

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION

WASHINGTON, D.C. 20549

FORM 10-Q

Quarterly Report pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934 for the Quarterly Period Ended September 30, 2021

Commission File Number 001-15877

German American Bancorp, Inc.
(Exact name of registrant as specified in its charter)

Indiana
(State or other jurisdiction of
incorporation or organization)

35-1547518
(I.R.S. Employer
Identification No.)

711 Main Street, Jasper, Indiana 47546
(Address of Principal Executive Offices and Zip Code)

Registrant's telephone number, including area code: (812) 482-1314

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 every Interactive Data File required to be submitted 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 such files).

Yes ☒ No ☐

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, a smaller reporting company, or an emerging growth company:

Large accelerated filer ☒ Accelerated filer ☐ Non-accelerated filer ☐ Smaller reporting company ☐ Emerging growth company ☐

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

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

Yes ☐ No ☒

Securities registered pursuant to Section 12(b) of the Act:

Title of each class	Trading Symbol(s)	Name of each exchange on which registered
Common Stock, no par value	GABC	Nasdaq Global Select Market

As of November 2, 2021, the registrant had 26,546,100 outstanding shares of Common Stock, no par value.

CAUTION REGARDING FORWARD-LOOKING STATEMENTS AND ASSOCIATED RISKS

Information included in or incorporated by reference in this Quarterly Report on Form 10-Q, our other filings with the Securities and Exchange Commission (the “SEC”) and our press releases or other public statements contains or may contain “forward-looking statements” within the meaning of the Private Securities Litigation Reform Act of 1995. Please refer to the discussions of our forward-looking statements and associated risks in our Annual Report on Form 10-K for the year ended December 31, 2020, in Item 1, “Business - Forward-Looking Statements and Associated Risks” and our discussion of risk factors in Item 1A, “Risk Factors” of that Annual Report on Form 10-K, as updated and supplemented from time to time by our subsequent SEC filings, including by the discussion under the heading “Forward-Looking Statements and Associated Risks” at the conclusion of Item 2 of Part I of this Report (“Management’s Discussion and Analysis of Financial Condition and Results of Operations”), and by the additional risk factors set forth in Part II, Item 1A, “Risk Factors” of this Report.

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GLOSSARY OF TERMS AND ACRONYMS

As used in this Report, references to “Company,” “we,” “our,” “us,” and similar terms refer to German American Bancorp, Inc. and its consolidated subsidiaries as a whole. Occasionally, we will refer to the term “parent company” or “holding company” when we mean to refer to only German American Bancorp, Inc. and the term “Bank” when we mean to refer only to German American Bank, the Company’s bank subsidiary.

The terms and acronyms identified below are used throughout this Report, including the Notes to Consolidated Financial Statements. You may find it helpful to refer to this Glossary as you read this Report.

2009 ESPP: German American Bancorp, Inc. 2009 Employee Stock Purchase Plan

2019 ESPP: German American Bancorp, Inc. 2019 Employee Stock Purchase Plan

2019 LTI Plan: German American Bancorp, Inc. 2019 Long-Term Equity Incentive Plan

ASC: Accounting Standards Codification

ASU: Accounting Standards Update

Basel III Rules: Regulatory capital rules agreed to by the Basel Committee on Banking Supervision, as issued by the FRB and OCC and published in the Federal Register on October 11, 2013

CAA: 2021 Consolidated Appropriations Act enacted on December 27, 2020, which included a \$900 billion COVID-19 relief package

CARES Act: Coronavirus Aid, Relief and Economic Security Act

CECL: Current expected credit losses

CET1: Common Equity Tier 1

CMO: Collateralized mortgage obligations

COVID-19: Novel coronavirus disease 2019 declared, in March 2020, by the World Health Organization as a global pandemic and by the President of the United States as a national emergency

CUB: Citizens Union Bancorp of Shelbyville, Inc., which is party to an Agreement and Plan of Reorganization with the Company, pursuant to which it will be merged with and into the Company, subject to certain conditions

Dodd-Frank Act: Dodd-Frank Wall Street Reform and Consumer Protection Act

FASB: Financial Accounting Standards Board

FDIC: Federal Deposit Insurance Corporation

federal banking

regulators: The FRB, the OCC, and the FDIC, collectively

FHLB: Federal Home Loan Bank

FRB: Board of Governors of the Federal Reserve System

GAAP: Generally Accepted Accounting Principles in the United States of America

LIBOR: London Interbank Offered Rate

MBS: Mortgage-backed securities

NPV: Net portfolio value

OCC: Office of the Comptroller of the Currency

PCD: Purchased with credit deterioration

PCI: Purchased credit impaired

PPP: Paycheck Protection Program established under the CARES Act

PPPL Facility: Paycheck Protection Program Liquidity Facility authorized by the FRB pursuant to the Federal Reserve Act

SBA: Small Business Administration

SEC: Securities and Exchange Commission

TDR: Troubled Debt Restructurings

PART I. FINANCIAL INFORMATION
Item 1. Unaudited Financial Statements

GERMAN AMERICAN BANCORP, INC.
CONSOLIDATED BALANCE SHEETS
(unaudited, dollars in thousands except share and per share data)

	September 30, 2021	December 31, 2020
ASSETS		
Cash and Due from Banks	\$ 54,617	\$ 57,972
Federal Funds Sold and Other Short-term Investments	394,126	287,776
Cash and Cash Equivalents	448,743	345,748
Interest-bearing Time Deposits with Banks	745	1,241
Securities Available-for-Sale, at Fair Value (Amortized Cost \$1,681,122 for September 30, 2021; Amortized Cost \$1,172,175 for December 31, 2020; No Allowance for Credit Losses)	1,696,225	1,217,852
Other Investments	353	353
Loans Held-for-Sale, at Fair Value	15,361	16,904
Loans	3,012,989	3,091,998
Less: Unearned Income	(3,729)	(3,926)
Allowance for Credit Losses	(37,798)	(46,859)
Loans, Net	2,971,462	3,041,213
Stock in FHLB of Indianapolis and Other Restricted Stock, at Cost	13,048	13,168
Premises, Furniture and Equipment, Net	89,649	96,593
Other Real Estate	112	325
Goodwill	121,761	121,956
Intangible Assets	6,514	8,984
Company Owned Life Insurance	69,895	69,250
Accrued Interest Receivable and Other Assets	41,882	43,990
TOTAL ASSETS	\$ 5,475,750	\$ 4,977,577
LIABILITIES		
Non-interest-bearing Demand Deposits	\$ 1,453,197	\$ 1,183,442
Interest-bearing Demand, Savings, and Money Market Accounts	2,762,328	2,428,636
Time Deposits	377,426	494,452
Total Deposits	4,592,951	4,106,530
FHLB Advances and Other Borrowings	186,389	194,529
Accrued Interest Payable and Other Liabilities	46,271	51,809
TOTAL LIABILITIES	4,825,611	4,352,868
SHAREHOLDERS' EQUITY		
Common Stock, no par value, \$1 stated value; 45,000,000 shares authorized	26,546	26,502
Additional Paid-in Capital	275,682	274,385
Retained Earnings	336,647	288,447
Accumulated Other Comprehensive Income	11,264	35,375
TOTAL SHAREHOLDERS' EQUITY	650,139	624,709
TOTAL LIABILITIES AND SHAREHOLDERS' EQUITY	\$ 5,475,750	\$ 4,977,577
End of period shares issued and outstanding	26,546,100	26,502,157

See accompanying notes to consolidated financial statements.

GERMAN AMERICAN BANCORP, INC.
CONSOLIDATED STATEMENTS OF INCOME
(unaudited, dollars in thousands except per share data)

	Three Months Ended September 30,	
	2021	2020
INTEREST INCOME		
Interest and Fees on Loans	\$ 35,483	\$ 36,543
Interest on Federal Funds Sold and Other Short-term Investments	141	45
Interest and Dividends on Securities:		
Taxable	3,261	2,350
Non-taxable	4,690	3,175
TOTAL INTEREST INCOME	43,575	42,113
INTEREST EXPENSE		
Interest on Deposits	1,139	2,492
Interest on FHLB Advances and Other Borrowings	1,149	1,233
TOTAL INTEREST EXPENSE	2,288	3,725
NET INTEREST INCOME	41,287	38,388
Provision (Benefit) for Credit Losses	(2,000)	4,500
NET INTEREST INCOME AFTER PROVISION FOR CREDIT LOSSES	43,287	33,888
NON-INTEREST INCOME		
Trust and Investment Product Fees	2,690	1,957
Service Charges on Deposit Accounts	2,017	1,773
Insurance Revenues	2,007	1,989
Company Owned Life Insurance	493	355
Interchange Fee Income	3,339	2,795
Other Operating Income	2,595	942
Net Gains on Sales of Loans	2,197	2,861
Net Gains on Securities	218	607
TOTAL NON-INTEREST INCOME	15,556	13,279
NON-INTEREST EXPENSE		
Salaries and Employee Benefits	17,274	17,409
Occupancy Expense	2,530	2,418
Furniture and Equipment Expense	923	944
FDIC Premiums	383	326
Data Processing Fees	2,006	1,693
Professional Fees	1,357	875
Advertising and Promotion	897	708
Intangible Amortization	661	860
Other Operating Expenses	6,413	4,187
TOTAL NON-INTEREST EXPENSE	32,444	29,420
Income before Income Taxes	26,399	17,747
Income Tax Expense	4,913	3,154
NET INCOME	\$ 21,486	\$ 14,593
Basic Earnings per Share	\$ 0.81	\$ 0.55
Diluted Earnings per Share	\$ 0.81	\$ 0.55

See accompanying notes to consolidated financial statements.

GERMAN AMERICAN BANCORP, INC.
CONSOLIDATED STATEMENTS OF INCOME
(unaudited, dollars in thousands except per share data)

	Nine Months Ended September 30,	
	2021	2020
INTEREST INCOME		
Interest and Fees on Loans	\$ 105,091	\$ 112,481
Interest on Federal Funds Sold and Other Short-term Investments	329	287
Interest and Dividends on Securities:		
Taxable	9,391	8,166
Non-taxable	12,583	8,291
TOTAL INTEREST INCOME	127,394	129,225
INTEREST EXPENSE		
Interest on Deposits	3,850	11,892
Interest on FHLB Advances and Other Borrowings	3,445	4,230
TOTAL INTEREST EXPENSE	7,295	16,122
NET INTEREST INCOME	120,099	113,103
Provision (Benefit) for Credit Losses	(8,500)	15,550
NET INTEREST INCOME AFTER PROVISION FOR CREDIT LOSSES	128,599	97,553
NON-INTEREST INCOME		
Trust and Investment Product Fees	7,668	5,855
Service Charges on Deposit Accounts	5,430	5,375
Insurance Revenues	7,319	7,048
Company Owned Life Insurance	1,230	1,933
Interchange Fee Income	9,651	7,753
Other Operating Income	5,287	2,251
Net Gains on Sales of Loans	6,417	7,378
Net Gains on Securities	1,493	2,190
TOTAL NON-INTEREST INCOME	44,495	39,783
NON-INTEREST EXPENSE		
Salaries and Employee Benefits	51,454	50,691
Occupancy Expense	8,735	7,461
Furniture and Equipment Expense	2,896	2,963
FDIC Premiums	1,046	449
Data Processing Fees	5,528	5,142
Professional Fees	4,030	3,041
Advertising and Promotion	2,384	2,661
Intangible Amortization	2,132	2,729
Other Operating Expenses	14,535	12,699
TOTAL NON-INTEREST EXPENSE	92,740	87,836
Income before Income Taxes	80,354	49,500
Income Tax Expense	15,489	8,180
NET INCOME	\$ 64,865	\$ 41,320
Basic Earnings per Share	\$ 2.44	\$ 1.56
Diluted Earnings per Share	\$ 2.44	\$ 1.56

See accompanying notes to consolidated financial statements.

GERMAN AMERICAN BANCORP, INC.
CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME (LOSS)
(unaudited, dollars in thousands)

	Three Months Ended September 30,	
	2021	2020
NET INCOME	<u><u>\$ 21,486</u></u>	<u><u>\$ 14,593</u></u>
Other Comprehensive Income (Loss):		
Unrealized Gains (Losses) on Securities:		
Unrealized Holding Gain (Loss) Arising During the Period	(18,983)	63
Reclassification Adjustment for Gains Included in Net Income	(218)	(607)
Tax Effect	4,040	138
Net of Tax	<u>(15,161)</u>	<u>(406)</u>
Total Other Comprehensive Income (Loss)	<u>(15,161)</u>	<u>(406)</u>
COMPREHENSIVE INCOME (LOSS)	<u><u>\$ 6,325</u></u>	<u><u>\$ 14,187</u></u>

	Nine Months Ended September 30,	
	2021	2020
NET INCOME	<u><u>\$ 64,865</u></u>	<u><u>\$ 41,320</u></u>
Other Comprehensive Income (Loss):		
Unrealized Gains (Losses) on Securities:		
Unrealized Holding Gain (Loss) Arising During the Period	(29,081)	22,051
Reclassification Adjustment for Gains Included in Net Income	(1,493)	(2,190)
Tax Effect	6,463	(4,223)
Net of Tax	<u>(24,111)</u>	<u>15,638</u>
Total Other Comprehensive Income (Loss)	<u>(24,111)</u>	<u>15,638</u>
COMPREHENSIVE INCOME (LOSS)	<u><u>\$ 40,754</u></u>	<u><u>\$ 56,958</u></u>

See accompanying notes to consolidated financial statements.

GERMAN AMERICAN BANCORP, INC.
CONSOLIDATED STATEMENTS OF CHANGES IN SHAREHOLDERS' EQUITY
(unaudited, dollars in thousands)

	Common Stock		Additional Paid-in Capital	Retained Earnings	Accumulated Other Comprehensive Income (Loss)	Total Shareholders' Equity
	Shares	Amount				
Balances, December 31, 2020	26,502,157	\$ 26,502	\$ 274,385	\$ 288,447	\$ 35,375	\$ 624,709
Net Income	—	—	—	19,557	—	19,557
Other Comprehensive Income (Loss)	—	—	—	—	(21,828)	(21,828)
Cash Dividends (\$0.21 per share)	—	—	—	(5,554)	—	(5,554)
Issuance of Common Stock for:						
Restricted Share Grants	44,123	44	285	—	—	329
Balances, March 31, 2021	26,546,280	\$ 26,546	\$ 274,670	\$ 302,450	\$ 13,547	\$ 617,213
Net Income	—	—	—	23,822	—	23,822
Other Comprehensive Income (Loss)	—	—	—	—	12,878	12,878
Cash Dividends (\$0.21 per share)	—	—	—	(5,555)	—	(5,555)
Issuance of Common Stock for:						
Restricted Share Grants	(576)	—	639	—	—	639
Balances, June 30, 2021	26,545,704	\$ 26,546	\$ 275,309	\$ 320,717	\$ 26,425	\$ 648,997
Net Income	—	—	—	21,486	—	21,486
Other Comprehensive Income (Loss)	—	—	—	—	(15,161)	(15,161)
Cash Dividends (\$0.21 per share)	—	—	—	(5,556)	—	(5,556)
Issuance of Common Stock for:						
Restricted Share Grants	396	—	373	—	—	373
Balances, September 30, 2021	26,546,100	\$ 26,546	\$ 275,682	\$ 336,647	\$ 11,264	\$ 650,139

See accompanying notes to consolidated financial statements.

GERMAN AMERICAN BANCORP, INC.
CONSOLIDATED STATEMENTS OF CHANGES IN SHAREHOLDERS' EQUITY
(unaudited, dollars in thousands)

	Common Stock						
	Shares	Amount	Additional Paid-in Capital	Retained Earnings	Accumulated Other Comprehensive Income (Loss)	Total Shareholders' Equity	
Balances, December 31, 2019	26,671,368	\$ 26,671	\$ 278,954	\$ 253,090	\$ 15,105	\$ 573,820	
Cumulative Effect of Change in Accounting Principles (See Note 2 - Recent Accounting Pronouncements)	—	—	—	(6,717)	—	(6,717)	
Balance, January 1, 2020	26,671,368	26,671	278,954	246,373	15,105	567,103	
Net Income	—	—	—	12,472	—	12,472	
Other Comprehensive Income	—	—	—	—	13,255	13,255	
Cash Dividends (\$0.19 per share)	—	—	—	(5,065)	—	(5,065)	
Issuance of Common Stock for:							
Restricted Share Grants	41,752	42	228	—	—	270	
Stock Repurchase	(173,089)	(173)	(4,322)	—	—	(4,495)	
Balances, March 31, 2020	26,540,031	\$ 26,540	\$ 274,860	\$ 253,780	\$ 28,360	\$ 583,540	
Net Income	—	—	—	14,255	—	14,255	
Other Comprehensive Income	—	—	—	—	2,789	2,789	
Cash Dividends (\$0.19 per share)	—	—	—	(5,024)	—	(5,024)	
Issuance of Common Stock for:							
Restricted Share Grants	1,426	1	281	—	—	282	
Stock Repurchase	(44,166)	(44)	(1,124)	—	—	(1,168)	
Balances, June 30, 2020	26,497,291	\$ 26,497	\$ 274,017	\$ 263,011	\$ 31,149	\$ 594,674	
Net Income	—	—	—	14,593	—	14,593	
Other Comprehensive Income	—	—	—	—	(406)	(406)	
Cash Dividends (\$0.19 per share)	—	—	—	(5,025)	—	(5,025)	
Issuance of Common Stock for:							
Restricted Share Grants	(378)	—	254	—	—	254	
Stock Repurchase	(4,047)	(4)	(105)	—	—	(109)	
Balances, September 30, 2020	26,492,866	\$ 26,493	\$ 274,166	\$ 272,579	\$ 30,743	\$ 603,981	

See accompanying notes to consolidated financial statements.

