reported in OCI are reflected in the consolidated income statement in the periods in which the results of operations are impacted by the variability of the cash flows of the hedged item. Generally, net interest income is increased or decreased by amounts receivable or payable with respect to the derivatives, which qualify for hedge accounting. At inception of the hedge,

Horizon establishes the method it uses for assessing the effectiveness of the hedging derivative and the measurement approach for determining the ineffective aspect of the hedge. The ineffective portion of the hedge, if any, is recognized currently in the consolidated statements of income. Horizon excludes the time value expiration of the hedge when measuring ineffectiveness.

Valuation Measurements

Valuation methodologies often involve a significant degree of judgment, particularly when there are no observable active markets for the items being valued. Investment securities, residential mortgage loans held for sale and derivatives are carried at fair value, as defined in FASB ASC 820, which requires key judgments affecting how fair value for such assets and liabilities is determined. In addition, the outcomes of valuations have a direct bearing on the carrying amounts of goodwill, mortgage servicing rights, and pension and other post-retirement benefit obligations. To determine the values of these assets and liabilities, as well as the extent, to which related assets may be impaired, management makes assumptions and estimates related to discount rates, asset returns, prepayment speeds and other factors. The use of different discount rates or other valuation assumptions could produce significantly different results, which could affect Horizon s results of operations.

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Financial Condition

On June 30, 2018, Horizon s total assets were $4.077 billion, an increase of approximately $112.3 million compared to December 31, 2017. The increase was primarily in net loans of $91.8 million, other assets of $6.2 million and investment securities available for sale and held to maturity of $16.5 million and $9.3 million, respectively, which were offset by decreases in cash and due from banks of $7.4 million and interest receivable of $3.3 million.

Investment securities were comprised of the following as of (dollars in thousands):

	June 30, 2018		December 31, 2017	
	Amortized Cost	Fair Value	Amortized Cost	Fair Value
Available for sale				
U.S. Treasury and federal agencies	$ 24,654	$ 24,219	$ 19,277	$ 19,052
State and municipal	136,732	134,981	148,045	149,564
Federal agency collateralized mortgage obligations	168,382	164,134	132,871	130,365
Federal agency mortgage-backed pools	203,593	196,995	211,487	208,657
Private labeled mortgage-backed pools			1,650	1,642
Corporate notes	5,725	5,866	272	385
Total available for sale investment securities	$ 539,086	$ 526,195	$ 513,602	$ 509,665
Held to maturity				
State and municipal	$ 190,079	$ 187,380	$ 179,836	$ 180,397
Federal agency collateralized mortgage obligations	5,409	5,260	5,734	5,682
Federal agency mortgage-backed pools	14,279	14,090	14,878	15,006
Total held to maturity investment securities	$ 209,767	$ 206,730	$ 200,448	$ 201,085

Total loans increased $92.4 million since December 31, 2017 to $2.928 billion as of June 30, 2018. This increase was the result of an increase in consumer loans of $46.9 million, residential mortgage loans of $27.9 million, mortgage warehouse loans of $14.5 million and commercial loans of $3.3 million, offset by a decrease in loans held for sale of $94,000. The growth markets of Fort Wayne, Grand Rapids, Indianapolis and Kalamazoo contributed total loan growth of $34.3 million during the first six months of 2018. Our experienced consumer loan team and increased focus on the consumer portfolio have been the main drivers for the increase in consumer loans.

Total deposits increased $135.2 million since December 31, 2017 to $3.016 billion as of June 30, 2018. Non-interest bearing transaction accounts and time deposits increased $13.2 million and $189.4 million, respectively, during the six months ended June 30, 2018 which was offset by a decrease in interest-bearing deposits of $67.5 million.

The Company decreased total borrowings from $564.2 million as of December 31, 2017 to $524.8 million as of June 30, 2018. At June 30, 2018, the Company had $366.4 million in short-term funds borrowed compared to $392.3 million at December 31, 2017. The decrease in borrowings was primarily due to the increase in deposits of $135.2 million from December 31, 2017.

Stockholders equity totaled $470.5 million at June 30, 2018 compared to $457.1 million at December 31, 2017. The increase in stockholders equity during the period was due to the generation of net income, net of dividends declared and a decrease in accumulated other comprehensive income. At June 30, 2018, the ratio of average stockholders equity to average assets was 11.60% compared to 11.70% at December 31, 2017. Book value per common share at June 30, 2018 increased to $12.27 compared to $11.93 at December 31, 2017.

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Results of Operations

Overview

Consolidated net income for the three-month period ended June 30, 2018 was $14.1 million compared to $9.1 million for the same period in 2017. Earnings per common share for the three months ended June 30, 2018 were $0.37 basic and diluted, compared to $0.27 basic and diluted for the same three-month period in the previous year. The increase in net income and earnings per share from the previous year reflects increases in net interest income of $6.4 million and non-interest income of $720,000, partially offset by increases in provision for loan losses of $305,000 and non-interest expense of $2.5 million. Non-interest expense increased primarily due to an increase in salaries, employee benefits, net occupancy expenses, data processing, loan expense, other losses and other expense. Excluding loss on sale of investment securities, death benefit on bank owned life insurance and purchase accounting adjustments, net income for the second quarter of 2018 was $12.7 million or $0.33 diluted earnings per share compared to $8.6 million or $0.26 diluted earnings per share in the same period of 2017.