GERMAN AMERICAN BANCORP, INC.
CONSOLIDATED STATEMENTS OF CASH FLOWS
(unaudited, dollars in thousands)

	Nine Months Ended September 30,	
	2021	2020
CASH FLOWS FROM OPERATING ACTIVITIES		
Net Income	\$ 64,865	\$ 41,320
Adjustments to Reconcile Net Income to Net Cash from Operating Activities:		
Net Amortization on Securities	4,873	4,097
Depreciation and Amortization	6,723	7,043
Loans Originated for Sale	(199,491)	(230,399)
Proceeds from Sales of Loans Held-for-Sale	207,767	226,237
Provision (Benefit) for Credit Losses	(8,500)	15,550
Gain on Sale of Loans, net	(6,417)	(7,378)
Gain on Securities, net	(1,493)	(2,190)
Gain on Sales of Other Real Estate and Repossessed Assets	(105)	(48)
Loss on Disposition and Donation of Premises and Equipment	482	127
Loss on Disposition of Land	—	30
Increase in Cash Surrender Value of Company Owned Life Insurance	(1,079)	(1,092)
Equity Based Compensation	1,341	813
Change in Assets and Liabilities:		
Interest Receivable and Other Assets	2,348	(6,046)
Interest Payable and Other Liabilities	2,619	8,114
Net Cash from Operating Activities	73,933	56,178
CASH FLOWS FROM INVESTING ACTIVITIES		
Proceeds from Maturity of Other Short-term Investments	496	496
Proceeds from Maturities of Securities Available-for-Sale	160,850	139,679
Proceeds from Sales of Securities Available-for-Sale	102,823	74,693
Purchase of Securities Available-for-Sale	(776,001)	(378,503)
Proceeds from Redemption of Federal Home Loan Bank Stock	120	800
Loans Made to Customers, net of Payments Received	59,455	(138,132)
Proceeds from Sales of Other Real Estate	1,315	316
Property and Equipment Expenditures	(2,794)	(5,162)
Proceeds from Sales of Land and Buildings	1,614	612
Proceeds from Life Insurance	434	1,082
Sale of Bank Branches	1,694	—
Net Cash from Investing Activities	(449,994)	(304,119)
CASH FLOWS FROM FINANCING ACTIVITIES		
Change in Deposits	504,102	550,003
Change in Short-term Borrowings	(314)	(94,756)
Repayments of Long-term Debt	(8,067)	(40,604)
Issuance (Retirement) of Common Stock	—	(5,779)
Dividends Paid	(16,665)	(15,114)
Net Cash from Financing Activities	479,056	393,750
Net Change in Cash and Cash Equivalents	102,995	145,809
Cash and Cash Equivalents at Beginning of Year	345,748	103,884
Cash and Cash Equivalents at End of Period	<u>\$ 448,743</u>	<u>\$ 249,693</u>
Cash Paid During the Period for		
Interest	\$ 7,254	\$ 16,796
Income Taxes	13,605	8,000
Supplemental Non Cash Disclosures		
Reclassification of Land and Buildings to Other Assets	\$ 1,536	\$ —

See accompanying notes to consolidated financial statements.

GERMAN AMERICAN BANCORP, INC.
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
September 30, 2021
(unaudited, dollars in thousands except share and per share data)

NOTE 1 – Basis of Presentation and Market Conditions

German American Bancorp, Inc. operates primarily in the banking industry. The accounting and reporting policies of German American Bancorp, Inc. and its subsidiaries (hereinafter collectively referred to as the "Company") conform to U.S. generally accepted accounting principles. Certain information and footnote disclosures normally included in financial statements prepared in accordance with U.S. generally accepted accounting principles have been condensed or omitted. All adjustments which are, in the opinion of management, necessary for a fair presentation of the results for the periods reported have been included in the accompanying unaudited consolidated financial statements, and all such adjustments are of a normal recurring nature. It is suggested that these consolidated financial statements and notes be read in conjunction with the financial statements and notes thereto in the Company's Annual Report on Form 10-K for the year ended December 31, 2020. Certain items included in the prior period financial statements were reclassified to conform to the current presentation. There was no effect on net income or total shareholders' equity based on these reclassifications.

Impact of COVID-19

The novel coronavirus disease 2019 (COVID-19) pandemic continued to impact our operations during the quarter ended September 30, 2021. While uncertainty remains as to the future effects of the pandemic, an improving business climate, supported by unprecedented fiscal stimulus, an accommodative Federal Reserve, and modest increases in COVID-19 vaccination rates, has helped to mitigate the negative impacts of the pandemic on our financial condition and results of operations, despite the challenges presented by very low interest rates, muted loan growth, and excess liquidity.

NOTE 2 - Recent Accounting Pronouncements

Loan Modifications and Troubled Debt Restructurings due to COVID-19

On April 7, 2020, the Board of Governors of the Federal Reserve System (the "FRB"), the Office of the Comptroller of the Currency (the "OCC"), and the Federal Deposit Insurance Corporation (the "FDIC") and, together with the FRB and OCC, the "federal banking regulators") issued a revised Interagency Statement on Loan Modifications and Reporting for Financial Institutions, which, among other things, encouraged financial institutions to work prudently with borrowers who are or may be unable to meet their contractual payment obligations because of the effects of COVID-19, and stated that institutions generally do not need to categorize COVID-19-related modifications as troubled debt restructurings and that the agencies will not direct supervised institutions to automatically categorize all COVID-19 related loan modifications as troubled debt restructurings. Similarly, under the CARES Act, provisions were included that allow for loan modifications to not be classified as TDRs if certain criteria are met. This TDR exemption, which was set to expire on December 31, 2020, was extended under the CAA to, effectively, January 1, 2022.

Adopted Accounting Guidance in 2020

In June 2016, the Financial Accounting Standards Board ("FASB") issued ASU 2016-13, Financial Instruments - Credit Losses (Topic 326): Measurement of Credit Losses on Financial Instruments, which replaces the incurred loss methodology with an expected loss methodology that is referred to as the current expected credit loss (CECL) methodology. The measurement of expected credit losses under the CECL methodology is applicable to financial assets measured at amortized cost, including loan receivables and held-to-maturity debt securities. It also applies to off-balance sheet credit exposures not accounted for as insurance (loan commitments, standby letters of credit, financial guarantees, and other similar instruments). The new CECL model requires an estimate of expected credit losses, measured over the contractual life of an instrument, which considers reasonable and supportable forecasts of future economic conditions in addition to information about past events and current conditions. The standard provides significant flexibility and requires a high degree of judgement with regards to pooling financial assets with similar risk characteristics and adjusting the relevant historical loss information in order to develop an estimate of expected lifetime losses.

The Company adopted ASC 326 on January 1, 2020 using the modified retrospective approach. Results for reporting periods after January 1, 2020 are presented under ASC 326 while prior period amounts continue to be reported in accordance with previously applicable GAAP. The Company recorded a net reduction of retained earnings of \$6,717 upon adoption.

The Company adopted ASC 326 using the prospective transition approach for financial assets purchased with credit deterioration (PCD) that were previously classified as purchased credit impaired (PCI) and accounted for under ASC 310-30. In accordance with the standard, management did not reassess whether PCI assets met the criteria of PCD assets as of the date

GERMAN AMERICAN BANCORP, INC.
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
September 30, 2021
(unaudited, dollars in thousands except share and per share data)

NOTE 2 - Recent Accounting Pronouncements (continued)

of adoption. On January 1, 2020, the amortized cost basis of the PCD assets were adjusted to reflect the addition of \$6,886 of the allowance for credit losses. The remaining noncredit discount (based on the adjusted amortized cost basis) will be accreted into interest income at the effective interest rate as of January 1, 2020.

The Company expanded the loan portfolio segments used to determine the allowance for credit losses for loans into eight loan segments as opposed to six loan segments under the incurred loss methodology. The following table illustrates the impact of the segment expansion as of January 1, 2020.

(dollars in thousands)	December 31, 2019 Statement Balance	Segment Portfolio Reclassifications	December 31, 2019 After Reclassification
Loans:			
Commercial and Industrial Loans	\$ 589,758	\$ (57,257)	\$ 532,501
Commercial Real Estate Loans	1,495,862	N/A	1,495,862
Agricultural Loans	384,526	N/A	384,526
Leases	N/A	57,257	57,257
Home Equity Loans	225,755	N/A	225,755
Consumer Loans	81,217	(11,953)	69,264
Credit Cards	N/A	11,953	11,953
Residential Mortgage Loans	304,855	N/A	304,855
Total Loans	<u>\$ 3,081,973</u>	<u>\$ —</u>	<u>\$ 3,081,973</u>

The following table illustrates the impact of ASC 326:

(dollars in thousands)	December 31, 2019 After Reclassification	Impact of ASC 326 Adoption	January 1, 2020 Post-ASC 326 Adoption
Assets:			
Loans:			
Commercial and Industrial Loans	\$ 532,501	\$ 2,191	\$ 534,692
Commercial Real Estate Loans	1,495,862	4,385	1,500,247
Agricultural Loans	384,526	128	384,654
Leases	57,257	—	57,257
Home Equity Loans	225,755	35	225,790
Consumer Loans	69,264	—	69,264
Credit Cards	11,953	—	11,953
Residential Mortgage Loans	304,855	147	305,002
Allowance for Credit Losses on Loans	(16,278)	(15,653)	(31,931)
Liabilities:			
Allowance for Credit Losses on Unfunded Loan Commitments	\$ —	\$ (173)	\$ (173)

In December 2018, federal banking regulators approved a final rule to address changes to credit loss accounting under GAAP, including banking organizations' implementation of CECL. The final rule provides banking organizations the option to phase in over a three-year period the day-one adverse effects on regulatory capital that may result from the adoption of the new accounting standard. On March 27, 2020, in an action related to the CARES Act, the federal banking regulators announced an interim final rule to delay the estimated impact on regulatory capital stemming from the implementation of CECL. The interim final rule, which was finalized effective September 30, 2020, maintains the three-year transition option in the previous rule and provides banks the option to delay for two years an estimate of CECL's effect on regulatory capital, relative to the incurred loss methodology's effect on regulatory capital, followed by a three-year transition period (five-year transition option). The Company has elected to adopt the five-year transition option. This election of the transition option is applicable only to

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NOTE 2 - Recent Accounting Pronouncements (continued)

regulatory capital computations under federal banking regulations and does not otherwise impact the financial statements prepared in accordance with GAAP.

Loans

Loans that management has the intent and ability to hold for the foreseeable future or until maturity or payoff are reported at amortized cost. Amortized cost is the principal balance outstanding, net of purchase premiums and discounts, deferred loan fees and costs. Accrued interest receivable totaled \$11,641 at September 30, 2021 and \$14,133 at December 31, 2020. Accrued interest receivable was reported in Accrued Interest Receivable and Other Assets on the Consolidated Balance Sheets. Interest income is accrued on the unpaid principal balance. Loan origination fees and costs are deferred and recognized in interest income using the level-yield method without anticipating prepayments.

Purchase Credit Deteriorated (PCD) Loans

The Company has purchased loans, some of which have experienced more than insignificant credit deterioration since origination. PCD loans are recorded at the amount paid. An allowance for credit losses on loans is determined using the same methodology as other loans held for investment. The initial allowance for credit losses on loans determined on a collective basis is allocated to individual loans. The sum of the loan's purchase price and allowance for credit losses on loans becomes its initial amortized cost basis. The difference between the initial amortized cost basis and the par value of the loan is a noncredit discount or premium, which is amortized into interest income over the life of the loan. Subsequent changes to the allowance for credit losses on loans are recorded through provision expense.

Allowance for Credit Losses - Loans

The allowance for credit losses is a valuation account that is deducted from the loans' amortized cost basis to present the net amount expected to be collected on the loans. Loans are charged off against the allowance when management believes the uncollectibility of a loan balance is confirmed. Expected recoveries do not exceed the aggregate of amounts previously charged-off and expected to be charged-off.

The Company estimates the allowance balance using relevant available information, from internal and external sources, relating to past events, current conditions, and reasonable and supportable forecasts. Historical loss experience provides the basis for the estimation of expected credit losses. Adjustments to historical loss information are made for changes in underwriting standards, portfolio mix, delinquency level, changes in environmental conditions, unemployment rates, risk classifications and collateral values.

The allowance for credit losses is measured on a collective (pooled) basis when similar risk characteristics exist. The Company has identified the following portfolio segments and measures the allowance for credit losses using the following methods:

Commercial and Industrial Loans - The principal risk of commercial and industrial loans is that these loans are primarily based on the identified cash flow of the borrower and secondarily on the collateral underlying the loans. Most commercial loans are secured by accounts receivable, inventory and equipment. If cash flow from business operations is reduced, the borrower's ability to repay the loan may diminish, and over time, it may also be difficult to substantiate current value of inventory and equipment. Repayment of these loans are more sensitive than other types of loans to adverse conditions in the general economy.

Commercial Real Estate Loans - Commercial real estate lending 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 adversely affected by conditions in the real estate markets or in the general economy. Commercial real estate loans are collateralized by the borrower's underlying real estate. Therefore, diminished cash flows not only affects the ability to repay the loan, it may also reduce the underlying collateral value.

Agricultural Loans - This portfolio is diversified between real estate financing, equipment financing and lines of credit in various segments including grain production, poultry production and livestock production. Mitigating any concentration of risk that may exist in the Company's agricultural loan portfolio is the use of federal government guarantee programs.

Leases - Leases are primarily for equipment leased to varying types of businesses. If the cash flows from the business operations is reduced, the business's ability to repay the lease is diminished as well.

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NOTE 2 - Recent Accounting Pronouncements (continued)

Home Equity Loans - Home equity loans are generally secured by 1-4 family residences that are owner-occupied. Repayment of these loans is primarily dependent on the personal income of the borrowers, which can be impacted by unemployment levels in the market area due to economic conditions.

Consumer Loans - Consumer loan repayment is typically dependent on the borrower remaining employed through the life of the loan as well as the borrower maintaining the underlying collateral adequately.

Credit Cards - Credit card loan are unsecured and repayment is primarily dependent on the personal income of the borrower.

Residential Mortgage Loans - Residential mortgage loans are typically secured by 1-4 family residences that are owner-occupied. Repayment of these loans is primarily dependent on the personal income of the borrowers, which can be impacted by unemployment levels in the market area due to economic conditions. Repayment may also be impacted by changes in residential property values.

Loans that do not share risk characteristics are evaluated on an individual basis. Loans evaluated individually are also not included in the collective evaluation. When the borrower is experiencing financial difficulty at the reporting date and repayment is expected to be provided substantially through the operation or sale of the collateral, expected credit losses are based on the fair value of the collateral at the reporting date adjusted for selling costs.

Troubled Debt Restructurings ("TDR")

A loan for which the terms have been modified resulting in a concession, and for which the borrower is experiencing financial difficulties, is considered to be a TDR. The allowances for credit losses on loans on a TDR is measured using the same method as all other loans held for investment, except that the original interest rate is used to discount the expected cash flows, not the rate specified within the restructuring. See "Loan Modifications and Troubled Debt Restructurings due to COVID-19" at the beginning of this Note 2 for additional information.

Allowance for Credit Losses on Available-For-Sale Securities

For available-for-sale debt securities in an unrealized loss position, the Company first assesses whether it intends to sell, or it is more likely than not that it will be required to sell, the security before recovery of its amortized cost basis. If either of the criteria regarding intent or requirement to sell is met, the security's amortized cost basis is written down to fair value through income. For debt securities available for sale that do not meet the aforementioned criteria, the Company evaluates whether the decline in fair value has resulted from credit losses or other factors. In making this assessment, management considers the extent to which fair value is less than amortized cost, any changes to the rating of the security by a rating agency, and adverse conditions specifically related to the security, among other factors. If this assessment indicates that a credit loss exists, the present value of cash flows expected to be collected from the security are compared to the amortized cost basis of the security. If the present value of cash flows expected to be collected is less than the amortized cost basis, a credit loss exists and an allowance for credit losses is recorded for the credit loss, limited by the amount that the fair value is less than the amortized cost basis. Any impairment that has not been recorded through an allowance for credit losses is recorded in other comprehensive income.

Changes in the allowance for credit losses are recorded as provision for, or reversal of, credit loss expense. Losses are charged against the allowance when management believes the uncollectibility of an available-for-sale security is confirmed or when either of the criteria regarding intent or requirement to sell is met.

Allowance for Credit Losses on Off-Balance Sheet Credit Exposures

The Company estimates expected credit losses over the contractual period in which the Company is exposed to credit risk via a contractual obligation to extend credit, unless that obligation is unconditionally cancellable by the Company. The allowance for credit losses on off-balance sheet credit exposures is adjusted as a provision for credit loss expense included in other expense on the consolidated income statement. The estimate includes consideration of the likelihood that funding will occur and an estimate of expected credit losses on commitments expected to be funded over its estimated life. Expected utilization rates are compared to the current funded portion of the total commitment amount as a practical expedient for funded exposure at default.

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NOTE 2 - Recent Accounting Pronouncements (continued)

Accounting Guidance Issued But Not Yet Adopted

In March 2020, the FASB issued ASU No. 2020-04, Reference Rate Reform (Topic 848): Facilitation of the Effects of Reference Rate Reform on Financial Reporting. These amendments provide temporary optional guidance to ease the potential burden in accounting for reference rate reform. The ASU provides optional expedients and exceptions for applying generally accepted accounting principles to contract modifications and hedging relationships, subject to meeting certain criteria, that reference LIBOR or another reference rate expected to be discontinued. It is intended to help stakeholders during the global market-wide reference rate transition period. The guidance is effective for all entities as of March 12, 2020 through December 31, 2022. The Company is evaluating the impact of adopting the new guidance on the consolidated financial statements on an ongoing basis with no material expected impact at this time.

NOTE 3 – Per Share Data

The computation of Basic Earnings per Share and Diluted Earnings per Share are as follows:

	Three Months Ended September 30,	
	2021	2020
Basic Earnings per Share:		
Net Income	\$ 21,486	\$ 14,593
Weighted Average Shares Outstanding	26,545,868	26,497,398
Basic Earnings per Share	<u>\$ 0.81</u>	<u>\$ 0.55</u>
Diluted Earnings per Share:		
Net Income	\$ 21,486	\$ 14,593
Weighted Average Shares Outstanding	26,545,868	26,497,398
Potentially Dilutive Shares, Net	—	—
Diluted Weighted Average Shares Outstanding	26,545,868	26,497,398
Diluted Earnings per Share	<u>\$ 0.81</u>	<u>\$ 0.55</u>

For the three months ended September 30, 2021 and 2020, there were no anti-dilutive shares.