Consolidated net income for the six-month period ended June 30, 2018 was $26.9 million compared to $17.3 million for the same period of 2017. Earnings per common share for the six months ended June 30, 2018 were $0.70 basic and diluted, compared to $0.52 basic and $0.51 diluted for the same six-month period in the previous year. The increase in net income and earnings per share from the previous year reflects increases in net interest income of $14.2 million and non-interest income of $1.5 million, partially offset by increases in provision for loan losses of $542,000 and non-interest expense of $6.8 million. Non-interest expense increased primarily due to an increase in salaries, employee benefits, net occupancy expenses, data processing, loan expense, other losses and other expense. Excluding acquisition-related expenses, gains on sale of investment securities, death benefit on bank owned life insurance and purchase accounting adjustments, net income for the six months ended June 30, 2018 was $23.9 million or $0.62 diluted earnings per share compared to $16.1 million or $0.47 diluted earnings per share in the same period of 2017.

Net Interest Income

The largest component of net income is net interest income. Net interest income is the difference between interest income, principally from loans and investment securities, and interest expense, principally on deposits and borrowings. Changes in the net interest income are the result of changes in volume and the net interest spread, which affects the net interest margin. Volume refers to the average dollar levels of interest-earning assets and interest-bearing liabilities. Net interest spread refers to the difference between the average yield on interest-earning assets and the average cost of interest-bearing liabilities. Net interest margin refers to net interest income divided by average interest-earning assets and is influenced by the level and relative mix of interest-earning assets and interest-bearing liabilities.

Net interest income during the three months ended June 30, 2018 was $33.6 million, an increase of $6.4 million from the $27.2 million earned during the same period in 2017. Yields on the Company s interest-earning assets increased by 24 basis points to 4.57% for the three months ending June 30, 2018 from 4.33% for the three months ended June 30, 2017. Interest income increased $9.9 million from $30.8 million for the three months ended June 30, 2017 to $40.7 million for the same period in 2018. This was due to an increase in average interest-earning assets through organic and acquisition-related growth. Interest income from acquisition-related purchase accounting adjustments was $1.6 million for the three months ending June 30, 2018 compared to $939,000 for the same period of 2017.

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The following are the average balance sheets for the three months ending (dollars in thousands):

	Three Months Ended June 30, 2018			Three Months Ended June 30, 2017		
	Average Balance	Interest	Average Rate	Average Balance	Interest	Average Rate
Assets						
Interest-earning assets						
Federal funds sold	$ 3,367	$ 15	1.79%	$ 1,728	$ 6	1.39%
Interest-earning deposits	25,946	107	1.65%	27,677	83	1.20%
Investment securities - taxable	416,182	2,441	2.35%	423,815	2,155	2.04%
Investment securities - non-taxable[1]	307,219	1,870	3.15%	290,494	1,766	3.40%
Loans receivable[2][3]	2,886,087	36,308	5.08%	2,199,913	26,795	4.94%
Total interest-earning assets[1]	3,638,801	40,741	4.57%	2,943,627	30,805	4.33%
Non-interest-earning assets						
Cash and due from banks	44,213			42,331		
Allowance for loan losses	(16,617)			(15,131)		
Other assets	351,154			279,024		
Total average assets	$ 4,017,551			$ 3,249,851		
Liabilities and Stockholders Equity						
Interest-bearing liabilities						
Interest-bearing deposits	$ 2,403,780	$ 3,920	0.65%	$ 1,980,025	$ 1,721	0.35%
Borrowings	489,608	2,679	2.19%	359,462	1,338	1.49%
Subordinated debentures	36,525	592	6.50%	36,340	548	6.05%
Total interest-bearing liabilities	2,929,913	7,191	0.98%	2,375,827	3,607	0.61%
Non-interest-bearing liabilities						
Demand deposits	605,188			499,446		
Accrued interest payable and other liabilities	16,482			19,143		
Stockholders equity	465,968			355,435		
	$ 4,017,551			$ 3,249,851		

Total average liabilities and stockholders equity				
Net interest income/spread	$ 33,550	3.59%	$ 27,198	3.73%
Net interest income as a percent of average interest-earning assets[1]		3.78%		3.84%

(1) Securities balances represent daily average balances for the fair value of securities. The average rate is calculated based on the daily average balance for the amortized cost of securities. The average rate is presented on a tax equivalent basis.

(2) Includes fees on loans. The inclusion of loan fees does not have a material effect on the average interest rate.

(3) Non-accruing loans for the purpose of the computations above are included in the daily average loan amounts outstanding. Loan totals are shown net of unearned income and deferred loan fees. The average rate is presented on a tax equivalent basis.

Rates paid on interest-bearing liabilities increased by 37 basis points for the three-month period ended June 30, 2018 compared to the same period in 2017 due to increases in the cost of interest-bearing deposits and borrowings. Interest expense increased $3.6 million compared to the three-month period ended June 30, 2017 to $7.2 million for the same period in 2018. This increase was due to higher average balances of interest-bearing deposits and borrowings in addition to the higher rates paid on both. Average balances of interest-bearing deposits increased $423.8 million and were due to the acquisitions of Lafayette and Wolverine during the third and fourth quarters of 2017, as well as organic growth during the first six months of 2018.

The net interest margin decreased 6 basis points from 3.84% for the three-month period ended June 30, 2017 to 3.78% for the same period in 2018. The decrease in the margin for the three-month period ended June 30, 2018 compared to the same period in 2017 was due to an increase in the cost of interest-bearing liabilities and the impact of the lower income tax rate on non-taxable interest-earning assets, offset by an increase in the yield of taxable interest-earning assets.

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Excluding the interest income recognized from the acquisition-related purchase accounting adjustments, the margin would have been 3.60% for the three-month period ending June 30, 2018 compared to 3.71% for the same period in 2017.

Net interest income during the six months ended June 30, 2018 was $67.0 million, an increase of $14.2 million from the $52.8 million earned during the same period in 2017. Yields on the Company s interest-earning assets increased by 26 basis points to 4.55% for the six months ending June 30, 2018 from 4.29% for the six months ended June 30, 2017. Interest income increased $20.5 million from $59.6 million for the six months ended June 30, 2017 to $80.2 million for the same period in 2018. This was due to an increase in average interest-earning assets through organic and acquisition-related growth. Interest income from acquisition-related purchase accounting adjustments was $3.7 million for the six months ending June 30, 2018 compared to $2.0 million for the same period of 2017.

The following are the average balance sheets for the six months ending (dollars in thousands):

	Six Months Ended June 30, 2018			Six Months Ended June 30, 2017		
	Average Balance	Interest	Average Rate	Average Balance	Interest	Average Rate
Assets						
Interest-earning assets						
Federal funds sold	$ 3,560	$ 29	1.64%	$ 2,377	$ 11	0.93%
Interest-earning deposits	24,749	197	1.61%	26,220	152	1.17%
Investment securities - taxable	409,669	4,767	2.35%	411,417	4,487	2.20%
Investment securities - non-taxable[1]	307,462	3,735	3.13%	280,563	3,403	3.40%
Loans receivable[2][3]	2,855,236	71,439	5.05%	2,150,307	51,586	4.85%
Total interest-earning assets[1]	3,600,676	80,167	4.55%	2,870,884	59,639	4.29%
Non-interest-earning assets						
Cash and due from banks	43,984			41,788		
Allowance for loan losses	(16,480)			(15,035)		
Other assets	352,684			279,497		
Total average assets	$ 3,980,864			$ 3,177,134		
Liabilities and Stockholders Equity						
Interest-bearing liabilities						

Interest-bearing deposits	$ 2,354,578	$ 6,791	0.58%	$ 1,970,235	$ 3,474	0.36%
Borrowings	508,731	5,251	2.08%	305,116	2,275	1.50%
Subordinated debentures	37,695	1,164	6.23%	36,315	1,124	6.24%
Total interest-bearing liabilities	2,901,004	13,206	0.92%	2,311,666	6,873	0.60%
Non-interest-bearing liabilities						
Demand deposits	600,214			495,262		
Accrued interest payable and other liabilities	16,490			19,901		
Stockholders equity	463,156			350,305		
Total average liabilities and stockholders equity	$ 3,980,864			$ 3,177,134		
Net interest income/spread		$ 66,961	3.64%		$ 52,766	3.69%
Net interest income as a percent of average interest-earning assets[1]			3.81%			3.81%

(1) Securities balances represent daily average balances for the fair value of securities. The average rate is calculated based on the daily average balance for the amortized cost of securities. The average rate is presented on a tax equivalent basis.

(2) Includes fees on loans. The inclusion of loan fees does not have a material effect on the average interest rate.

(3) Non-accruing loans for the purpose of the computations above are included in the daily average loan amounts outstanding. Loan totals are shown net of unearned income and deferred loan fees. The average rate is presented on a tax equivalent basis.

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Rates paid on interest-bearing liabilities increased by 32 basis points for the six-month period ended June 30, 2018 compared to the same period in 2017 due to increases in the cost of interest-bearing deposits and borrowings. Interest expense increased $6.3 million compared to the six-month period ended June 30, 2017 to $13.2 million for the same period in 2018. This increase was due to higher average balances of interest-bearing deposits and borrowings in addition to the higher rates paid on both. Average balances of interest-bearing deposits increased $384.3 million and were due to the acquisitions of Lafayette and Wolverine during the third and fourth quarters of 2017, as well as organic growth during the first six months of 2018.

The net interest margin remained at 3.81% for the six-month periods ended June 30, 2018 and 2017, respectively. The increase in the cost of interest-bearing liabilities and the impact of the lower income tax rate on non-taxable interest-earning assets was offset by an increase in the yield of taxable interest-earning assets when comparing the six-month periods ended June 30, 2017 and 2018. Excluding the interest income recognized from the acquisition-related purchase accounting adjustments, the margin would have been 3.61% for the six-month period ending June 30, 2018 compared to 3.67% for the same period in 2017.