	Nine Months Ended September 30,	
	2021	2020
Basic Earnings per Share:		
Net Income	\$ 64,865	\$ 41,320
Weighted Average Shares Outstanding	26,534,044	26,554,369
Basic Earnings per Share	<u>\$ 2.44</u>	<u>\$ 1.56</u>
Diluted Earnings per Share:		
Net Income	\$ 64,865	\$ 41,320
Weighted Average Shares Outstanding	26,534,044	26,554,369
Potentially Dilutive Shares, Net	—	—
Diluted Weighted Average Shares Outstanding	26,534,044	26,554,369
Diluted Earnings per Share	<u>\$ 2.44</u>	<u>\$ 1.56</u>

For the nine months ended September 30, 2021 and 2020, there were no anti-dilutive shares.

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NOTE 4 – Securities

The amortized cost, unrealized gross gains and losses recognized in accumulated other comprehensive income (loss), and fair value of Securities Available-for-Sale were as follows:

Securities Available-for-Sale:	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Allowance for Credit Losses	Fair Value
September 30, 2021					
Obligations of State and Political Subdivisions	\$ 813,088	\$ 26,425	\$ (6,060)	\$ —	\$ 833,453
MBS/CMO	728,789	6,250	(8,407)	—	726,632
US Gov't Sponsored Entities & Agencies	139,245	23	(3,128)	—	136,140
Total	<u>\$ 1,681,122</u>	<u>\$ 32,698</u>	<u>\$ (17,595)</u>	<u>\$ —</u>	<u>\$ 1,696,225</u>
December 31, 2020					
Obligations of State and Political Subdivisions	\$ 548,273	\$ 33,077	\$ (103)	\$ —	\$ 581,247
MBS/CMO	535,526	12,806	(25)	—	548,307
US Gov't Sponsored Entities & Agencies	88,376	120	(198)	—	88,298
Total	<u>\$ 1,172,175</u>	<u>\$ 46,003</u>	<u>\$ (326)</u>	<u>\$ —</u>	<u>\$ 1,217,852</u>

All mortgage-backed securities in the above table (identified above and throughout this Note 4 as "MBS/CMO") are residential and multi-family mortgage-backed securities and guaranteed by government sponsored entities. The US Gov't Sponsored Entities & Agencies in the above table have underlying collateral of equipment, machinery and commercial real estate.

The amortized cost and fair value of Securities at September 30, 2021 by contractual maturity are shown below. Expected maturities may differ from contractual maturities because some issuers have the right to call or prepay certain obligations with or without call or prepayment penalties. Mortgage-backed Securities are not due at a single maturity date and are shown separately.

Securities Available-for-Sale:	Amortized Cost	Fair Value
Due in one year or less	\$ 2,150	\$ 2,173
Due after one year through five years	22,212	23,391
Due after five years through ten years	68,621	73,304
Due after ten years	720,105	734,585
MBS/CMO	728,789	726,632
US Gov't Sponsored Entities & Agencies	139,245	136,140
Total	<u>\$ 1,681,122</u>	<u>\$ 1,696,225</u>

Proceeds from the Sales of Securities are summarized below:

	Three Months Ended September 30, 2021	Three Months Ended September 30, 2020
Proceeds from Sales	\$ 36,075	\$ 11,270
Gross Gains on Sales	218	607
Income Taxes on Gross Gains	46	127

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NOTE 4 - Securities (continued)

	Nine Months Ended September 30, 2021	Nine Months Ended September 30, 2020
Proceeds from Sales	\$ 102,823	\$ 74,693
Gross Gains on Sales	1,493	2,190
Income Taxes on Gross Gains	314	464

The carrying value of securities pledged to secure repurchase agreements, public and trust deposits, and for other purposes as required by law was \$190,514 and \$237,506 as of September 30, 2021 and December 31, 2020, respectively.

Below is a summary of securities with unrealized losses as of September 30, 2021 and December 31, 2020, presented by length of time the securities have been in a continuous unrealized loss position:

	Less than 12 Months		12 Months or More		Total	
	Fair Value	Unrealized Loss	Fair Value	Unrealized Loss	Fair Value	Unrealized Loss
September 30, 2021						
Obligations of State and Political Subdivisions	\$ 303,113	\$ (5,917)	\$ 1,452	\$ (143)	\$ 304,565	\$ (6,060)
MBS/CMO	475,726	(8,404)	309	(3)	476,035	(8,407)
US Gov't Sponsored Entities & Agencies	126,137	(3,128)	—	—	126,137	(3,128)
Total	<u>\$ 904,976</u>	<u>\$ (17,449)</u>	<u>\$ 1,761</u>	<u>\$ (146)</u>	<u>\$ 906,737</u>	<u>\$ (17,595)</u>

	Less than 12 Months		12 Months or More		Total	
	Fair Value	Unrealized Loss	Fair Value	Unrealized Loss	Fair Value	Unrealized Loss
December 31, 2020						
Obligations of State and Political Subdivisions	\$ 10,652	\$ (103)	\$ —	\$ —	\$ 10,652	\$ (103)
MBS/CMO	19,631	(25)	—	—	19,631	(25)
US Gov't Sponsored Entities & Agencies	59,054	(198)	—	—	59,054	(198)
Total	<u>\$ 89,337</u>	<u>\$ (326)</u>	<u>\$ —</u>	<u>\$ —</u>	<u>\$ 89,337</u>	<u>\$ (326)</u>

Available-for-sale debt securities in unrealized loss positions are evaluated for impairment related to credit losses at least quarterly. For available-for-sale debt securities in an unrealized loss position, the Company assesses whether we intend to sell, or it is more likely than not that we will be required to sell the security before recovery of its amortized cost basis. If either of the criteria regarding intent or requirement to sell is met, the security's amortized cost basis is reduced to fair value with an allowance. For available-for sale debt securities that do not meet the criteria, the Company evaluates whether the decline in fair value has resulted from credit losses or other factors. In making this assessment, management considers the extent to which fair value is less than amortized cost, any changes to the rating of the security by a rating agency, and adverse conditions specifically related to the security and the issuer, among other factors. If this assessment indicates that a credit loss exists, we compare the present value of cash flows expected to be collected from the security with the amortized cost basis of the security. If the present value of cash flows expected to be collected is less than the amortized cost basis for the security, a credit loss exists and an allowance for credit losses is recorded, limited to the amount that the fair value of the security is less than its amortized cost basis. Any impairment that has not been recorded through an allowance for credit losses is recognized in other comprehensive income, net of applicable taxes. No allowance for credit losses for available-for-sale debt securities was needed at September 30, 2021 or December 31, 2020. Accrued interest receivable on available-for-sale debt securities totaled \$8,143 at September 30, 2021 and \$5,954 at December 31, 2020. Accrued interest receivable is excluded from the estimate of credit losses.

The Company's equity securities are listed as Other Investments on the Consolidated Balance Sheets and consist of one non-controlling investment in a single banking organization at September 30, 2021 and December 31, 2020. The original investment totaled \$1,350 and other-than-temporary impairment was previously recorded totaling \$997. The Company's equity securities are considered not to have readily determinable fair value and are carried at cost and evaluated for impairment. At September 30, 2021, there was no additional impairment recognized through earnings.

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NOTE 5 – Derivatives

The Company executes interest rate swaps with commercial banking customers to facilitate their respective risk management strategies. The notional amounts of these interest rate swaps and the offsetting counterparty derivative instruments were \$134,130 at September 30, 2021 and \$117,621 at December 31, 2020. These interest rate swaps are simultaneously hedged by offsetting interest rate swaps that the Company executes with a third party, such that the Company minimizes its net risk exposure resulting from such transactions with approved, reputable, independent counterparties with substantially matching terms. The agreements are considered stand-alone derivatives and changes in the fair value of derivatives are reported in earnings as non-interest income.

Credit risk arises from the possible inability of counterparties to meet the terms of their contracts. The Company's exposure is limited to the replacement value of the contracts rather than the notional, principal or contract amounts. There are provisions in the agreements with the counterparties that allow for certain unsecured credit exposure up to an agreed threshold. Exposures in excess of the agreed thresholds are collateralized. In addition, the Company minimizes credit risk through credit approvals, limits, and monitoring procedures.

The following table reflects the fair value hedges included in the Consolidated Balance Sheets as of:

	September 30, 2021		December 31, 2020	
	Notional Amount	Fair Value	Notional Amount	Fair Value
Included in Other Assets:				
Interest Rate Swaps	\$ 134,130	\$ 5,741	\$ 117,621	\$ 8,806
Included in Other Liabilities:				
Interest Rate Swaps	\$ 134,130	\$ 5,997	\$ 117,621	\$ 9,353

The following table presents the effect of derivative instruments on the Consolidated Statements of Income for the periods presented:

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2021	2020	2021	2020
Interest Rate Swaps:				
Included in Other Operating Income	\$ 179	\$ 64	\$ 675	\$ (169)

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NOTE 6 – Loans

Loans were comprised of the following classifications:

	September 30, 2021	December 31, 2020
Commercial:		
Commercial and Industrial Loans	\$ 510,583	\$ 638,773
Commercial Real Estate Loans	1,528,493	1,467,397
Agricultural Loans	349,321	376,186
Leases	56,186	55,664
Retail:		
Home Equity Loans	217,994	219,348
Consumer Loans	67,150	66,717
Credit Cards	13,856	11,637
Residential Mortgage Loans	269,406	256,276
Subtotal	3,012,989	3,091,998
Less: Unearned Income	(3,729)	(3,926)
Allowance for Credit Losses	(37,798)	(46,859)
Loans, net	<u>\$ 2,971,462</u>	<u>\$ 3,041,213</u>

As previously disclosed, the Coronavirus Aid, Relief and Economic Security Act (the “CARES Act”) was signed into law in March 2020, providing an approximately \$2 trillion stimulus package that included direct payments to individual taxpayers, economic stimulus to significantly impacted industry sectors, emergency funding for hospitals and providers, small business loans, increased unemployment benefits, and a variety of tax incentives. For small businesses, eligible nonprofits and certain others, the CARES Act established a Paycheck Protection Program (“PPP”), a lending program administered by the Small Business Administration (“SBA”) that is intended to incentivize participants to retain their employees by providing them with loans that are fully guaranteed by the U.S. government and subject to forgiveness if program guidelines are met. The PPP was later extended and modified by the Paycheck Protection Program and Health Care Enhancement Act in April 2020 and the Paycheck Protection Program Flexibility Act in June 2020, with PPP funding under this initial round expiring on August 8, 2020.

In December 2020, the Economic Aid to Hard-Hit Small Businesses, Nonprofits, and Venues Act was signed into law as part of the Consolidated Appropriations Act, 2021 (the “CAA”). In addition to direct stimulus payments and other aid, this Act provided for a second round of PPP loans through March 31, 2021. Under the American Rescue Plan Act of 2021 and the PPP Extension Act of 2021, which were both enacted during March 2021, additional funds were provided for the program and the deadline for applying for PPP loans was extended through May 31, 2021 (with the SBA given until June 30, 2021 to process loan applications).

The Company actively participated in both rounds of the PPP, lending funds primarily to its existing loan and/or deposit customers. The PPP loans carry an interest rate of 1.00% and included a processing fee that varied depending on the balance of the loan at origination (which fee is recognized over the life of the loan). The vast majority of the Company’s PPP loans made during 2020 had two-year maturities, while PPP loans made during 2021 have five-year maturities.

Under the first round of the PPP (i.e., the 2020 round), the Company originated loans totaling approximately \$351,260 in principal amount, with approximately \$12,024 of related net processing fees on 3,070 PPP loan relationships. As of September 30, 2021, \$347,556 of those first round PPP loans had been forgiven by the SBA and repaid to the Company pursuant to the terms of the program, with \$11,997 in net processing fees having been recognized by the Company.

Under the second round of the PPP (i.e., the 2021 round), the Company originated loans totaling approximately \$157,042 in principal amount, with approximately \$9,022 of related net processing fees, on 2,601 PPP loan relationships. As of September

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NOTE 6 - Loans (continued)

30, 2021, \$89,524 of second round PPP loans had been forgiven by the SBA and repaid to the Company, with \$5,873 in net processing fees having been recognized by the Company. As a result of the forgiveness of the first and second round PPP loans, \$71,222 of total PPP loans remain outstanding as of September 30, 2021, with approximately \$3,175 of net fees remaining deferred on that date.

Allowance for Credit Losses for Loans

The following tables present the activity in the allowance for credit losses by portfolio segment for the three months ended September 30, 2021 and 2020:

September 30, 2021	Commercial and Industrial Loans	Commercial Real Estate Loans	Agricultural Loans	Leases	Consumer Loans	Home Equity Loans	Credit Cards	Residential Mortgage Loans	Unallocated	Total
Allowance for Credit Losses:										
Beginning balance	\$ 6,080	\$ 24,220	\$ 5,847	\$ 204	\$ 460	\$ 908	\$ 181	\$ 2,095	\$ —	\$ 39,995
Provision (Benefit) for credit loss expense	1,965	(2,833)	(1,152)	(1)	167	124	19	(289)	—	(2,000)
Loans charged-off	—	—	—	—	(204)	(15)	(16)	(44)	—	(279)
Recoveries collected	9	5	—	—	60	—	8	—	—	82
Total ending allowance balance	<u>\$ 8,054</u>	<u>\$ 21,392</u>	<u>\$ 4,695</u>	<u>\$ 203</u>	<u>\$ 483</u>	<u>\$ 1,017</u>	<u>\$ 192</u>	<u>\$ 1,762</u>	<u>\$ —</u>	<u>\$ 37,798</u>

September 30, 2020	Commercial and Industrial Loans	Commercial Real Estate Loans	Agricultural Loans	Leases	Consumer Loans	Home Equity Loans	Credit Cards	Residential Mortgage Loans	Unallocated	Total
Allowance for Credit Losses:										
Beginning balance	\$ 8,787	\$ 22,369	\$ 7,030	\$ 202	\$ 496	\$ 1,062	\$ 125	\$ 2,360	\$ —	\$ 42,431
Provision (Benefit) for credit loss expense	(1,017)	5,931	(315)	4	70	—	39	(212)	—	4,500
Loans charged-off	(73)	(9)	—	—	(138)	(67)	(27)	(8)	—	(322)
Recoveries collected	3	91	—	—	64	—	—	1	—	159
Total ending allowance balance	<u>\$ 7,700</u>	<u>\$ 28,382</u>	<u>\$ 6,715</u>	<u>\$ 206</u>	<u>\$ 492</u>	<u>\$ 995</u>	<u>\$ 137</u>	<u>\$ 2,141</u>	<u>\$ —</u>	<u>\$ 46,768</u>

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NOTE 6 - Loans (continued)

The following tables present the activity in the allowance for credit losses by portfolio segment for the nine months ended September 30, 2021 and 2020:

September 30, 2021	Commercial and Industrial Loans	Commercial Real Estate Loans	Agricultural Loans	Leases	Consumer Loans	Home Equity Loans	Credit Cards	Residential Mortgage Loans	Unallocated	Total
Allowance for Credit Losses:										
Beginning balance	\$ 6,445	\$ 29,878	\$ 6,756	\$ 200	\$ 490	\$ 996	\$ 150	\$ 1,944	\$ —	\$ 46,859
Provision (Benefit) for credit loss expense	1,747	(8,502)	(2,061)	3	234	30	186	(137)	—	(8,500)
Loans charged-off	(190)	(10)	—	—	(472)	(15)	(158)	(47)	—	(892)
Recoveries collected	52	26	—	—	231	6	14	2	—	331
Total ending allowance balance	<u>\$ 8,054</u>	<u>\$ 21,392</u>	<u>\$ 4,695</u>	<u>\$ 203</u>	<u>\$ 483</u>	<u>\$ 1,017</u>	<u>\$ 192</u>	<u>\$ 1,762</u>	<u>\$ —</u>	<u>\$ 37,798</u>

September 30, 2020	Commercial and Industrial Loans	Commercial Real Estate Loans	Agricultural Loans	Leases	Consumer Loans	Home Equity Loans	Credit Cards	Residential Mortgage Loans	Unallocated	Total
Allowance for Credit Losses:										
Beginning balance prior to adoption of ASC 326	\$ 4,799	\$ 4,692	\$ 5,315	\$ —	\$ 434	\$ 200	\$ —	\$ 333	\$ 505	\$ 16,278
Impact of adopting ASC 326	2,245	3,063	1,438	105	(59)	762	124	1,594	(505)	8,767
Impact of adopting ASC 326 - PCD Loans	2,191	4,385	128	—	—	35	—	147	—	6,886
Provision (Benefit) for credit loss expense	(1,182)	16,145	(166)	101	385	65	98	104	—	15,550
Initial allowance on loans purchased with credit deterioration	—	—	—	—	—	—	—	—	—	—
Loans charged-off	(369)	(9)	—	—	(520)	(67)	(86)	(39)	—	(1,090)
Recoveries collected	16	106	—	—	252	—	1	2	—	377
Total ending allowance balance	<u>\$ 7,700</u>	<u>\$ 28,382</u>	<u>\$ 6,715</u>	<u>\$ 206</u>	<u>\$ 492</u>	<u>\$ 995</u>	<u>\$ 137</u>	<u>\$ 2,141</u>	<u>\$ —</u>	<u>\$ 46,768</u>

The Company utilizes the Static Pool methodology in determining expected future credit losses. Static pool analysis means segmenting and tracking loans over a period of time based on similar risk characteristics such as loan structure, collateral type, industry of borrower and concentrations, contractual terms and credit risk indicators. Static pool calculates a loss rate on a closed pool of loans that existed on a specified start date based upon the remaining life of each segment.

The Company's expected loss estimate is anchored in historical credit loss experience, with an emphasis on all available portfolio data. The Company's historical look-back period includes January 2014 through the current period, on a monthly basis.

Qualitative reserves reflect management's overall estimate of the extent to which current expected credit losses on collectively evaluated loans will differ from historical loss experience. The analysis takes into consideration industry and collateral concentrations, acquired loan portfolio characteristics and other credit-related analytics as deemed appropriate. Management attempts to quantify qualitative reserves whenever possible.