Provision for Loan Losses

Horizon assesses the adequacy of its Allowance for Loan and Lease Losses (ALLL) by regularly reviewing the performance of its loan portfolio. During the three-month period ended June 30, 2018, a provision of $635,000 was required to adequately fund the ALLL compared to $330,000 for the same period of 2017. Commercial loan net charge-offs during the three-month period ended June 30, 2018 were negative $40,000, residential mortgage loan net charge-offs were negative $2,000 and consumer loan net charge-offs were $80,000. The increase in the provision for loan losses in the second quarter of 2018 compared to the same period of 2017 was due to additional general and non-specific allocations for loan growth in new markets, higher than anticipated growth of the indirect loan portfolio and an increase in allocation for other economic factors, including the potential of a recession. The ALLL balance at June 30, 2018 was $17.1 million or 0.58% of total loans. This compares to an ALLL balance of $16.4 million at December 31, 2017 or 0.58% of total loans.

For the six-month period ended June 30, 2018, the provision for loan losses totaled $1.2 million compared to $660,000 in the same period of 2017. The increase in the provision for loan losses was due to additional general and non-specific allocations for loan growth in new markets, higher than anticipated growth of the indirect loan portfolio and an increase in allocation for other economic factors, including the potential of a recession.

Horizon s loan loss reserve ratio, excluding loans with credit-related purchase accounting adjustments, stood at 0.75% as of June 30, 2018. Loan loss reserves and credit-related loan discounts on acquired loans as a percentage of total loans was 1.08% as of June 30, 2018. The table below illustrates Horizon s loan loss reserve ratio composition as of June 30, 2018.

Non-GAAP Allowance for Loan and Lease Loss Detail

As of June 30, 2018

(Dollars in Thousands, Unaudited)

	Pre-discount Loan Balance	Allowance for Loan Losses (ALLL)	Loan Discount	ALLL + Loan Discount	Loans, net	ALLL/ Pre-discount Loan Balance	Loan Discount/ Pre-discount Loan Balance	ALLL+Loan Discount/ Pre-discount Loan Balance
Horizon Legacy	$ 2,280,089	$ 17,071	N/A	$ 17,071	$ 2,263,018	0.75%	0.00%	0.75%
Heartland	10,290		725	725	9,565	0.00%	7.05%	7.05%
Summit	31,357		1,858	1,858	29,499	0.00%	5.93%	5.93%
Peoples	99,586		2,259	2,259	97,327	0.00%	2.27%	2.27%
Kosciusko	46,070		700	700	45,370	0.00%	1.52%	1.52%
LaPorte	108,429		3,283	3,283	105,146	0.00%	3.03%	3.03%
CNB	5,293		144	144	5,149	0.00%	2.72%	2.72%
Lafayette	112,352		2,036	2,036	110,316	0.00%	1.81%	1.81%
Wolverine	234,050		3,447	3,447	230,603	0.00%	1.47%	1.47%
Total	$ 2,927,516	$ 17,071	$ 14,452	$ 31,523	$ 2,895,993	0.58%	0.49%	1.08%

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No assurance can be given that Horizon will not, in any particular period, sustain loan losses that are significant in relation to the amount reserved, or that subsequent evaluations of the loan portfolio, in light of factors then prevailing, including economic conditions and management s ongoing quarterly assessments of the portfolio, will not require increases in the allowance for loan losses. Horizon considers the allowance for loan losses to be appropriate to cover probable incurred losses in the loan portfolio as of June 30, 2018.

Non-performing loans totaled $15.4 million as of June 30, 2018, down from $16.4 million as of December 31, 2017. Non-performing real estate and consumer loans decreased by $1.8 million and $837,000, respectively, at June 30, 2018 compared to December 31, 2017. Non-performing commercial loans increased $1.6 million at June 30, 2018 compared to December 31, 2017.

Other Real Estate Owned (OREO) and repossessed assets totaled $3.0 million at June 30, 2018 compared to $838,000 on December 31, 2017 and $2.2 million on June 30, 2017. The majority of this increase was due to several bank owned properties acquired through acquisitions and listed for sale being re-classified to other real estate owned and recorded at fair value during the second quarter of 2018.

Non-interest Income

The following is a summary of changes in non-interest income (table dollar amounts in thousands):

	Three Months Ended			
Non-interest Income	**June 30 2018**	**June 30 2017**	**Amount Change**	**Percent Change**
Service charges on deposit accounts	**$ 1,907**	$ 1,566	$ 341	21.8%
Wire transfer fees	**180**	178	2	1.1%
Interchange fees	**1,555**	1,382	173	12.5%
Fiduciary activities	**1,818**	1,943	(125)	-6.4%
Gain on sale of investment securities		(3)	3	-100.0%
Gain on sale of mortgage loans	**1,896**	2,054	(158)	-7.7%
Mortgage servicing net of impairment	**511**	359	152	42.3%
Increase in cash surrender value of bank owned life insurance	**442**	408	34	8.3%
Death benefit on bank owned life insurance	**154**		154	0.0%
Other income	**469**	325	144	44.3%
Total non-interest income	**$ 8,932**	$ 8,212	$ 720	8.8%