The Company estimates the allowance balance using relevant available information, from internal and external sources, relating to past events, current conditions, and reasonable and supportable forecasts. Historical loss experience provides the basis for the estimation of expected credit losses. Adjustments to historical loss information are made for changes in underwriting standards, portfolio mix, delinquency level, changes in environmental conditions, unemployment rates, risk classifications and collateral values. The allowance for credit losses is measured on a collective (pooled) basis when similar risk characteristics exist. Based on the potential increased losses related to the economic impact of the COVID-19 pandemic, the bank has

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NOTE 6 - Loans (continued)

considered this loss experience may align with loss experience from the recessionary period from 2008-2011 and qualitative adjustments have been made accordingly.

Loans that do not share risk characteristics are evaluated on an individual basis. Loans evaluated individually are not included in the collective evaluation. When the borrower is experiencing financial difficulty at the reporting date and repayment is expected to be provided substantially through the operation or sale of the collateral, expected credit losses are based on the fair value of the collateral at the reporting date adjusted for selling costs.

For the nine months ended September 30, 2021, the allowance for credit losses decreased primarily due to a decline in individually analyzed loans as well as a decline in the reserve attributable to pandemic-related stressed sectors. While there continues to be great uncertainty related to COVID-19 on our borrowers and communities, we have recognized improvements in employment and gross domestic product which are key indicators utilized in our forecasting for our allowance calculations. The impact of fiscal stimulus, including direct payments to individuals, ongoing increased unemployment benefits, as well as the various government-sponsored loan programs, was also considered in our qualitative adjustments. Since PPP loans are guaranteed by the Small Business Administration (SBA), they have minimal impact on the allowance for credit losses.

All classes of loans, including loans acquired with deteriorated credit quality, are generally placed on non-accrual status when scheduled principal or interest payments are past due for 90 days or more or when the borrower's ability to repay becomes doubtful. For purchased loans, the determination is made at the time of acquisition as well as over the life of the loan. Uncollected accrued interest for each class of loans is reversed against income at the time a loan is placed on non-accrual. Interest received on such loans is accounted for on the cash-basis or cost-recovery method, until qualifying for return to accrual. All classes of loans are returned to accrual status when all the principal and interest amounts contractually due are brought current and future payments are reasonably assured. Loans are typically charged-off at 180 days past due, or earlier if deemed uncollectible. Exceptions to the non-accrual and charge-off policies are made when the loan is well secured and in the process of collection.

The following tables present the amortized cost in non-accrual loans and loans past due over 89 days still accruing by class of loans as of September 30, 2021 and December 31, 2020:

September 30, 2021	Non-Accrual With No Allowance for Credit Loss ⁽¹⁾	Total Non-Accrual	Loans Past Due Over 89 Days Still Accruing
Commercial and Industrial Loans	\$ 4,283	\$ 13,852	\$ —
Commercial Real Estate Loans	50	2,766	—
Agricultural Loans	1,073	1,174	—
Leases	—	—	—
Home Equity Loans	22	22	—
Consumer Loans	16	16	—
Credit Cards	62	62	—
Residential Mortgage Loans	542	542	—
Total	\$ 6,048	\$ 18,434	\$ —

⁽¹⁾ Non-accrual loans with no allowance for credit loss and are also included in Total Non-Accrual loans of \$18,434.

Interest income on non-accrual loans recognized during the three and nine months ended September 30, 2021 totaled \$39 and \$71, respectively.

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NOTE 6 - Loans (continued)

December 31, 2020	Non-Accrual With No Allowance for Credit Loss ⁽¹⁾	Total Non-Accrual	Loans Past Due Over 89 Days Still Accruing
Commercial and Industrial Loans	\$ 4,571	\$ 8,133	\$ —
Commercial Real Estate Loans	3,152	10,188	—
Agricultural Loans	1,291	1,915	—
Leases	—	—	—
Home Equity Loans	271	271	—
Consumer Loans	77	84	—
Credit Cards	86	86	—
Residential Mortgage Loans	671	830	—
Total	\$ 10,119	\$ 21,507	\$ —

⁽¹⁾ Includes non-accrual loans with no allowance for credit loss and are also included in Total Non-Accrual loans of \$21,507.

Interest income on non-accrual loans recognized during the three and nine months ended September 30, 2020 totaled \$1 and \$17, respectively.

The following tables present the amortized cost basis of collateral-dependent loans by class of loans as of September 30, 2021 and December 31, 2020:

September 30, 2021	Real Estate	Equipment	Accounts Receivable	Other	Total
Commercial and Industrial Loans	\$ 2,618	\$ 2,487	\$ 579	\$ 8,719	\$ 14,403
Commercial Real Estate Loans	5,170	—	—	25	5,195
Agricultural Loans	1,560	—	—	—	1,560
Leases	—	—	—	—	—
Home Equity Loans	412	—	—	—	412
Consumer Loans	5	—	—	—	5
Credit Cards	—	—	—	—	—
Residential Mortgage Loans	664	—	—	—	664
Total	\$ 10,429	\$ 2,487	\$ 579	\$ 8,744	\$ 22,239

December 31, 2020	Real Estate	Equipment	Accounts Receivable	Other	Total
Commercial and Industrial Loans	\$ 4,943	\$ 3,014	\$ 669	\$ 154	\$ 8,780
Commercial Real Estate Loans	11,877	—	—	1,530	13,407
Agricultural Loans	3,064	—	—	—	3,064
Leases	—	—	—	—	—
Home Equity Loans	416	—	—	—	416
Consumer Loans	4	4	—	3	11
Credit Cards	—	—	—	—	—
Residential Mortgage Loans	817	—	—	—	817
Total	\$ 21,121	\$ 3,018	\$ 669	\$ 1,687	\$ 26,495

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NOTE 6 - Loans (continued)

The following tables present the aging of the amortized cost basis in past due loans by class of loans as of September 30, 2021 and December 31, 2020:

September 30, 2021	30-59 Days Past Due	60-89 Days Past Due	Greater Than 89 Days Past Due	Total Past Due	Loans Not Past Due	Total
Commercial and Industrial Loans	\$ 98	\$ —	\$ 438	\$ 536	\$ 510,047	\$ 510,583
Commercial Real Estate Loans	—	6	1,232	1,238	1,527,255	1,528,493
Agricultural Loans	—	—	—	—	349,321	349,321
Leases	—	—	—	—	56,186	56,186
Home Equity Loans	222	111	23	356	217,638	217,994
Consumer Loans	136	32	—	168	66,982	67,150
Credit Cards	31	15	62	108	13,748	13,856
Residential Mortgage Loans	2,619	504	327	3,450	265,956	269,406
Total	<u>\$ 3,106</u>	<u>\$ 668</u>	<u>\$ 2,082</u>	<u>\$ 5,856</u>	<u>\$ 3,007,133</u>	<u>\$ 3,012,989</u>

December 31, 2020	30-59 Days Past Due	60-89 Days Past Due	Greater Than 89 Days Past Due	Total Past Due	Loans Not Past Due	Total
Commercial and Industrial Loans	\$ 477	\$ 909	\$ 2,441	\$ 3,827	\$ 634,946	\$ 638,773
Commercial Real Estate Loans	5	4,877	3,682	8,564	1,458,833	1,467,397
Agricultural Loans	—	—	651	651	375,535	376,186
Leases	—	—	—	—	55,664	55,664
Home Equity Loans	672	5	271	948	218,400	219,348
Consumer Loans	233	84	65	382	66,335	66,717
Credit Cards	95	80	86	261	11,376	11,637
Residential Mortgage Loans	3,737	1,590	529	5,856	250,420	256,276
Total	<u>\$ 5,219</u>	<u>\$ 7,545</u>	<u>\$ 7,725</u>	<u>\$ 20,489</u>	<u>\$ 3,071,509</u>	<u>\$ 3,091,998</u>

Troubled Debt Restructurings:

In certain instances, the Company may choose to restructure the contractual terms of loans. A troubled debt restructuring occurs when the Bank grants a concession to the borrower that it would not otherwise consider due to a borrower's financial difficulty. In order to determine whether a borrower is experiencing financial difficulty, an evaluation is performed of the probability that the borrower will be in payment default on any of its debt in the foreseeable future without modification. This evaluation is performed under the Company's internal underwriting policy. The Company uses the same methodology for loans acquired with deteriorated credit quality as for all other loans when determining whether the loan is a troubled debt restructuring.

As of September 30, 2021, the Company had troubled debt restructurings totaling \$106. The Company had no specific allocation of allowance for these loans at September 30, 2021. As of December 31, 2020, the Company had troubled debt restructurings totaling \$111. The Company had no specific allocation of allowance for these loans at December 31, 2020.

The Company had not committed to lending any additional amounts as of September 30, 2021 and December 31, 2020 to customers with outstanding loans that are classified as troubled debt restructurings.

For the three and nine months ended September 30, 2021 and 2020, the Company had no loans modified as troubled debt restructurings. Additionally, there were no loans modified as troubled debt restructurings for which there was a payment default within twelve months following the modification during the three and nine months ended September 30, 2021 and 2020.

A loan is considered to be in payment default once it is 30 days contractually past due under the modified terms.

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NOTE 6 - Loans (continued)

Loan Modifications and Troubled Debt Restructurings due to COVID-19

On April 7, 2020, the federal banking regulators issued a revised Interagency Statement on Loan Modifications and Reporting for Financial Institutions, which, among other things, encouraged financial institutions to work prudently with borrowers who are or may be unable to meet their contractual payment obligations because of the effects of COVID-19, and stated that institutions generally do not need to categorize COVID-19-related modifications as troubled debt restructurings and that the agencies will not direct supervised institutions to automatically categorize all COVID-19 related loan modifications as troubled debt restructurings. Similarly, under the CARES Act, provisions were included that allow for loan modifications to not be classified as TDRs if certain criteria are met. This TDR exemption, which was set to expire on December 31, 2020, was extended under the CAA to, effectively, January 1, 2022.

Credit Quality Indicators:

The Company categorizes loans into risk categories based on relevant information about the ability of borrowers to service their debt such as: current financial information, historical payment experience, credit documentation, public information, and current economic trends, among other factors. The Company classifies loans as to credit risk by individually analyzing loans. This analysis includes commercial and industrial loans, commercial real estate loans, and agricultural loans with an outstanding balance greater than \$250. This analysis is typically performed on at least an annual basis. The Company uses the following definitions for risk ratings:

Special Mention. Loans classified as special mention have a potential weakness that deserves management's close attention. If left uncorrected, these potential weaknesses may result in deterioration of the repayment prospects for the loan or of the institution's credit position at some future date.

Substandard. Loans classified as substandard are inadequately protected by the current net worth and paying capacity of the obligor or of the collateral pledged, if any. Loans so classified have a well-defined weakness or weaknesses that jeopardize the liquidation of the debt. They are characterized by the distinct possibility that the institution will sustain some loss if the deficiencies are not corrected.

Doubtful. Loans classified as doubtful have all the weaknesses inherent in those classified as substandard, with the added characteristic that the weaknesses make collection or liquidation in full, on the basis of currently existing facts, conditions, and values, highly questionable and improbable.

Loans not meeting the criteria above that are analyzed individually as part of the above described process are considered to be pass rated loans.

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NOTE 6 - Loans (continued)

Based on the analysis performed at September 30, 2021 and December 31, 2020, the risk category of loans by class of loans is as follows:

Term Loans Amortized Cost Basis by Origination Year								
As of September 30, 2021	2021	2020	2019	2018	2017	Prior	Revolving Loans Amortized Cost Basis	Total
Commercial and Industrial:								
Risk Rating								
Pass	\$ 149,411	\$ 64,297	\$ 67,633	\$ 32,264	\$ 18,335	\$ 51,778	\$ 101,684	\$ 485,402
Special Mention	616	25	246	806	1,236	1,844	2,750	7,523
Substandard	600	543	455	1,583	1,401	3,099	9,977	17,658
Doubtful	—	—	—	—	—	—	—	—
Total Commercial & Industrial Loans	<u>\$ 150,627</u>	<u>\$ 64,865</u>	<u>\$ 68,334</u>	<u>\$ 34,653</u>	<u>\$ 20,972</u>	<u>\$ 56,721</u>	<u>\$ 114,411</u>	<u>\$ 510,583</u>
Commercial Real Estate:								
Risk Rating								
Pass	\$ 328,394	\$ 271,691	\$ 179,773	\$ 146,504	\$ 147,663	\$ 361,853	\$ 18,524	\$ 1,454,402
Special Mention	2,440	42	755	14,876	22,585	16,149	—	56,847
Substandard	74	—	7,688	1,568	—	7,814	100	17,244
Doubtful	—	—	—	—	—	—	—	—
Total Commercial Real Estate Loans	<u>\$ 330,908</u>	<u>\$ 271,733</u>	<u>\$ 188,216</u>	<u>\$ 162,948</u>	<u>\$ 170,248</u>	<u>\$ 385,816</u>	<u>\$ 18,624</u>	<u>\$ 1,528,493</u>
Agricultural:								
Risk Rating								
Pass	\$ 36,115	\$ 46,365	\$ 24,474	\$ 25,349	\$ 25,461	\$ 73,419	\$ 70,038	\$ 301,221
Special Mention	1,654	5,666	4,292	3,146	6,473	7,512	8,249	36,992
Substandard	—	—	66	385	1,080	9,347	230	11,108
Doubtful	—	—	—	—	—	—	—	—
Total Agricultural Loans	<u>\$ 37,769</u>	<u>\$ 52,031</u>	<u>\$ 28,832</u>	<u>\$ 28,880</u>	<u>\$ 33,014</u>	<u>\$ 90,278</u>	<u>\$ 78,517</u>	<u>\$ 349,321</u>
Leases:								
Risk Rating								
Pass	\$ 15,307	\$ 13,689	\$ 14,794	\$ 6,774	\$ 3,274	\$ 2,348	\$ —	\$ 56,186
Special Mention	—	—	—	—	—	—	—	—
Substandard	—	—	—	—	—	—	—	—
Doubtful	—	—	—	—	—	—	—	—
Total Leases	<u>\$ 15,307</u>	<u>\$ 13,689</u>	<u>\$ 14,794</u>	<u>\$ 6,774</u>	<u>\$ 3,274</u>	<u>\$ 2,348</u>	<u>\$ —</u>	<u>\$ 56,186</u>

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NOTE 6 - Loans (continued)

Term Loans Amortized Cost Basis by Origination Year								
As of December 31, 2020	2020	2019	2018	2017	2016	Prior	Revolving Loans Amortized Cost Basis	Total
Commercial and Industrial:								
Risk Rating								
Pass	\$ 260,027	\$ 88,273	\$ 46,681	\$ 31,612	\$ 21,025	\$ 48,508	\$ 109,228	\$ 605,354
Special Mention	618	1,102	2,756	1,739	206	1,972	9,948	18,341
Substandard	143	164	1,283	1,530	607	5,416	5,935	15,078
Doubtful	—	—	—	—	—	—	—	—
Total Commercial & Industrial Loans	<u>\$ 260,788</u>	<u>\$ 89,539</u>	<u>\$ 50,720</u>	<u>\$ 34,881</u>	<u>\$ 21,838</u>	<u>\$ 55,896</u>	<u>\$ 125,111</u>	<u>\$ 638,773</u>
Commercial Real Estate:								
Risk Rating								
Pass	\$ 296,265	\$ 215,226	\$ 179,129	\$ 183,703	\$ 171,016	\$ 295,641	\$ 29,634	\$ 1,370,614
Special Mention	883	9,361	15,232	23,489	7,578	20,294	147	76,984
Substandard	—	1,131	1,735	1,692	4,292	10,849	100	19,799
Doubtful	—	—	—	—	—	—	—	—
Total Commercial Real Estate Loans	<u>\$ 297,148</u>	<u>\$ 225,718</u>	<u>\$ 196,096</u>	<u>\$ 208,884</u>	<u>\$ 182,886</u>	<u>\$ 326,784</u>	<u>\$ 29,881</u>	<u>\$ 1,467,397</u>
Agricultural:								
Risk Rating								
Pass	\$ 49,242	\$ 25,449	\$ 31,285	\$ 32,368	\$ 22,702	\$ 64,890	\$ 75,871	\$ 301,807
Special Mention	11,503	9,911	3,111	8,767	2,707	10,125	16,318	62,442
Substandard	578	73	394	1,228	4,466	5,198	—	11,937
Doubtful	—	—	—	—	—	—	—	—
Total Agricultural Loans	<u>\$ 61,323</u>	<u>\$ 35,433</u>	<u>\$ 34,790</u>	<u>\$ 42,363</u>	<u>\$ 29,875</u>	<u>\$ 80,213</u>	<u>\$ 92,189</u>	<u>\$ 376,186</u>
Leases:								
Risk Rating								
Pass	\$ 18,258	\$ 17,517	\$ 9,176	\$ 5,415	\$ 1,605	\$ 3,693	\$ —	\$ 55,664
Special Mention	—	—	—	—	—	—	—	—
Substandard	—	—	—	—	—	—	—	—
Doubtful	—	—	—	—	—	—	—	—
Total Leases	<u>\$ 18,258</u>	<u>\$ 17,517</u>	<u>\$ 9,176</u>	<u>\$ 5,415</u>	<u>\$ 1,605</u>	<u>\$ 3,693</u>	<u>\$ —</u>	<u>\$ 55,664</u>

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NOTE 6 - Loans (continued)

The Company considers the performance of the loan portfolio and its impact on the allowance for credit losses. For residential and consumer loan classes, the Company also evaluates credit quality based on the aging status of the loan, which was previously presented, and by payment activity. The following tables present the amortized cost in residential, home equity and consumer loans based on payment activity.