Total non-interest income was $720,000 higher during the second quarter of 2018 compared to the same period of 2017. Service charges on deposit accounts increased $341,000 and interchange fees increased by $173,000 primarily due to overall company growth and increased volume. Residential mortgage loan activity during the second quarter of 2018 generated $1.9 million of income from the gain on sale of mortgage loans, down $158,000 from the same period in 2017. The decrease in the gain on sale of mortgage loans was due to a decrease in the volume of mortgage loans sold from $57.5 million in the second quarter of 2017 to $51.0 million in the same period of 2018. Total mortgage loan originations, including mortgage loans sold, decreased to $109.0 million for the second quarter of 2018 compared to $110.4 million for the second quarter of 2017.

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The following is a summary of changes in non-interest income (table dollar amounts in thousands):

	Six Months Ended			
Non-interest Income	**June 30 2018**	**June 30 2017**	**Amount Change**	**Percent Change**
Service charges on deposit accounts	**$ 3,795**	$ 2,966	$ 829	28.0%
Wire transfer fees	**330**	328	2	0.6%
Interchange fees	**2,883**	2,558	325	12.7%
Fiduciary activities	**3,743**	3,865	(122)	-3.2%
Gain on sale of investment securities	**11**	32	(21)	-65.6%
Gain on sale of mortgage loans	**3,319**	3,968	(649)	-16.4%
Mortgage servicing net of impairment	**860**	806	54	6.7%
Increase in cash surrender value of bank owned life insurance	**877**	872	5	0.6%
Death benefit on bank owned life insurance	**154**		154	0.0%
Other income	**1,278**	376	902	239.9%
Total non-interest income	**$ 17,250**	$ 15,771	$ 1,479	9.4%

Total non-interest income was $1.5 million higher during the first six months of 2018 compared to the same period of 2017. Service charges on deposit accounts increased $829,000 and interchange fees increased by $325,000 primarily due to overall company growth and increased volume. Residential mortgage loan activity during the first six months of 2018 generated $3.3 million of income from the gain on sale of mortgage loans, down $649,000 from the same period in 2017. The decrease in the gain on sale of mortgage loans was due to a decrease in the volume of mortgage loans sold from $107.5 million during the first six months of 2017 to $86.8 million during the same period of 2018. Total mortgage loan originations, including mortgage loans sold, increased to $181.3 million for the first six months of 2018 compared to $176.3 million for the same period of 2017.

Non-interest Expense

The following is a summary of changes in non-interest expense (table dollar amounts in thousands):

Three Months Ended

Non-interest Expense	June 30 2018	June 30 2017	Amount Change	Percent Change
Salaries	**$ 10,043**	$ 9,116	$ 927	10.2%
Commission and bonuses	**1,509**	1,389	120	8.6%
Employee benefits	**2,257**	1,961	296	15.1%
Net occupancy expenses	**2,520**	2,196	324	14.8%
Data processing	**1,607**	1,502	105	7.0%
Professional fees	**376**	535	(159)	-29.7%
Outside services and consultants	**1,267**	1,265	2	0.2%
Loan expense	**1,525**	1,250	275	22.0%
FDIC deposit insurance	**345**	243	102	42.0%
Other losses	**269**	78	191	244.9%
Other expenses	**3,224**	2,953	271	9.2%
Total non-interest expense	**$ 24,942**	$ 22,488	$ 2,454	10.9%

Total non-interest expense was $2.5 million higher in the second quarter of 2018 compared to the same period of 2017. The increase was primarily due to an increase in salaries and employee benefits of $1.3 million, net occupancy expenses of $324,000, loan expense of $275,000, other expenses of $271,000, other losses of $191,000, data processing of $105,000 and FDIC deposit insurance of $102,000. The increase in salaries and employee benefits, net occupancy expense, other expense, data processing and FDIC deposit insurance reflect overall company growth and the acquisitions of Lafayette Community Bancorp and Wolverine Bancorp, Inc. during the third and fourth quarters of

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2017. Loan expense increased due to a higher level of loan originations and loan collection expenses when compared to the second quarter of 2017. Other losses increased primarily due to write-downs on other bank owned properties and an accrual for a potential loss on a fiduciary account recorded during the second quarter of 2018.

The following is a summary of changes in non-interest expense (table dollar amounts in thousands):

	Six Months Ended			
Non-interest Expense	**June 30 2018**	**June 30 2017**	**Amount Change**	**Percent Change**
Salaries	**$ 20,117**	$ 17,622	$ 2,495	14.2%
Commission and bonuses	**2,856**	2,450	406	16.6%
Employee benefits	**5,209**	4,103	1,106	27.0%
Net occupancy expenses	**5,486**	4,648	838	18.0%
Data processing	**3,303**	2,809	494	17.6%
Professional fees	**877**	1,148	(271)	-23.6%
Outside services and consultants	**2,531**	2,487	44	1.8%
Loan expense	**2,782**	2,357	425	18.0%
FDIC deposit insurance	**655**	506	149	29.4%
Other losses	**415**	128	287	224.2%
Other expenses	**6,548**	5,751	797	13.9%
Total non-interest expense	**$ 50,779**	$ 44,009	$ 6,770	15.4%

Total non-interest expense was $6.8 million higher for the six months ended June 30, 2018 when compared to the six months ended June 30, 2017. The increase was primarily due to increases in salaries and employee benefits of $4.0 million, net occupancy expenses of $838,000, other expense of $797,000, data processing of $494,000 and loan expense of $425,000. The increase in salaries and employee benefits, net occupancy expense, other expense and data processing expense reflect overall company growth and recent acquisitions. Loan expense increased due to a higher level of loan originations and collection expenses during the six months ended June 30, 2018 when compared to the same period of 2017. Offsetting these increases was a decrease of $271,000 in professional fees primarily due to a lack of acquisition-related expenses in 2018.

Income Taxes

Income tax expense totaled $2.8 million for the second quarter of 2018, a decrease of $730,000 when compared to the second quarter of 2017. The decrease was primarily due to the impact of the new corporate tax rate which was signed

into law at the end of 2017 reducing the effective federal tax rate from 35% to 21% and the benefits from the exercising of stock options. This decrease was offset by an increase in income before income taxes of $4.3 million when comparing the second quarter of 2018 to the same period of 2017.

Income tax expense totaled $5.3 million for the six months ended June 30, 2018, a decrease of $1.3 million when compared to the six months ended June 30, 2017. The decrease was primarily due to the impact of the new corporate tax rate which was signed into law at the end of 2017 reducing the effective federal tax rate from 35% to 21% and the benefits from the exercising of stock options. This decrease was offset by an increase in income before income taxes of $8.4 million when comparing the first six months of 2018 to the same period of 2017.

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Liquidity

The Bank maintains a stable base of core deposits provided by long-standing relationships with individuals and local businesses. These deposits are the principal source of liquidity for Horizon. Other sources of liquidity for Horizon include earnings, loan repayment, investment security sales and maturities, proceeds from the sale of residential mortgage loans, unpledged investment securities and borrowing relationships with correspondent banks, including the FHLB. During the six months ended June 30, 2018, cash and cash equivalents decreased by approximately $7.4 million. At June 30, 2018, in addition to liquidity available from the normal operating, funding, and investing activities of Horizon, the Bank had approximately $207.3 million in unused credit lines with various money center banks, including the FHLB and the FRB Discount Window compared to $127.2 million at December 31, 2017 and $181.2 million at June 30, 2017. The Bank had approximately $561.3 million of unpledged investment securities at June 30, 2018 compared to $518.2 million at December 31, 2017 and $545.0 million at June 30, 2017.

Capital Resources

The capital resources of Horizon and the Bank exceeded regulatory capital ratios for well capitalized banks at June 30, 2018. Stockholders equity totaled $470.5 million as of June 30, 2018, compared to $457.1 million as of December 31, 2017. For the six months ended June 30, 2018, the ratio of average stockholders equity to average assets was 11.63% compared to 11.15% for the twelve months ended December 31, 2017. The increase in stockholders equity during the period was the result of the generation of net income, net of dividends declared.

Horizon declared common stock dividends in the amount of $0.20 per share during the first six months of 2018 and $0.16 per share for the same period of 2017. The dividend payout ratio (dividends as a percent of basic earnings per share) was 28.5% and 30.8% for the first six months of 2018 and 2017, respectively. For additional information regarding dividends, see Horizon s Annual Report on Form 10-K for 2017.

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Use of Non-GAAP Financial Measures

Certain information set forth in this quarterly report on Form 10-Q refers to financial measures determined by methods other than in accordance with GAAP. Specifically, we have included non-GAAP financial measures relating to net income, diluted earnings per share, net interest margin, the allowance for loan and lease losses, tangible stockholders equity, tangible book value per share, the return on average assets and the return on average common equity. In each case, we have identified special circumstances that we consider to be non-recurring and have excluded them, to show the impact of such events as acquisition-related purchase accounting adjustments and the tax reform bill, among others we have identified in our reconciliations. Horizon believes that these non-GAAP financial measures are helpful to investors and provide a greater understanding of our business without giving effect to the purchase accounting impacts and one-time costs of acquisitions and non-core items. These measures are not necessarily comparable to similar measures that may be presented by other companies and should not be considered in isolation or as a substitute for the related GAAP measure. See the tables and other information below and contained elsewhere in this Report on Form 10-Q for reconciliations of the non-GAAP figures identified herein and their most comparable GAAP measures.