	Term Loans Amortized Cost Basis by Origination Year						Revolving Loans Amortized Cost Basis	Total
As of September 30, 2021	2021	2020	2019	2018	2017	Prior		
Consumer:								
Payment performance								
Performing	\$ 31,330	\$ 19,007	\$ 5,614	\$ 5,201	\$ 880	\$ 1,944	\$ 3,158	\$ 67,134
Nonperforming	—	—	—	—	—	16	—	16
Total Consumer Loans	<u>\$ 31,330</u>	<u>\$ 19,007</u>	<u>\$ 5,614</u>	<u>\$ 5,201</u>	<u>\$ 880</u>	<u>\$ 1,960</u>	<u>\$ 3,158</u>	<u>\$ 67,150</u>
Home Equity:								
Payment performance								
Performing	\$ —	\$ 28	\$ —	\$ 21	\$ 45	\$ 920	\$ 216,957	\$ 217,971
Nonperforming	—	—	—	—	—	1	22	23
Total Home Equity Loans	<u>\$ —</u>	<u>\$ 28</u>	<u>\$ —</u>	<u>\$ 21</u>	<u>\$ 45</u>	<u>\$ 921</u>	<u>\$ 216,979</u>	<u>\$ 217,994</u>
Residential Mortgage:								
Payment performance								
Performing	\$ 76,533	\$ 41,468	\$ 15,892	\$ 18,773	\$ 21,480	\$ 94,721	\$ —	\$ 268,867
Nonperforming	—	—	—	—	—	539	—	539
Total Residential Mortgage Loans	<u>\$ 76,533</u>	<u>\$ 41,468</u>	<u>\$ 15,892</u>	<u>\$ 18,773</u>	<u>\$ 21,480</u>	<u>\$ 95,260</u>	<u>\$ —</u>	<u>\$ 269,406</u>

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NOTE 6 - Loans (continued)

Term Loans Amortized Cost Basis by Origination Year								
As of December 31, 2020	2020	2019	2018	2017	2016	Prior	Revolving Loans Amortized Cost Basis	Total
Consumer:								
Payment performance								
Performing	\$ 33,857	\$ 16,486	\$ 8,456	\$ 2,115	\$ 910	\$ 2,245	\$ 2,563	\$ 66,632
Nonperforming	—	—	11	2	14	23	35	85
Total Consumer Loans	<u>\$ 33,857</u>	<u>\$ 16,486</u>	<u>\$ 8,467</u>	<u>\$ 2,117</u>	<u>\$ 924</u>	<u>\$ 2,268</u>	<u>\$ 2,598</u>	<u>\$ 66,717</u>
Home Equity:								
Payment performance								
Performing	\$ —	\$ —	\$ 34	\$ 46	\$ 67	\$ 490	\$ 218,440	\$ 219,077
Nonperforming	—	—	—	—	—	—	271	271
Total Home Equity Loans	<u>\$ —</u>	<u>\$ —</u>	<u>\$ 34</u>	<u>\$ 46</u>	<u>\$ 67</u>	<u>\$ 490</u>	<u>\$ 218,711</u>	<u>\$ 219,348</u>
Residential Mortgage:								
Payment performance								
Performing	\$ 45,945	\$ 26,536	\$ 28,050	\$ 28,764	\$ 25,155	\$ 100,998	\$ —	\$ 255,448
Nonperforming	—	—	—	—	—	828	—	828
Total Residential Mortgage Loans	<u>\$ 45,945</u>	<u>\$ 26,536</u>	<u>\$ 28,050</u>	<u>\$ 28,764</u>	<u>\$ 25,155</u>	<u>\$ 101,826</u>	<u>\$ —</u>	<u>\$ 256,276</u>

The Company considers the performance of the loan portfolio and its impact on the allowance for credit loan losses. For certain retail loan classes, the Company also evaluates credit quality based on the aging status of the loan, which was previously presented, and by payment activity. The following table presents the recorded investment in credit cards based on payment activity:

Credit Cards	September 30, 2021	December 31, 2020
Performing	\$ 13,794	\$ 11,551
Nonperforming	62	86
Total	<u>\$ 13,856</u>	<u>\$ 11,637</u>

The following tables present loans purchased and/or sold during the year by portfolio segment:

September 30, 2021	Commercial and Industrial Loans	Commercial Real Estate Loans	Agricultural Loans	Leases	Consumer Loans	Home Equity Loans	Credit Cards	Residential Mortgage Loans	Total
Purchases	\$ —	\$ —	\$ —	\$ —	\$ —	\$ —	\$ —	\$ —	\$ —
Sales	2,273	15,415	111	—	—	—	—	—	17,799
December 31, 2020	Commercial and Industrial Loans	Commercial Real Estate Loans	Agricultural Loans	Leases	Consumer Loans	Home Equity Loans	Credit Cards	Residential Mortgage Loans	Total
Purchases	\$ —	\$ —	\$ —	\$ —	\$ —	\$ —	\$ —	\$ —	\$ —
Sales	—	3,128	—	—	—	—	—	—	3,128

On September 24, 2021, the Company sold two branches which included \$17,799 in loans and \$17,614 in deposits.

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NOTE 7 – Repurchase Agreements Accounted for as Secured Borrowings

Repurchase agreements are short-term borrowings included in FHLB Advances and Other Borrowings and mature overnight and continuously. Repurchase agreements, which were secured by mortgage-backed securities, totaled \$52,591 and \$52,905 as of September 30, 2021 and December 31, 2020, respectively. Risk could arise when the collateral pledged to a repurchase agreement declines in fair value. The Company minimizes risk by consistently monitoring the value of the collateral pledged. At the point in time where the collateral has declined in fair value, the Company is required to provide additional collateral based on the value of the underlying securities.

NOTE 8 – Segment Information

The Company's operations include three primary segments: core banking, wealth management services, and insurance operations. The core banking segment involves attracting deposits from the general public and using such funds to originate consumer, commercial and agricultural, commercial and agricultural real estate, and residential mortgage loans, primarily in the Company's local markets. The core banking segment also involves the sale of residential mortgage loans in the secondary market. The wealth management segment involves providing trust, investment advisory, brokerage and retirement planning services to customers. The insurance segment offers a full range of personal and corporate property and casualty insurance products, primarily in the Company's banking subsidiary's local markets.

The core banking segment is comprised by the Company's banking subsidiary, German American Bank, which operated through 64 banking offices at September 30, 2021. Net interest income from loans and investments funded by deposits and borrowings is the primary revenue for the core-banking segment. The wealth management segment's revenues are comprised primarily of fees generated by the trust operations of the Company's banking subsidiary and by German American Investment Services, Inc. These fees are derived by providing trust, investment advisory, brokerage and retirement planning services to its customers. The insurance segment primarily consists of German American Insurance, Inc., which provides a full line of personal and corporate insurance products. Commissions derived from the sale of insurance products are the primary source of revenue for the insurance segment.

The following segment financial information has been derived from the internal financial statements of the Company which are used by management to monitor and manage financial performance. The accounting policies of the three segments are the same as those of the Company. The evaluation process for segments does not include holding company income and expense. Holding company amounts are the primary differences between segment amounts and consolidated totals, and are reflected in the column labeled "Other" below, along with amounts to eliminate transactions between segments.

	Core Banking	Wealth Management Services	Insurance	Other	Consolidated Totals
Three Months Ended					
September 30, 2021					
Net Interest Income	\$ 41,925	\$ 15	\$ 3	\$ (656)	\$ 41,287
Net Gains on Sales of Loans	2,197	—	—	—	2,197
Net Gains on Securities	218	—	—	—	218
Trust and Investment Product Fees	1	2,689	—	—	2,690
Insurance Revenues	2	3	2,002	—	2,007
Noncash Items:					
Provision (Benefit) for Credit Losses	(2,000)	—	—	—	(2,000)
Depreciation and Amortization	2,038	11	13	80	2,142
Income Tax Expense (Benefit)	5,069	233	79	(468)	4,913
Segment Profit (Loss)	21,267	722	250	(753)	21,486
Segment Assets at September 30, 2021	5,465,132	5,819	12,350	(7,551)	5,475,750

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NOTE 8 - Segment Information (continued)

	Core Banking	Wealth Management Services	Insurance	Other	Consolidated Totals
Three Months Ended					
September 30, 2020					
Net Interest Income	\$ 39,039	\$ 4	\$ 2	\$ (657)	\$ 38,388
Net Gains on Sales of Loans	2,861	—	—	—	2,861
Net Gains on Securities	607	—	—	—	607
Trust and Investment Product Fees	2	1,955	—	—	1,957
Insurance Revenues	6	1	1,982	—	1,989
Noncash Items:					
Provision (Benefit) for Credit Losses	4,500	—	—	—	4,500
Depreciation and Amortization	2,237	2	16	80	2,335
Income Tax Expense (Benefit)	3,268	108	71	(293)	3,154
Segment Profit (Loss)	14,628	321	216	(572)	14,593
Segment Assets at December 31, 2020	4,963,655	4,480	10,263	(821)	4,977,577

	Core Banking	Wealth Management Services	Insurance	Other	Consolidated Totals
Nine Months Ended					
September 30, 2021					
Net Interest Income	\$ 122,028	\$ 36	\$ 8	\$ (1,973)	\$ 120,099
Net Gains on Sales of Loans	6,417	—	—	—	6,417
Net Gains on Securities	1,493	—	—	—	1,493
Trust and Investment Product Fees	4	7,664	—	—	7,668
Insurance Revenues	9	6	7,304	—	7,319
Noncash Items:					
Provision (Benefit) for Credit Losses	(8,500)	—	—	—	(8,500)
Depreciation and Amortization	6,403	35	44	241	6,723
Income Tax Expense (Benefit)	15,549	583	575	(1,218)	15,489
Segment Profit (Loss)	63,204	1,811	1,812	(1,962)	64,865
Segment Assets at September 30, 2021	5,465,132	5,819	12,350	(7,551)	5,475,750

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NOTE 8 - Segment Information (continued)

	Core Banking	Wealth Management Services	Insurance	Other	Consolidated Totals
Nine Months Ended					
September 30, 2020					
Net Interest Income	\$ 115,148	\$ 12	\$ 9	\$ (2,066)	\$ 113,103
Net Gains on Sales of Loans	7,378	—	—	—	7,378
Net Gains on Securities	2,190	—	—	—	2,190
Trust and Investment Product Fees	3	5,852	—	—	5,855
Insurance Revenues	11	12	7,025	—	7,048
Noncash Items:					
Provision (Benefit) for Credit Losses	15,550	—	—	—	15,550
Depreciation and Amortization	6,748	4	50	241	7,043
Income Tax Expense (Benefit)	8,635	336	471	(1,262)	8,180
Segment Profit (Loss)	40,573	991	1,437	(1,681)	41,320
Segment Assets at December 31, 2020	4,963,655	4,480	10,263	(821)	4,977,577

NOTE 9 – Stock Repurchase Plan

On January 25, 2021, the Company's Board of Directors approved a plan to repurchase up to one million shares of the Company's outstanding common stock. On a share basis, the amount of common stock subject to the repurchase plan represents approximately 4% of the Company's outstanding shares. The Company is not obligated to purchase shares under the plan, and the plan may be discontinued at any time. The actual timing, number and share price of shares purchased under the repurchase plan will be determined by the Company at its discretion and will depend upon such factors as the market price of the stock, general market and economic conditions and applicable legal requirements. At the time it approved the new plan, the Board also terminated a similar plan that had been adopted in January 2020. At the time of its termination, the Company had been authorized to purchase up to 778,088 shares of common stock under the 2020 repurchase plan. The Company has not repurchased any shares of common stock under the 2021 repurchase plan.

NOTE 10 – Equity Plans and Equity Based Compensation

During the periods presented, the Company maintained two equity incentive plans under which stock options, restricted stock, and other equity incentive awards have been or could be granted. Those plans include (i) the Company's 2009 Long-Term Equity Incentive Plan, under which no new grants may be made, and (ii) the Company's 2019 Long-Term Equity Incentive Plan (the "2019 LTI Plan"). The 2019 LTI Plan, which authorizes a maximum aggregate issuance of 1,000,000 shares of common stock (subject to certain permitted adjustments), became effective on May 16, 2019, following approval of the Company's shareholders. It will remain in effect until May 16, 2029, or until all shares of common stock subject to the 2019 LTI Plan are distributed, all awards have expired or terminated, or the plan is terminated pursuant to its terms, whichever occurs first.

For the three and nine months ended September 30, 2021 and 2020, the Company granted no options. The Company recorded no stock compensation expense applicable to options during the three and nine months ended September 30, 2021 and 2020. In addition, there was no unrecognized option expense.

During the periods presented, awards of long-term incentives were granted in the form of restricted stock. In 2019 and prior, awards that were granted to management and selected other employees under the Company's management incentive plan were granted in tandem with cash credit entitlements in the form of 60% restricted stock grants and 40% cash credit entitlements. In 2020, awards granted under the management incentive plan were granted in tandem with cash credit entitlements in the form of 66.67% restricted stock grants and 33.33% cash credit entitlements. In 2019 and prior, the restricted stock grants and tandem cash credit entitlements, generally, vested in three annual installments of 33.33% each. In 2020, 100% of the cash portion of an award vests towards the end of the year in which the grant was made, followed by the restricted stock grants vesting 50% in each of the 2nd and 3rd years. Beginning in 2021 for named executive officers, awards are granted in the form of 100%

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NOTE 10 - Equity Plans and Equity Based Compensation (continued)

restricted stock grants which will vest in one-third installments on the first, second and third anniversaries of the award date. Awards that are granted to directors as additional retainers for their services do not include any cash credit entitlement. These director restricted stock grants are subject to forfeiture in the event that the recipient of the grant does not continue in service as a director of the Company through December 31 of the year after grant or does not satisfy certain meeting attendance requirements, at which time they generally vest 100 percent. For measuring compensation costs, restricted stock awards are valued based upon the market value of the common shares on the date of grant. During the three and nine months ended September 30, 2021, the Company granted awards of 396 and 44,519 shares of restricted stock, respectfully. During the three and nine months ended September 30, 2020, the Company granted awards of 1,192 and 44,370 shares of restricted stock, respectively. Total unvested restricted stock awards at September 30, 2021 and December 31, 2020 were 99,956 and 64,401, respectively.

The following table presents expense recorded for restricted stock and cash entitlements as well as the related tax information for the periods presented:

	Three Months Ended September 30,	
	2021	2020
Restricted Stock Expense	\$ 355	\$ 254
Cash Entitlement Expense	180	249
Tax Effect	(139)	(125)
Net of Tax	<u>\$ 396</u>	<u>\$ 378</u>
	Nine Months Ended September 30,	
	2021	2020
Restricted Stock Expense	\$ 1,322	\$ 806
Cash Entitlement Expense	547	737
Tax Effect	(485)	(384)
Net of Tax	<u>\$ 1,384</u>	<u>\$ 1,159</u>

Unrecognized expense associated with the restricted stock grants and cash entitlements totaled \$2,753 and \$1,071 as of September 30, 2021 and 2020, respectively.

Through August 16, 2019, the Company maintained the 2009 Employee Stock Purchase Plan (the "2009 ESPP") whereby eligible employees had the option to purchase the Company's common stock at a discount. The purchase price of the shares under this plan was set at 95% of the fair value of the Company's common stock as of the last day of the plan year. The plan had provided for the purchase of up to 750,000 shares of common stock, which the Company may obtain by purchases on the open market or from private sources, or by issuing authorized but unissued common shares.

The Company's shareholders approved the Company's new 2019 Employee Stock Purchase Plan on May 16, 2019, as well as an Amended and Restated 2019 Employee Stock Purchase Plan on May 21, 2020, which was amended and restated to reflect certain clarifying changes (the "2019 ESPP"). The 2019 ESPP replaces the 2009 ESPP, which expired by its own terms on August 16, 2019. The 2019 ESPP, which became effective as of October 1, 2019, provides for a series of 3-month offering periods, commencing on the first day and ending on the last trading day of each calendar quarter, for the purchase of the Company's common stock by participating employees. The purchase price of the shares has been set at 95% of the fair value of the Company's common stock on the last trading day of the offering period. A total of 750,000 common shares has been reserved for issuance under the 2019 ESPP. The 2019 ESPP will continue until September 30, 2029, or, if earlier, until all of the shares of common stock allocated to the 2019 ESPP have been purchased. Funding for the purchase of common stock is from employee and Company contributions.

For the three months ended September 30, 2021, the Company recorded \$14 of expense related to the employee stock purchase plan resulting in \$11 net of tax. For the nine months ended September 30, 2021, the Company recorded \$24 of expense, \$18 net of tax, for the employee stock purchase plan. For the three months ended September 30, 2020, the Company recorded \$11 of expense, \$8 net of tax, for the employee stock purchase plan. For the nine months ended September 30, 2020, the Company

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NOTE 10 - Equity Plans and Equity Based Compensation (continued)

recorded \$30 of expense, \$23 net of tax, for the employee stock purchase plan. There was no unrecognized compensation expense as of September 30, 2021 and 2020 for the employee stock purchase plan.

NOTE 11 – Fair Value

Fair value is the exchange price that would be received for an asset or paid to transfer a liability (exit price) in the principal or most advantageous market for the asset or liability in an orderly transaction between market participants on the measurement date. There are three levels of inputs that may be used to measure fair values:

Level 1: Quoted prices (unadjusted) for identical assets or liabilities in active markets that the entity has the ability to access as of the measurement date.

Level 2: Significant other 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.

Level 3: Significant unobservable inputs that reflect a reporting entity's own assumptions about the assumptions that market participants would use in pricing an asset or liability.

The Company used the following methods and significant assumptions to estimate the fair value of each type of financial instrument:

Investment Securities: The fair values for investment securities are determined by quoted market prices, if available (Level 1). For investment securities where quoted prices are not available, fair values are calculated based on market prices of similar investment securities (Level 2). For investment securities where quoted prices or market prices of similar investment securities are not available, fair values are calculated using discounted cash flows or other market indicators (Level 3). Level 3 pricing is obtained from a third-party based upon similar trades that are not traded frequently without adjustment by the Company. At September 30, 2021, the Company held no Level 3 securities. Absent the credit rating, significant assumptions must be made such that the credit risk input becomes an unobservable input and thus these investment securities are reported by the Company in a Level 3 classification.

Derivatives: The fair values of derivatives are based on valuation models using observable market data as of the measurement date (Level 2).