Non-GAAP Reconciliation of Net Interest Margin

(Dollars in Thousands, Unaudited)

	Three Months Ended			Six Months Ended	
	June 30 2018	**March 31 2018**	**June 30 2017**	**June 30 2018**	**June 30 2017**
Non-GAAP Reconciliation of Net Interest Margin					
Net interest income as reported	$ 33,550	$ 33,411	$ 27,198	$ 66,961	$ 52,766
Average interest-earning assets	3,638,801	3,580,143	2,943,627	3,600,676	2,870,884
Net interest income as a percentage of average interest-earning assets (Net Interest Margin)	3.78%	3.81%	3.84%	3.81%	3.81%
Acquisition-related purchase accounting adjustments (PAUs)	$ (1,634)	$ (2,037)	$ (939)	(3,671)	(1,955)
Core net interest income	$ 31,916	$ 31,374	$ 26,259	63,290	50,811

Core net interest margin	3.60%	3.55%	3.71%	3.61%	3.67%

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Non-GAAP Reconciliation of Net Income and Diluted Earnings per Share

(Dollars in Thousands, Except per Share Data, Unaudited)

	Three Months Ended			Six Months Ended	
	June 30 2018	March 31 2018	June 30 2017	June 30 2018	June 30 2017
Non-GAAP Reconciliation of Net Income					
Net income as reported	$ 14,115	$ 12,804	$ 9,072	$ 26,919	$ 17,296
Merger expenses			200		200
Tax effect			(70)		(70)
Net income excluding merger expenses	14,115	12,804	9,202	26,919	17,426
Gain on sale of investment securities		(11)	3	(11)	(32)
Tax effect		2	(1)	2	11
Net income excluding gain on sale of investment securities	14,115	12,795	9,204	26,910	17,405
Death benefit on bank owned life insurance (BOLI)	(154)			(154)	
Tax effect	32			32	
Net income excluding death benefit on BOLI	13,993	12,795	9,204	26,788	17,405
Acquisition-related purchase accounting adjustments (PAUs)	(1,634)	(2,037)	(939)	(3,671)	(1,955)
Tax effect	343	428	329	771	684
Core Net Income	$ 12,702	$ 11,186	$ 8,594	$ 23,888	$ 16,134
Non-GAAP Reconciliation of Diluted Earnings per Share					
Diluted earnings per share (EPS) as reported	$ 0.37	$ 0.33	$ 0.27	$ 0.70	$ 0.51
Merger expenses			0.01		0.01
Tax effect					
Diluted EPS excluding merger expenses	0.37	0.33	0.28	0.70	0.52
Gain on sale of investment securities					

Tax effect										
Diluted EPS excluding gain on sale of investment securities		0.37		0.33		0.28		0.70		0.52
Death benefit on BOLI										
Tax effect										
Diluted EPS excluding death benefit on BOLI		0.37		0.33		0.28		0.70		0.52
Acquisition-related PAUs		(0.04)		(0.05)		(0.03)		(0.10)		(0.06)
Tax effect				0.01		0.01		0.02		0.01
Core Diluted EPS	$	0.33	$	0.29	$	0.26	$	0.62	$	0.47

Non-GAAP Reconciliation of Tangible Stockholders Equity and Tangible Book Value per Share

(Dollars in Thousands Except per Share Data, Unaudited)

		June 30 2018		March 31 2018		December 31 2017		September 30 2017		June 30 2017
Total stockholders equity	$	470,535	$	460,416	$	457,078	$	392,055	$	357,259
Less: Intangible assets		131,239		131,724		132,282		103,244		86,726
Total tangible stockholders equity	$	339,296	$	328,692	$	324,796	$	288,811	$	270,533
Common shares outstanding		38,362,640		38,332,853		38,294,729		34,988,189		33,264,698
Tangible book value per common share	$	8.84	$	8.57	$	8.48	$	8.25	$	8.13

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Non-GAAP Reconciliation of Return on Average Assets and Return on Average Common Equity

(Dollars in Thousands, Unaudited)

	Three Months Ended			Six Months Ended	
	June 30 2018	March 31 2018	June 30 2017	June 30 2018	June 30 2017
Non-GAAP Reconciliation of Return on Average Assets					
Average assets	$ 4,017,551	$ 3,942,837	$ 3,249,851	$ 3,980,864	$ 3,177,134
Return on average assets (ROAA) as reported	1.41%	1.32%	1.12%	1.36%	1.10%
Merger expenses	0.00%	0.00%	0.02%	0.00%	0.01%
Tax effect	0.00%	0.00%	-0.01%	0.00%	0.00%
ROAA excluding merger expenses	1.41%	1.32%	1.13%	1.36%	1.11%
Gain on sale of investment securities	0.00%	0.00%	0.00%	0.00%	0.00%
Tax effect	0.00%	0.00%	0.00%	0.00%	0.00%
ROAA excluding gain on sale of investment securities	1.41%	1.32%	1.13%	1.36%	1.11%
Death benefit on bank owned life insurance (BOLI)	-0.02%	0.00%	0.00%	-0.01%	0.00%
Tax effect	0.00%	0.00%	0.00%	0.00%	0.00%
ROAA excluding death benefit on BOLI	1.39%	1.32%	1.13%	1.35%	1.11%
Acquisition-related purchase accounting adjustments (PAUs)	-0.16%	-0.21%	-0.12%	-0.19%	-0.12%
Tax effect	0.03%	0.04%	0.04%	0.04%	0.04%
Core ROAA	1.26%	1.15%	1.05%	1.20%	1.03%