Individually Analyzed Loans: Fair values for collateral dependent loans are generally based on appraisals obtained from licensed real estate appraisers and in certain circumstances includes consideration of offers obtained to purchase properties prior to foreclosure. Appraisals for commercial real estate generally use three methods to derive value: cost, sales or market comparison and income approach. The cost method bases value in the cost to replace the current property. Value of market comparison approach evaluates the sales price of similar properties in the same market area. The income approach considers net operating income generated by the property and an investor's required return. Adjustments are routinely made in the appraisal process by the independent appraisers to adjust for differences between the comparable sales and income data available. Comparable sales adjustments are based on known sales prices of similar type and similar use properties and duration of time that the property has been on the market to sell. Such adjustments made in the appraisal process are typically significant and result in a Level 3 classification of the inputs for determining fair value.

Appraisals for both collateral-dependent impaired loans and other real estate owned are performed by certified general appraisers (for commercial properties) or certified residential appraisers (for residential properties) whose qualifications and licenses have been reviewed and verified by the Company. Once received, a member of the Company's Risk Management Area reviews the assumptions and approaches utilized in the appraisal. In determining the value of impaired collateral dependent loans and other real estate owned, significant unobservable inputs may be used which include: physical condition of comparable properties sold, net operating income generated by the property and investor rates of return.

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NOTE 11 - Fair Value (continued)

Other Real Estate: Nonrecurring adjustments to certain commercial and residential real estate properties classified as other real estate (ORE) are measured at the lower of carrying amount or fair value, less costs to sell. Fair values are generally based on third party appraisals of the property utilizing similar techniques as discussed above for Impaired Loans, resulting in a Level 3 classification. In cases where the carrying amount exceeds the fair value, less costs to sell, impairment loss is recognized.

Loans Held-for-Sale: The fair values of loans held for sale are determined by using quoted prices for similar assets, adjusted for specific attributes of that loan resulting in a Level 2 classification.

Assets and Liabilities Measured on a Recurring Basis

Assets and liabilities measured at fair value on a recurring basis, including financial assets and liabilities for which the Company has elected the fair value option, are summarized below:

	Fair Value Measurements at September 30, 2021 Using			
	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)	Total
Assets:				
Obligations of State and Political Subdivisions	\$ —	\$ 833,453	\$ —	\$ 833,453
MBS/CMO	—	726,632	—	726,632
US Gov't Sponsored Entities & Agencies	—	136,140	—	136,140
Total Securities	\$ —	\$ 1,696,225	\$ —	\$ 1,696,225
Loans Held-for-Sale	\$ —	\$ 15,361	\$ —	\$ 15,361
Derivative Assets	\$ —	\$ 5,741	\$ —	\$ 5,741
Derivative Liabilities	\$ —	\$ 5,997	\$ —	\$ 5,997

	Fair Value Measurements at December 31, 2020 Using			
	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)	Total
Assets:				
Obligations of State and Political Subdivisions	\$ —	\$ 580,750	\$ 497	\$ 581,247
MBS/CMO	—	548,307	—	548,307
US Gov't Sponsored Entities & Agencies	—	88,298	—	88,298
Total Securities	\$ —	\$ 1,217,355	\$ 497	\$ 1,217,852
Loans Held-for-Sale	\$ —	\$ 16,904	\$ —	\$ 16,904
Derivative Assets	\$ —	\$ 8,806	\$ —	\$ 8,806
Derivative Liabilities	\$ —	\$ 9,353	\$ —	\$ 9,353

As of September 30, 2021 and December 31, 2020, the aggregate fair value, contractual balance (including accrued interest), and gain or loss on Loans Held-for-Sale was as follows:

	September 30, 2021	December 31, 2020
Aggregate Fair Value	\$ 15,361	\$ 16,904
Contractual Balance	14,994	16,378
Gain (Loss)	367	526

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NOTE 11 - Fair Value (continued)

The total amount of gains and losses from changes in fair value included in earnings for the three and nine months ended September 30, 2021 were \$(79) and \$(159), respectively. The total amount of gains and losses from changes in fair value included in earnings for the three and nine months ended September 30, 2020 were \$233 and \$330, respectively.

The table below presents a reconciliation of all assets measured at fair value on a recurring basis using significant unobservable inputs (Level 3) for the three and nine months ended September 30, 2021 and 2020:

	Obligations of State and Political Subdivisions	
	2021	2020
Balance of Recurring Level 3 Assets at July 1	\$ —	\$ 2,495
Total Losses Included in Other Comprehensive Income	—	(3)
Maturities / Calls	—	(1,995)
Purchases	—	—
Balance of Recurring Level 3 Assets at September 30	<u>\$ —</u>	<u>\$ 497</u>

	Obligations of State and Political Subdivisions	
	2021	2020
Balance of Recurring Level 3 Assets at January 1	\$ 497	\$ 4,021
Total Losses Included in Other Comprehensive Income	(2)	(26)
Maturities / Calls	(495)	(3,498)
Purchases	—	—
Balance of Recurring Level 3 Assets at September 30	<u>\$ —</u>	<u>\$ 497</u>

Of the total gain/loss included in earnings for the three months ended September 30, 2021 and 2020, \$0 and \$(3) was attributable to other changes in fair value, respectively. Of the total gain/loss included in earnings for the nine months ended September 30, 2021 and 2020, \$(2) and \$(26) was attributable to other changes in fair value, respectively.

Assets and Liabilities Measured on a Non-Recurring Basis

Assets and liabilities measured at fair value on a non-recurring basis are summarized below:

	Fair Value Measurements at September 30, 2021 Using				
	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)	Total	
Assets:					
Individually Analyzed Loans					
Commercial and Industrial Loans	\$ —	\$ —	\$ 8,710	\$ 8,710	
Commercial Real Estate Loans	\$ —	\$ —	\$ 2,148	\$ 2,148	
Agricultural Loans	\$ —	\$ —	\$ 79	\$ 79	
Consumer Loans	\$ —	\$ —	\$ —	\$ —	
Home Equity Loans	\$ —	\$ —	\$ 345	\$ 345	
Residential Mortgage Loans	\$ —	\$ —	\$ —	\$ —	

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NOTE 11 - Fair Value (continued)

	Fair Value Measurements at December 31, 2020 Using				
	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)	Total	
Assets:					
Individually Analyzed Loans					
Commercial and Industrial Loans	\$ —	\$ —	\$ 4,985	\$ 4,985	
Commercial Real Estate Loans	\$ —	\$ —	\$ 8,893	\$ 8,893	
Agricultural Loans	\$ —	\$ —	\$ 551	\$ 551	
Consumer Loans	\$ —	\$ —	\$ —	\$ —	
Home Equity Loans	\$ —	\$ —	\$ 369	\$ 369	
Residential Mortgage Loans	\$ —	\$ —	\$ 75	\$ 75	

The following tables present quantitative information about Level 3 fair value measurements for financial instruments measured at fair value on a non-recurring basis at September 30, 2021 and December 31, 2020:

September 30, 2021	Fair Value	Valuation Technique(s)	Unobservable Input(s)	Range (Weighted Average)
Individual Analyzed Loans - Commercial and Industrial Loans	\$ 8,710	Sales comparison approach	Adjustment for physical condition of comparable properties sold	30%-100% (55%)
Individual Analyzed Loans - Commercial Real Estate Loans	\$ 2,148	Sales comparison approach	Adjustment for physical condition of comparable properties sold	9%-100% (25%)
Individual Analyzed Loans - Agricultural Loans	\$ 79	Sales comparison approach	Adjustment for physical condition of comparable properties sold	30%-96% (90%)
Individual Analyzed Loans - Consumer Loans	\$ —	Sales comparison approach	Adjustment for physical condition of comparable properties sold	—%—% (—%)
Individual Analyzed Loans - Home Equity Loans	\$ 345	Sales comparison approach	Adjustment for physical condition of comparable properties sold	23%-23% (23%)
Individual Analyzed Loans - Residential Mortgage Loans	\$ —	Sales comparison approach	Adjustment for physical condition of comparable properties sold	—%—% (—%)

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NOTE 11 - Fair Value (continued)

December 31, 2020	Fair Value	Valuation Technique(s)	Unobservable Input(s)	Range (Weighted Average)
Individual Analyzed Loans - Commercial and Industrial Loans	\$ 4,985	Sales comparison approach	Adjustment for physical condition of comparable properties sold	26%-100% (61%)
Individual Analyzed Loans - Commercial Real Estate Loans	\$ 8,893	Sales comparison approach	Adjustment for physical condition of comparable properties sold	30%-100% (56%)
Individual Analyzed Loans - Agricultural Loans	\$ 551	Sales comparison approach	Adjustment for physical condition of comparable properties sold	30%-96% (65%)
Individual Analyzed Loans - Consumer Loans	\$ —	Sales comparison approach	Adjustment for physical condition of comparable properties sold	100% (100%)
Individual Analyzed Loans - Home Equity Loans	\$ 369	Sales comparison approach	Adjustment for physical condition of comparable properties sold	9%-9% (9%)
Individual Analyzed Loans - Residential Mortgage Loans	\$ 75	Sales comparison approach	Adjustment for physical condition of comparable properties sold	43%-97% (67%)

The carrying amounts and estimated fair values of the Company's financial instruments not previously presented are provided in the tables below for the periods ending September 30, 2021 and December 31, 2020. Not all of the Company's assets and liabilities are considered financial instruments, and therefore are not included in the tables. Because no active market exists for a significant portion of the Company's financial instruments, fair value estimates were based on subjective judgments, and therefore cannot be determined with precision.

		Fair Value Measurements at September 30, 2021 Using			
	Carrying Value	Level 1	Level 2	Level 3	Total
Financial Assets:					
Cash and Short-term Investments	\$ 448,743	\$ 54,617	\$ 394,126	\$ —	\$ 448,743
Interest Bearing Time Deposits with Banks	745	—	745	—	745
Loans, Net	2,960,180	—	—	2,962,916	2,962,916
Accrued Interest Receivable	20,002	—	8,362	11,640	20,002
Financial Liabilities:					
Demand, Savings, and Money Market Deposits	(4,215,525)	(4,215,525)	—	—	(4,215,525)
Time Deposits	(377,426)	—	(376,922)	—	(376,922)
Short-term Borrowings	(52,591)	—	(52,591)	—	(52,591)
Long-term Debt	(133,799)	—	(79,221)	(54,144)	(133,365)
Accrued Interest Payable	(1,126)	—	(1,093)	(33)	(1,126)

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NOTE 11 - Fair Value (continued)

	Fair Value Measurements at December 31, 2020 Using				
	Carrying Value	Level 1	Level 2	Level 3	Total
Financial Assets:					
Cash and Short-term Investments	\$ 345,748	\$ 57,972	\$ 287,776	\$ —	\$ 345,748
Interest Bearing Time Deposits with Banks	1,241	—	1,241	—	1,241
Loans, Net	3,026,340	—	—	3,032,690	3,032,690
Accrued Interest Receivable	20,278	—	6,137	14,141	20,278
Financial Liabilities:					
Demand, Savings, and Money Market Deposits	(3,612,078)	(3,612,078)	—	—	(3,612,078)
Time Deposits	(494,452)	—	(495,171)	—	(495,171)
Short-term Borrowings	(52,905)	—	(52,905)	—	(52,905)
Long-term Debt	(141,624)	—	(88,342)	(54,960)	(143,302)
Accrued Interest Payable	(1,084)	—	(1,049)	(35)	(1,084)

NOTE 12 - Other Comprehensive Income (Loss)

The tables below summarize the changes in accumulated other comprehensive income (loss) by component for the three and nine months ended September 30, 2021 and 2020, net of tax:

September 30, 2021	Unrealized Gains and Losses on Available-for- Sale Securities	Postretirement Benefit Items	Total
Beginning Balance at July 1, 2021	\$ 26,993	\$ (568)	\$ 26,425
Other Comprehensive Income (Loss) Before Reclassification	(14,989)	—	(14,989)
Amounts Reclassified from Accumulated Other Comprehensive Income (Loss)	(172)	—	(172)
Net Current Period Other Comprehensive Income (Loss)	(15,161)	—	(15,161)
Ending Balance at September 30, 2021	<u>\$ 11,832</u>	<u>\$ (568)</u>	<u>\$ 11,264</u>

September 30, 2021	Unrealized Gains and Losses on Available-for- Sale Securities	Postretirement Benefit Items	Total
Beginning Balance at January 1, 2021	\$ 35,943	\$ (568)	\$ 35,375
Other Comprehensive Income (Loss) Before Reclassification	(22,932)	—	(22,932)
Amounts Reclassified from Accumulated Other Comprehensive Income (Loss)	(1,179)	—	(1,179)
Net Current Period Other Comprehensive Income (Loss)	(24,111)	—	(24,111)
Ending Balance at September 30, 2021	<u>\$ 11,832</u>	<u>\$ (568)</u>	<u>\$ 11,264</u>

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NOTE 12 - Other Comprehensive Income (Loss) (continued)

September 30, 2020	Unrealized Gains and Losses on Available-for-Sale Securities	Postretirement Benefit Items	Total
Beginning Balance at July 1, 2020	\$ 31,717	\$ (568)	\$ 31,149
Other Comprehensive Income (Loss) Before Reclassification	74	—	74
Amounts Reclassified from Accumulated Other Comprehensive Income (Loss)	(480)	—	(480)
Net Current Period Other Comprehensive Income (Loss)	(406)	—	(406)
Ending Balance at September 30, 2020	<u>\$ 31,311</u>	<u>\$ (568)</u>	<u>\$ 30,743</u>

September 30, 2020	Unrealized Gains and Losses on Available-for-Sale Securities	Postretirement Benefit Items	Total
Beginning Balance at January 1, 2020	\$ 15,673	\$ (568)	\$ 15,105
Other Comprehensive Income (Loss) Before Reclassification	17,364	—	17,364
Amounts Reclassified from Accumulated Other Comprehensive Income (Loss)	(1,726)	—	(1,726)
Net Current Period Other Comprehensive Income (Loss)	15,638	—	15,638
Ending Balance at September 30, 2020	<u>\$ 31,311</u>	<u>\$ (568)</u>	<u>\$ 30,743</u>

The tables below summarize the classifications out of accumulated other comprehensive income (loss) by component for the three and nine months ended September 30, 2021 and 2020:

Details about Accumulated Other Comprehensive Income (Loss) Components	Amount Reclassified From Accumulated Other Comprehensive Income (Loss)	Affected Line Item in the Statement Where Net Income is Presented
Unrealized Gains and Losses on Available-for-Sale Securities	\$ 218	Net Gains on Securities
	(46)	Income Tax Expense
	<u>172</u>	Net of Tax

Total Reclassifications for the Three Months Ended September 30, 2021

\$ 172

Details about Accumulated Other Comprehensive Income (Loss) Components	Amount Reclassified From Accumulated Other Comprehensive Income (Loss)	Affected Line Item in the Statement Where Net Income is Presented
Unrealized Gains and Losses on Available-for-Sale Securities	\$ 1,493	Net Gains on Securities
	(314)	Income Tax Expense
	<u>1,179</u>	Net of Tax

Total Reclassifications for the Nine Months Ended September 30, 2021

\$ 1,179

GERMAN AMERICAN BANCORP, INC.
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NOTE 12 - Other Comprehensive Income (Loss) (continued)

Details about Accumulated Other Comprehensive Income (Loss) Components	Amount Reclassified From Accumulated Other Comprehensive Income (Loss)	Affected Line Item in the Statement Where Net Income is Presented
Unrealized Gains and Losses on Available-for-Sale Securities	\$ 607	Net Gains on Securities
	(127)	Income Tax Expense
	480	Net of Tax
Total Reclassifications for the Three Months Ended September 30, 2020	\$ 480	

Details about Accumulated Other Comprehensive Income (Loss) Components	Amount Reclassified From Accumulated Other Comprehensive Income (Loss)	Affected Line Item in the Statement Where Net Income is Presented
Unrealized Gains and Losses on Available-for-Sale Securities	\$ 2,190	Net Gains on Securities
	(464)	Income Tax Expense
	1,726	Net of Tax
Total Reclassifications for the Nine Months Ended September 30, 2020	\$ 1,726	

NOTE 13 - Revenue Recognition

The following table presents non-interest income, segregated by revenue streams in-scope and out-of-scope of FASB ASU No. 2014-09, Revenue from Contracts with Customers (Topic 606), for the three and nine months ended September 30, 2021 and 2020. Trust and investment product fees are included in the wealth management services segment while insurance revenues are included in the insurance segment. All other revenue streams are primarily included in the banking segment.

	Three Months Ended September 30,	
	2021	2020
Non-interest Income		
In-Scope of Topic 606:		
Trust and Investment Product Fees	\$ 2,690	\$ 1,957
Service Charges on Deposit Accounts	2,017	1,773
Insurance Revenues	2,007	1,989
Interchange Fee Income	3,339	2,795
Other Operating Income	760	653
Non-interest Income (in-scope of Topic 606)	10,813	9,167
Non-interest Income (out-of-scope of Topic 606)	4,743	4,112
Total Non-interest Income	\$ 15,556	\$ 13,279

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NOTE 13 - Revenue Recognition (continued)

	Nine Months Ended	
	September 30,	
	2021	2020
Non-interest Income		
In-Scope of Topic 606:		
Trust and Investment Product Fees	\$ 7,668	\$ 5,855
Service Charges on Deposit Accounts	5,430	5,375
Insurance Revenues	7,319	7,048
Interchange Fee Income	9,651	7,753
Other Operating Income	2,149	1,727
Non-interest Income (in-scope of Topic 606)	32,217	27,758
Non-interest Income (out-of-scope of Topic 606)	12,278	12,025
Total Non-interest Income	\$ 44,495	\$ 39,783

A description of the Company's revenue streams accounted for under Topic 606 follows:

Service Charges on Deposit Accounts: The Company earns fees from its deposit customers for transaction-based, account maintenance, and overdraft services. Transaction-based fees, which include services such as stop payment charges and statement rendering, are recognized at the time the transaction is executed (the point in time the Company fills the customer's request). Account maintenance fees, which relate primarily to monthly maintenance, are earned over the course of a month, representing the period over which the Company satisfies the performance obligation. Overdraft fees are recognized at the point in time that the overdraft occurs.

Interchange Fee Income: The Company earns interchange fees from debit/credit cardholder transactions conducted through various payment networks. Interchange fees from cardholder transactions represent a percentage of the underlying transaction value and are recognized daily, concurrently with the transaction processing services provided to the cardholder.

Trust and Investment Product Fees: The Company earns trust and investment brokerage fees from its contracts with trust and brokerage customers to manage assets for investment and/or to transact their accounts. These fees are primarily earned over time as the Company provides the contracted monthly or quarterly services and are generally assessed based on the market value of assets under management at month-end. Fees that are transaction based, including trade execution services, are recognized at the point in time that the transaction is executed (trade date).

Insurance Revenues: The Company earns insurance revenue from commissions derived from the sale of personal and corporate property and casualty insurance products. These commissions are primarily earned over time as the Company provides the contracted insurance product to customers.

NOTE 14 – Leases

At the inception of a contract, an entity should determine whether the contract contains a lease. Topic 842 defines a lease as a contract, or part of a contract, that conveys the right to control the use of identified property, plant, or equipment (an identified asset) for a period of time in exchange for consideration. Control over the use of an identified asset means that the customer has both (1) the right to obtain substantially all of the economic benefits from the use of the asset and (2) the right to direct the use of the asset.

German American has finance leases for branch offices as well as operating leases for branch offices, ATM locations and certain office equipment. The right-of-use asset is included in the 'Premises, Furniture and Equipment, Net' line of the Consolidated Balance Sheet. The lease liability is included in the 'Accrued Interest Payable and Other Liabilities' line of the Consolidated Balance Sheet.

The Company used the implicit lease rate when determining the present value of lease payments for finance leases. The present value of lease payments for operating leases was determined using the incremental borrowing rate as of the date the Company adopted this standard.

GERMAN AMERICAN BANCORP, INC.
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NOTE 14 - Leases (continued)

The components of lease expense were as follows:

	Three Months Ended	Three Months Ended
	September 30, 2021	September 30, 2020
Finance Lease Cost:		
Amortization of Right-of -Use Assets	\$ 53	\$ 52
Interest on Lease Liabilities	86	91
Operating Lease Cost	331	446
Short-term Lease Cost	36	—
Total Lease Cost	<u>\$ 506</u>	<u>\$ 589</u>
	Nine Months Ended	Nine Months Ended
	September 30, 2021	September 30, 2020
Finance Lease Cost:		
Amortization of Right-of -Use Assets	\$ 157	\$ 157
Interest on Lease Liabilities	261	274
Operating Lease Cost	1,092	1,352
Short-term Lease Cost	43	34
Total Lease Cost	<u>\$ 1,553</u>	<u>\$ 1,817</u>

The weighted average lease term and discount rates were as follows:

	September 30, 2021	September 30, 2020
Weighted Average Remaining Lease Term:		
Finance Leases	10 years	11 years
Operating Leases	7 years	8 years
Weighted Average Discount Rate:		
Finance Leases	11.46 %	11.48 %
Operating Leases	3.04 %	3.18 %

Supplemental balance sheet information related to leases were as follows:

	September 30, 2021	September 30, 2020
Finance Leases		
Premises, Furniture and Equipment, Net	\$ 2,120	\$ 2,330
Other Borrowings	3,096	3,265
Operating Leases		
Operating Lease Right-of-Use Assets	\$ 6,241	\$ 8,579
Operating Lease Liabilities	6,344	8,675

GERMAN AMERICAN BANCORP, INC.
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NOTE 14 - Leases (continued)

Supplemental cash flow information related to leases were as follows:

	Nine Months Ended	Nine Months Ended
	September 30, 2021	September 30, 2020
Cash paid for amounts in the measurement of lease liabilities:		
Operating Cash Flows from Finance Leases	\$ 261	\$ 274
Operating Cash Flows from Operating Leases	2,522	1,292
Financing Cash Flows from Finance Leases	111	92

The following table presents a maturity analysis of Finance and Operating Lease Liabilities:

	September 30, 2021	
	Finance Leases	Operating Leases
Year 1	\$ 519	\$ 1,161
Year 2	519	1,083
Year 3	519	987
Year 4	519	886
Year 5	519	674
Thereafter	2,564	2,390
Total Lease Payments	5,159	7,181
Less Imputed Interest	(2,063)	(837)
Total	\$ 3,096	\$ 6,344

NOTE 15 - Business Combinations

Pending Acquisition

On September 20, 2021, the Company entered into an Agreement and Plan of Reorganization with Citizens Union Bancorp of Shelbyville, Inc. ("CUB"), pursuant to which CUB agreed to be merged with and into the Company (the "Merger"). Shortly following completion of the Merger, CUB's subsidiary bank, Citizens Union Bank of Shelbyville, Inc., will be merged with and into the Company's subsidiary bank, German American Bank. CUB, based in Shelbyville, Kentucky, operates 15 retail banking offices through Citizens Union Bank of Shelbyville, Inc. in Kentucky. At June 30, 2021, CUB reported total assets of approximately \$1,074,000, total loans of approximately \$716,400 and total deposits of approximately \$889,200.

Under terms of the definitive agreement, CUB common shareholders will receive a fixed exchange ratio of a 0.7739 share of German American common stock for each share of CUB in a tax-free exchange, and a cash payment of \$13.44 per CUB share. Based on the number of CUB common shares expected to be outstanding at closing, The Company would issue approximately 2.9 million shares of its common stock, and pay approximately \$49,813 cash, for all of the issued and outstanding common shares of CUB. The Company has also agreed, upon completion of the Merger, to make a cash payment in cancellation of CUB's unexercised stock options, which payment is currently estimated to total approximately \$918, if none of the outstanding options were to be exercised before closing.

Consummation of the Merger is subject to approval by federal and state banking regulatory authorities, approval by the shareholders of CUB and certain other closing conditions. Assuming such approvals are timely secured, the Company expects that the Merger will be completed in the first quarter of 2022.

This pending bank acquisition will be consistent with the Company's strategy to enhance its presence in the Louisville, Kentucky metropolitan market area. The acquisition offers the Company the opportunity to increase profitability by introducing existing products and services to the acquired customer base as well as add new customers in the expanded region.

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

GERMAN AMERICAN BANCORP, INC. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

German American Bancorp, Inc. is a Nasdaq-traded (symbol: GABC) financial holding company based in Jasper, Indiana. German American, through its banking subsidiary German American Bank, operates 64 banking offices in 19 contiguous southern Indiana counties and seven Kentucky counties. The Company also owns an investment brokerage subsidiary (German American Investment Services, Inc.) and a full line property and casualty insurance agency (German American Insurance, Inc.).

Throughout this Management's Discussion and Analysis, as elsewhere in this Report, when we use the term "Company," we will usually be referring to the business and affairs (financial and otherwise) of German American Bancorp, Inc. and its subsidiaries and affiliates as a whole. Occasionally, we will refer to the term "parent company" or "holding company" when we mean to refer to only German American Bancorp, Inc.

This section presents an analysis of the consolidated financial condition of the Company as of September 30, 2021 and December 31, 2020 and the consolidated results of operations for the three and nine months ended September 30, 2021 and 2020. This discussion should be read in conjunction with the consolidated financial statements and other financial data presented elsewhere herein and with the financial statements and other financial data, as well as the Management's Discussion and Analysis of Financial Condition and Results of Operations, included in the Company's Annual Report on Form 10-K for the year ended December 31, 2020.

MANAGEMENT OVERVIEW

This updated discussion should be read in conjunction with the Management Overview that was included in our Management's Discussion and Analysis of Financial Condition and Results of Operations in the Company's Annual Report on Form 10-K for the year ended December 31, 2020.

Net income for the quarter ended September 30, 2021 totaled \$21,486,000, or \$0.81 per share, an increase of 47% on a per share basis compared with the third quarter 2020 net income of \$14,593,000, or \$0.55 per share. Net income for the nine months ended September 30, 2021 totaled \$64,865,000, or \$2.44 per share, an increase of 56% on a per share basis compared with the first nine months of 2020 net income of \$41,320,000, or \$1.56 per share. The net income growth during the third quarter and first nine months of 2021 compared with the same periods of 2020 was driven by a number of factors including improved net interest income, lower provision for credit losses and increased non-interest revenue which was partially offset by a modestly higher level of non-interest expense.

On September 20, 2021, the Company entered into an Agreement and Plan of Reorganization with Citizens Union Bancorp of Shelbyville, Inc. ("CUB"), pursuant to which CUB agreed to merge with and into the Company. The merger agreement also provides that CUB's wholly-owned banking subsidiary, Citizens Union Bank of Shelbyville, Inc. will be merged with and into the Company's subsidiary bank, German American Bank, shortly following the holding company merger. Based on the number of CUB common shares expected to be outstanding at closing, the Company would issue approximately 2.9 million shares of its common stock, and pay approximately \$50.7 million cash, for all of the issued and outstanding common shares of CUB and in cancellation of all outstanding options to acquire CUB common stock. Citizens Union Bancorp of Shelbyville, Inc. is a bank holding company headquartered in Shelbyville, Kentucky. Citizens Union has branch offices located in Shelby, Jefferson, Spencer, Bullitt, Oldham, Owen, Gallatin and Hardin counties in Kentucky. At June 30, 2021, CUB reported total assets of approximately \$1.1 billion, total loans of approximately \$716.4 million, and total deposits of approximately \$889.2 million. Completion of the mergers is subject to approval by regulatory authorities and CUB's shareholders, as well as certain other closing conditions. The transaction is expected to be completed in the first quarter of 2022.

For further information regarding this pending acquisition, see Note 15 (Business Combinations) in the Notes to the Consolidated Financial Statements included in Item 1 of this Report.

On March 12, 2021, the Company announced an operating optimization plan, pursuant to which the Company's banking subsidiary will consolidate seven branch offices and will implement various staff reductions during 2021. In making its decision to consolidate these branches, which are generally expected to be integrated with other nearby bank branches, the Company considered, among other factors, the operating costs of the branches, certain physical limitations impacting the bank facilities, and their proximity to other branch locations. In addition, the Company's evaluation of the branch consolidations and the reductions in staff also took into consideration the numbers and types of transactions being conducted by its customers and the increased usage of online and mobile banking. As a result of these optimization actions, the Company recorded pre-tax

charges of approximately \$2.6 million during the first nine months of 2021, primarily for valuation adjustments on branch facilities, lease termination costs, and severance and related payments. The branch consolidations and staff reductions are expected to primarily be completed by year-end 2021.

As a part of the operating optimization plan, the Company announced on June 4, 2021 that German American Bank, its wholly-owned banking subsidiary, had entered into a Branch Purchase and Assumption Agreement with The Home Savings and Loan Company of Kenton, Ohio ("HSLC"), pursuant to which German American Bank would sell its two branches located in Lexington, Kentucky. On September 24, 2021, the Company completed the sale of its these two branches. As part of the sale, HSLC assumed approximately \$17.6 million in total deposits and purchased approximately \$17.8 million in total loans.

CRITICAL ACCOUNTING POLICIES AND ESTIMATES

The financial condition and results of operations for the Company presented in the Consolidated Financial Statements, accompanying Notes to the Consolidated Financial Statements, and selected financial data appearing elsewhere within this Report, are, to a large degree, dependent upon the Company's accounting policies. The selection of and application of these policies involve estimates, judgments, and uncertainties that are subject to change. The critical accounting policies and estimates that the Company has determined to be the most susceptible to change in the near term relate to the determination of the allowance for credit losses, the valuation of securities available for sale, income tax expense, and the valuation of goodwill and other intangible assets.

Allowance for Credit Losses

The Company maintains an allowance for credit losses to cover the estimated expected credit losses over the expected contractual life of the loan portfolio. Loan losses are charged against the allowance when management believes the uncollectibility of a loan balance is confirmed. Subsequent recoveries, if any, are credited to the allowance. Allocations of the allowance may be made for specific loans, but the entire allowance is available for any loan that, in management's judgment, should be charged-off. A provision for credit losses is charged to operations based on management's periodic evaluation of the necessary allowance balance. Evaluations are conducted at least quarterly and more often if deemed necessary. The ultimate recovery of all loans is susceptible to future market factors beyond the Company's control.

The Company has an established process to determine the adequacy of the allowance for credit losses. The determination of the allowance is inherently subjective, as it requires significant estimates, including the amounts and timing of expected future cash flows on individually analyzed loans, estimated losses on other classified loans and pools of homogeneous loans, and consideration of past loan loss experience, the nature and volume of the portfolio, information about specific borrower situations and estimated collateral values, economic conditions, reasonable and supportable forecasts and other factors, all of which may be susceptible to significant change. The allowance consists of two components of allocations, specific and general. These two components represent the total allowance for credit losses deemed adequate to cover expected credit losses over the expected life of the loan portfolio.

Commercial and agricultural loans are subject to a standardized grading process administered by an internal loan review function. The need for specific reserves is considered for credits when: (a) the customer's cash flow or net worth appears insufficient to repay the loan; (b) the loan has been criticized in a regulatory examination; (c) the loan is on non-accrual; or (d) other reasons where the ultimate collectability of the loan is in question, or the loan characteristics require special monitoring.

Specific reserves on individually analyzed loans are determined by comparing the loan balance to the present value of expected cash flows or expected collateral proceeds. Allocations are also applied to categories of loans not individually analyzed but for which the rate of loss is expected to be greater than other similar type loans, including non-performing consumer or residential real estate loans. Such allocations are based on past loss experience, reasonable and supportable forecasts and information about specific borrower situations and estimated collateral values.

General allocations are made for commercial and agricultural loans that are graded as substandard and special mention, but are not individually analyzed for specific reserves as well as other pools of loans, including non-classified loans, homogeneous portfolios of consumer and residential real estate loans, and loans within certain industry categories believed to present unique risk of loss. General allocations of the allowance are primarily made based on historical averages for loan losses for these portfolios along with reasonable and supportable forecasts, judgmentally adjusted for economic, external and internal quantitative and qualitative factors and portfolio trends. Economic factors include evaluating changes in international, national, regional and local economic and business conditions that affect the collectability of the loan portfolio. Internal factors include evaluating changes in lending policies and procedures; changes in the nature and volume of the loan portfolio; and changes in experience, ability and depth of lending management and staff.

The allowance for credit losses for loans represents management's estimate of all expected credit losses over the expected contractual life of the loan portfolio. Determining the appropriateness and adequacy of the allowance is complex and requires judgment by management about the effect of matters that are inherently uncertain. Subsequent evaluations of the loan portfolio may result in significant changes in the allowance for credit losses in future periods.

Securities Valuation

Available-for-sale debt securities in unrealized loss positions are evaluated for impairment related to credit losses at least quarterly. For available-for-sale debt securities in an unrealized loss position, the Company assesses whether we intend to sell, or it is more likely than not that we will be required to sell the security before recovery of its amortized cost basis. If either of the criteria regarding intent or requirement to sell is met, the security's amortized cost basis is written down to fair value through income. For available-for-sale debt securities that do not meet the criteria, the Company evaluates whether the decline in fair value has resulted from credit losses or other factors. In making this assessment, management considers the extent to which fair value is less than amortized cost, any changes to the rating of the security by a rating agency, and adverse conditions specifically related to the security and the issuer, among other factors. If this assessment indicates that a credit loss exists, the Company compares the present value of cash flows expected to be collected from the security with the amortized cost basis of the security. If the present value of cash flows expected to be collected is less than the amortized cost basis for the security, a credit loss exists and an allowance for credit losses is recorded, limited to the amount that the fair value of the security is less than its amortized cost basis. Any impairment that has not been recorded through an allowance for credit losses is recognized in other comprehensive income, net of applicable taxes. No allowance for credit losses for available-for-sale debt securities was needed at September 30, 2021. Accrued interest receivable on available-for-sale debt securities is excluded from the estimate of credit losses. As of September 30, 2021, gross unrealized gains on the securities available-for-sale portfolio totaled approximately \$32,698,000 and gross unrealized losses totaled approximately \$17,595,000 net of applicable taxes is included in other comprehensive income.

Equity securities that do not have readily determinable fair values are carried at cost, less impairment with observable price changes being recognized in earnings.

Income Tax Expense

Income tax expense involves estimates related to the valuation allowance on deferred tax assets and loss contingencies related to exposure from tax examinations presumed to occur.

A valuation allowance reduces deferred tax assets to the amount management believes is more likely than not to be realized. In evaluating the realization of deferred tax assets, management considers the likelihood that sufficient taxable income of appropriate character will be generated within carry-back and carry-forward periods, including consideration of available tax planning strategies. Tax-related loss contingencies, including assessments arising from tax examinations and tax strategies, are recorded as liabilities when the likelihood of loss is probable and an amount or range of loss can be reasonably estimated. In considering the likelihood of loss, management considers the nature of the contingency, the progress of any examination or related protest or appeal, the views of legal counsel and other advisors, experience of the Company or other enterprises in similar matters, if any, and management's intended response to any assessment.

Goodwill and Other Intangible Assets

Goodwill resulting from business combinations represents the excess of the purchase price over the fair value of the net assets of businesses acquired. Goodwill resulting from business combinations is generally determined as the excess of the fair value of the consideration transferred, plus the fair value of any noncontrolling interests in the acquiree, over the fair value of the net assets acquired and liabilities assumed as of the acquisition date. Goodwill and intangible assets acquired in a purchase business combination and determined to have an indefinite useful life are not amortized, but tested for impairment at least annually. The Company has selected December 31 as the date to perform the annual impairment test. Goodwill is the only intangible asset with an indefinite life on the Company's balance sheet. No impairment to Goodwill was indicated based on year-end testing and no triggering events occurred in 2021 causing reassessment.

Intangible assets with definite useful lives are amortized over their estimated useful lives to their estimated residual values. Other intangible assets consist of core deposit and acquired customer relationship intangible assets. They are initially measured at fair value and then are amortized over their estimated useful lives, which range from 6 to 10 years.

COVID-19 PANDEMIC BUSINESS UPDATE

The novel coronavirus disease 2019 (COVID-19) pandemic continued to impact our operations during the quarter ended September 30, 2021. While uncertainty remains as to the future effects of the pandemic, an improving business climate,

supported by unprecedented fiscal stimulus, an accommodative Federal Reserve, and modest increases in COVID-19 vaccination rates, has helped to mitigate the negative impacts of the pandemic on our financial condition and results of operations, despite the challenges presented by very low interest rates, muted loan growth, and excess liquidity.