Non-GAAP Reconciliation of Return on Average Common Equity

Average Common Equity	$ 465,968	$ 460,076	$ 355,435	$ 463,156	$ 350,305
Return on average common equity (ROACE) as reported	12.15%	11.29%	10.24%	11.72%	9.96%
Merger expenses	0.00%	0.00%	0.23%	0.00%	0.12%
Tax effect	0.00%	0.00%	-0.08%	0.00%	-0.04%
ROACE excluding merger expenses	12.15%	11.29%	10.39%	11.72%	10.04%
Gain on sale of investment securities	0.00%	-0.01%	0.00%	0.00%	-0.02%
Tax effect	0.00%	0.00%	0.00%	0.00%	0.01%
ROACE excluding gain on sale of investment securities	12.15%	11.28%	10.39%	11.72%	10.03%
Death benefit on bank owned life insurance (BOLI)	-0.13%	0.00%	0.00%	-0.07%	0.00%
Tax effect	0.03%	0.00%	0.00%	0.01%	0.00%
ROACE excluding death benefit on BOLI	12.05%	11.28%	10.39%	11.66%	10.03%
Acquisition-related purchase accounting adjustments (PAUs)	-1.41%	-1.80%	-1.06%	-1.60%	-1.13%
Tax effect	0.30%	0.38%	0.37%	0.34%	0.39%
Core ROACE	10.94%	9.86%	9.70%	10.40%	9.29%

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HORIZON BANCORP, INC. AND SUBSIDIARIES

Quantitative and Qualitative Disclosures About Market Risk

For the Three and Six Months ended June 30, 2018 and 2017

ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

We refer you to Horizon s 2017 Annual Report on Form 10-K for analysis of its interest rate sensitivity. Horizon believes there have been no significant changes in its interest rate sensitivity since it was reported in its 2017 Annual Report on Form 10-K.

ITEM 4. CONTROLS AND PROCEDURES

Evaluation of Disclosure Controls and Procedures

Based on an evaluation of disclosure controls and procedures as of June 30, 2018, Horizon s Chief Executive Officer and Chief Financial Officer have evaluated the effectiveness of Horizon s disclosure controls (as defined in Exchange Act Rule 13a-15(e) of the Securities Exchange Act of 1934 (the Exchange Act)). Based on such evaluation, such officers have concluded that, as of the evaluation date, Horizon s disclosure controls and procedures are effective to ensure that the information required to be disclosed by Horizon in the reports it files under the Exchange Act is recorded, processed, summarized and reported within the time specified in Securities and Exchange Commission rules and forms and are designed to ensure that information required to be disclosed in those reports is accumulated and communicated to management as appropriate to allow timely decisions regarding disclosure.

Changes in Internal Control Over Financial Reporting

Horizon s management, including its Chief Executive Officer and Chief Financial Officer, also have concluded that during the fiscal quarter ended June 30, 2018, there have been no changes in Horizon s internal control over financial reporting that have materially affected, or are reasonably likely to materially affect, Horizon s internal control over financial reporting.

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HORIZON BANCORP, INC. AND SUBSIDIARIES

Part II Other Information

For the Three and Six Months ended June 30, 2018 and 2017

ITEM 1. LEGAL PROCEEDINGS

Horizon and its subsidiaries are involved in various legal proceedings incidental to the conduct of their business. Management does not expect that the outcome of any such proceedings will have a material adverse effect on our consolidated financial position or results of operations.

ITEM 1A. RISK FACTORS

There have been no material changes from the factors previously disclosed under Item 1A of Horizon s Annual Report on Form 10-K for 2017.

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

Not Applicable

ITEM 3. DEFAULTS UPON SENIOR SECURITIES

Not Applicable

ITEM 4. MINE SAFETY DISCLOSURES

Not Applicable

ITEM 5. OTHER INFORMATION

Not Applicable

HORIZON BANCORP, INC. AND SUBSIDIARIES

Part II Other Information

For the Three and Six Months ended June 30, 2018 and 2017

ITEM 6. EXHIBITS

(a) Exhibits

Exhibit Index

Exhibit No.	Description	Location
3.1	Amended and Restated Articles of Incorporation of Horizon Bancorp, Inc., as amended by the Articles of Amendment effective May 16, 2018	Incorporated by reference to Exhibit 3.1 to Registrant s Form 8-K filed May 16, 2018
10.1	Horizon Bancorp Amended and Restated 2013 Omnibus Equity Incentive Plan (effective February 1, 2013; amended and restated as of December 19, 2017; approved by shareholders effective May 3, 2018	Incorporated by reference to Appendix B to Registrant s Definitive Proxy Statement for its 2018 Annual Meeting of Shareholders
31.1	Certification of Craig M. Dwight	Attached
31.2	Certification of Mark E. Secor	Attached
32	Certification of Chief Executive and Chief Financial Officer pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002	Attached
101	Interactive Data Files	Attached

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SIGNATURES

Pursuant to the requirements of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned thereunto duly authorized.

HORIZON BANCORP

Dated: August 7, 2018	/s/ Craig M. Dwight Craig M. Dwight Chief Executive Officer
Dated: August 7, 2018	/s/ Mark E. Secor Mark E. Secor Chief Financial Officer