CARES Act and the Paycheck Protection Program

As previously disclosed, the Coronavirus Aid, Relief and Economic Security Act (the “CARES Act”) was signed into law in March 2020, providing an approximately \$2 trillion stimulus package that included direct payments to individual taxpayers, economic stimulus to significantly impacted industry sectors, emergency funding for hospitals and providers, small business loans, increased unemployment benefits, and a variety of tax incentives. For small businesses, eligible nonprofits and certain others, the CARES Act established a Paycheck Protection Program (“PPP”), a lending program administered by the Small Business Administration (“SBA”) that is intended to incentivize participants to retain their employees by providing them with loans that are fully guaranteed by the U.S. government and subject to forgiveness if program guidelines are met. The PPP was later extended and modified by the Paycheck Protection Program and Health Care Enhancement Act in April 2020 and the Paycheck Protection Program Flexibility Act in June 2020, with PPP funding under this initial round expiring on August 8, 2020.

In December 2020, the Economic Aid to Hard-Hit Small Businesses, Nonprofits, and Venues Act was signed into law as part of the Consolidated Appropriations Act, 2021 (the “CAA”). In addition to direct stimulus payments and other aid, this Act provided for a second round of PPP loans through March 31, 2021. Under the American Rescue Plan Act of 2021 and the PPP Extension Act of 2021, which were both enacted during March 2021, additional funds were provided for the program and the deadline for applying for PPP loans was extended through May 31, 2021 (with the SBA having been given until June 30, 2021 to process loan applications).

The Company actively participated in both rounds of the PPP, lending funds primarily to its existing loan and/or deposit customers. The PPP loans carry an interest rate of 1.00% and included a processing fee that varied depending on the balance of the loan at origination (which fee is recognized over the life of the loan). The vast majority of the Company’s PPP loans made during 2020 had two-year maturities, while PPP loans made during 2021 have five-year maturities.

Under the first round of the PPP (i.e., the 2020 round), the Company originated loans totaling approximately \$351.3 million in principal amount, with approximately \$12.0 million of related net processing fees on 3,070 PPP loan relationships. As of September 30, 2021, \$347.6 million of those first round PPP loans had been forgiven by the SBA and repaid to the Company pursuant to the terms of the program or repaid by customers, with nearly \$12.0 million in net processing fees having been recognized by the Company.

Under the second round of the PPP (i.e., the 2021 round), the Company originated loans totaling approximately \$157.0 million in principal amount, with approximately \$9.0 million of related net processing fees, on 2,601 PPP loan relationships. As of September 30, 2021, \$89.5 million of second round PPP loans had been forgiven by the SBA and repaid to the Company, with \$5.9 million in net processing fees having been recognized by the Company. As a result of the forgiveness of the first and second round PPP loans, \$71.2 million of total PPP loans remain outstanding as of September 30, 2021, with approximately \$3.2 million of net fees remaining deferred on that date.

RESULTS OF OPERATIONS

Net Income:

Net income for the quarter ended September 30, 2021 totaled \$21,486,000, or \$0.81 per share, an increase of 47% on a per share basis compared with the third quarter 2020 net income of \$14,593,000, or \$0.55 per share. Net income for the nine months ended September 30, 2021 totaled \$64,865,000, or \$2.44 per share, an increase of 56% on a per share basis compared with the first nine months of 2020 net income of \$41,320,000, or \$1.56 per share. The net income growth during the third quarter and first nine months of 2021 compared with the same periods of 2020 was driven by a number of factors including improved net interest income, lower provision for credit losses and increased non-interest revenue which was partially offset by a modestly higher level of non-interest expense.

Net Interest Income:

Net interest income is the Company’s single largest source of earnings, and represents the difference between interest and fees realized on earning assets, less interest paid on deposits and borrowed funds. Several factors contribute to the determination of net interest income and net interest margin, including the volume and mix of earning assets, interest rates, and income taxes. Many factors affecting net interest income are subject to control by management policies and actions. Factors beyond the

control of management include the general level of credit and deposit demand, Federal Reserve Board monetary policy, and changes in tax laws.

The following table summarizes net interest income (on a tax-equivalent basis) for the three months ended September 30, 2021 and 2020. For tax-equivalent adjustments, an effective tax rate of 21% was used for both periods⁽¹⁾.

Average Balance Sheet (Tax-equivalent basis / dollars in thousands)						
	Three Months Ended September 30, 2021			Three Months Ended September 30, 2020		
	Principal Balance	Income / Expense	Yield / Rate	Principal Balance	Income / Expense	Yield / Rate
ASSETS						
Federal Funds Sold and Other Short-term Investments	\$ 391,814	\$ 141	0.14 %	\$ 197,203	\$ 45	0.09 %
Securities:						
Taxable	857,394	3,261	1.52 %	559,488	2,350	1.68 %
Non-taxable	788,128	5,937	3.01 %	461,623	4,019	3.48 %
Total Loans and Leases ⁽²⁾	3,055,926	35,538	4.62 %	3,260,435	36,612	4.47 %
TOTAL INTEREST EARNING ASSETS	5,093,262	44,877	3.51 %	4,478,749	43,026	3.83 %
Other Assets	384,892			399,138		
Less: Allowance for Credit Losses	(40,687)			(42,933)		
TOTAL ASSETS	<u>\$ 5,437,467</u>			<u>\$ 4,834,954</u>		
LIABILITIES AND SHAREHOLDERS' EQUITY						
Interest-bearing Demand, Savings and Money Market Deposits	\$ 2,737,358	\$ 663	0.10 %	\$ 2,279,517	\$ 813	0.14 %
Time Deposits	395,114	476	0.48 %	540,248	1,679	1.24 %
FHLB Advances and Other Borrowings	190,252	1,149	2.40 %	212,859	1,233	2.30 %
TOTAL INTEREST-BEARING LIABILITIES	3,322,724	2,288	0.27 %	3,032,624	3,725	0.49 %
Demand Deposit Accounts	1,409,841			1,144,685		
Other Liabilities	46,268			54,490		
TOTAL LIABILITIES	4,778,833			4,231,799		
Shareholders' Equity	658,634			603,155		
TOTAL LIABILITIES AND SHAREHOLDERS' EQUITY	<u>\$ 5,437,467</u>			<u>\$ 4,834,954</u>		
COST OF FUNDS			0.18 %			0.33 %
NET INTEREST INCOME		<u>\$ 42,589</u>			<u>\$ 39,301</u>	
NET INTEREST MARGIN			3.33 %			3.50 %

⁽¹⁾ Effective tax rates were determined as though interest earned on the Company's investments in municipal bonds and loans was fully taxable.

⁽²⁾ Loans held-for-sale and non-accruing loans have been included in average loans.

During the third quarter of 2021, net interest income, on a non tax-equivalent basis, totaled \$41,287,000, an increase of \$2,899,000, or 8%, compared to the third quarter of 2020 net interest income of \$38,388,000. The increase in net interest income in the third quarter of 2021 compared with the third quarter of 2020 was largely attributable to an increase in average earning assets, a higher level of fees recognized related to PPP loans which were partially offset by a lower level of accretion of discounts on acquired loans, and a decreased level of interest expense on deposit accounts related to lower interest rates.

The tax equivalent net interest margin for the quarter ended September 30, 2021 was 3.33% compared to 3.50% in the third quarter of 2020. The Company's net interest margin in both periods presented has been impacted significantly by fees recognized as a part of the PPP and accretion of discounts on acquired loans.

Fees recognized on PPP loans through net interest income totaled \$4,109,000 during the third quarter of 2021 and \$1,457,000 during the third quarter of 2020. The fees recognized related to the PPP contributed approximately 32 basis points to the net interest margin on an annualized basis in the third quarter of 2021 and 13 basis points in the third quarter of 2020. Accretion of discounts on acquired loans contributed approximately 4 basis points to the net interest margin in the third quarter of 2021 and 11 basis points in the third quarter of 2020. Accretion of discounts on acquired loans totaled \$516,000 during the third quarter of 2021 and \$1,189,000 during the third quarter of 2020.

Historically low market interest rates continue to impact the Company's net interest margin. Lower market interest rates continue to negatively impact earning asset yields, with these declines being partially mitigated by a lower cost of funds. The Company has also continued to carry excess liquidity on the balance sheet that resulted from significant deposit growth during 2020, which has continued in the first nine months of 2021, along with the forgiveness of PPP loans.

The following table summarizes net interest income (on a tax-equivalent basis) for the nine months ended September 30, 2021 and 2020. For tax-equivalent adjustments, an effective tax rate of 21% was used for both periods⁽¹⁾.

Average Balance Sheet (Tax-equivalent basis / dollars in thousands)						
	Nine Months Ended September 30, 2021			Nine Months Ended September 30, 2020		
	Principal Balance	Income / Expense	Yield / Rate	Principal Balance	Income / Expense	Yield / Rate
ASSETS						
Federal Funds Sold and Other Short-term Investments	\$ 372,177	\$ 329	0.12 %	\$ 160,818	\$ 287	0.24 %
Securities:						
Taxable	794,023	9,391	1.58 %	548,229	8,166	1.99 %
Non-taxable	681,153	15,928	3.12 %	381,530	10,495	3.67 %
Total Loans and Leases ⁽²⁾	3,094,214	105,263	4.55 %	3,191,254	112,702	4.72 %
TOTAL INTEREST EARNING ASSETS	4,941,567	130,911	3.54 %	4,281,831	131,650	4.10 %
Other Assets	400,058			397,224		
Less: Allowance for Credit Losses	(44,612)			(37,492)		
TOTAL ASSETS	<u>\$ 5,297,013</u>			<u>\$ 4,641,563</u>		
LIABILITIES AND SHAREHOLDERS' EQUITY						
Interest-bearing Demand, Savings and Money Market Deposits	\$ 2,645,261	\$ 1,972	0.10 %	\$ 2,164,832	\$ 5,303	0.33 %
Time Deposits	429,201	1,878	0.59 %	588,121	6,589	1.50 %
FHLB Advances and Other Borrowings	184,467	3,445	2.50 %	225,477	4,230	2.51 %
TOTAL INTEREST-BEARING LIABILITIES	3,258,929	7,295	0.30 %	2,978,430	16,122	0.72 %
Demand Deposit Accounts	1,352,519			1,022,884		
Other Liabilities	46,282			51,324		
TOTAL LIABILITIES	4,657,730			4,052,638		
Shareholders' Equity	639,283			588,925		
TOTAL LIABILITIES AND SHAREHOLDERS' EQUITY	<u>\$ 5,297,013</u>			<u>\$ 4,641,563</u>		
COST OF FUNDS			0.20 %			0.50 %
NET INTEREST INCOME		<u>\$ 123,616</u>			<u>\$ 115,528</u>	
NET INTEREST MARGIN			3.34 %			3.60 %

⁽¹⁾ Effective tax rates were determined as though interest earned on the Company's investments in municipal bonds and loans was fully taxable.

⁽²⁾ Loans held-for-sale and non-accruing loans have been included in average loans.

During the nine months ended September 30, 2021, net interest income, on a non tax-equivalent basis, totaled \$120,099,000, an increase of \$6,996,000, or 6%, compared to the first nine months of 2020 net interest income of \$113,103,000. The increase in net interest income in the first nine months of 2021 compared with the same period of 2020 was largely attributable to an increase in average earning assets, a higher level of fees recognized related to PPP loans which were partially offset by a lower level of accretion of loan discounts on acquired loans, and a decreased level of interest expense on interest bearing liabilities related to lower interest rates.

The tax equivalent net interest margin for the nine months ended September 30, 2021 was 3.34% compared to 3.60% in the first nine months of 2020. The Company's net interest margin in both periods presented has been impacted significantly by fees recognized as a part of the PPP and accretion of discounts on acquired loans.

Fees recognized on PPP loans through net interest income totaled \$9,902,000 during the first nine months of 2021 and \$2,578,000 during the same period of 2020. The fees recognized related to the PPP contributed approximately 27 basis points to the net interest margin on an annualized basis in the first nine months of 2021 and 8 basis points in the same period of 2020.

Accretion of discounts on acquired loans contributed approximately 6 basis points to the net interest margin in the nine months ended September 30, 2021 and 15 basis points in the same period of 2020. Accretion of discounts on acquired loans totaled \$2,054,000 during the first nine months of 2021 and \$4,714,000 during the same period of 2020.

Historically low market interest rates continue to impact the Company's net interest margin. Lower market interest rates continue to negatively impact earning asset yields, with these declines being partially mitigated by a lower cost of funds. The Company has also continued to carry excess liquidity on the balance sheet that resulted from significant deposit growth during 2020, which has continued in the first nine months of 2021, forgiveness of PPP loans, and somewhat muted loan growth.

Provision for Credit Losses:

The Company provides for credit losses through regular provisions to the allowance for credit losses. The provision is affected by net charge-offs on loans and changes in specific and general allocations of the allowance. During the quarter ended September 30, 2021, the Company recorded a negative provision for credit losses of \$2,000,000 compared with the third quarter of 2020 provision for credit losses of \$4,500,000. The negative provision for credit losses represented approximately 26 basis points of average loans on an annualized basis in the third quarter of 2021 compared to a provision for credit losses of 55 basis points of average loans on an annualized basis in the third quarter of 2020.

During the nine months ended September 30, 2021, the Company recorded a negative provision for credit losses of \$8,500,000 compared with the first nine months of 2020 provision for credit losses of \$15,550,000. The negative provision for credit losses represented approximately 37 basis points of average loans on an annualized basis in the first nine months of 2021 compared to a provision for credit losses of 65 basis points of average loans on an annualized basis in the same period of 2020.

The negative provision for credit losses in the third quarter and first nine months of 2021 was largely due to declines in certain adversely criticized assets and improvement in certain pandemic-related stressed sectors for which the Company had provided significant levels of allowance for credit losses during 2020. The level of provision for credit losses during the third quarter and first nine months of 2020 was primarily due to the developments related to the COVID-19 pandemic and the resulting impact on the economic assumptions used in the CECL model.

Net charge-offs totaled \$197,000 or 3 basis points on an annualized basis of average loans outstanding during the three months ended September 30, 2021, compared with \$163,000 or 2 basis point on an annualized basis of average loans outstanding during the same period of 2020. Net charge-offs totaled \$561,000 or 2 basis points on an annualized basis of average loans outstanding during the nine months ended September 30, 2021, compared with \$714,000 or 3 basis points on an annualized basis of average loans outstanding during the same period of 2020.

The provision for credit losses made during the three and nine months ended September 30, 2021 was made at a level deemed necessary by management to absorb expected losses in the loan portfolio. A detailed evaluation of the adequacy of the allowance for credit losses is completed quarterly by management, the results of which are used to determine provision for credit losses. Management estimates the allowance balance required using past loan loss experience, the nature and volume of the portfolio, information about specific borrower situations and estimated collateral values, economic conditions and reasonable and supportable forecasts along with other qualitative and quantitative factors.

Non-interest Income:

During the quarter ended September 30, 2021, non-interest income totaled \$15,556,000, an increase of \$2,277,000, or 17%, compared with the third quarter of 2020.

Non-interest Income (dollars in thousands)	Three Months Ended September 30,		Change From Prior Period	
	2021	2020	Amount Change	Percent Change
Trust and Investment Product Fees	\$ 2,690	\$ 1,957	\$ 733	37 %
Service Charges on Deposit Accounts	2,017	1,773	244	14
Insurance Revenues	2,007	1,989	18	1
Company Owned Life Insurance	493	355	138	39
Interchange Fee Income	3,339	2,795	544	19
Other Operating Income	2,595	942	1,653	175
Subtotal	13,141	9,811	3,330	34
Net Gains on Sales of Loans	2,197	2,861	(664)	(23)
Net Gains on Securities	218	607	(389)	(64)
Total Non-interest Income	\$ 15,556	\$ 13,279	\$ 2,277	17

Trust and investment product fees increased \$733,000, or 37%, during the third quarter of 2021 compared with the third quarter of 2020. The increase during the third quarter of 2021 was largely attributable to increased assets under management within the Company's wealth management group.

Interchange fee income increased \$544,000, or 19%, during the quarter ended September 30, 2021 compared with the third quarter of 2020. The increased level of fees during the third quarter of 2021 compared with the third quarter of 2020 was due to increased economic activity and increased card utilization by customers. Card utilization in 2020 was impacted by the economic impacts of the COVID-19 pandemic.

Other operating income increased \$1,653,000, or 175%, during the third quarter of 2021 compared with the third quarter of 2020. The increase during the third quarter of 2021 was primarily attributable to the net gain of approximately \$1.4 million related to the sale of the two branch office locations.

Net gains on sales of loans declined \$664,000, or 23%, during the third quarter of 2021 compared with the third quarter of 2020. The decline in the third quarter of 2021 compared with the third quarter of 2020 was generally attributable to a lower volume of loans sold and fair value adjustments on commitments to sell loans, which were partially offset by higher pricing levels on loans sold. Loan sales totaled \$69.7 million during the third quarter of 2021 compared with \$83.5 million during the third quarter of 2020.

The Company realized \$218,000 in gains on sales of securities during the third quarter of 2021 compared with \$607,000 during the third quarter of 2020. The sales of securities in both periods was done as part of modest shifts in the allocations within the securities portfolio.

During the nine months ended September 30, 2021, non-interest income totaled \$44,495,000, an increase of \$4,712,000, or 12%, compared with the first nine months of 2020.

Non-interest Income (dollars in thousands)	Nine Months Ended September 30,		Change From Prior Period	
	2021	2020	Amount Change	Percent Change
Trust and Investment Product Fees	\$ 7,668	\$ 5,855	\$ 1,813	31 %
Service Charges on Deposit Accounts	5,430	5,375	55	1
Insurance Revenues	7,319	7,048	271	4
Company Owned Life Insurance	1,230	1,933	(703)	(36)
Interchange Fee Income	9,651	7,753	1,898	24
Other Operating Income	5,287	2,251	3,036	135
Subtotal	36,585	30,215	6,370	21
Net Gains on Sales of Loans	6,417	7,378	(961)	(13)
Net Gains on Securities	1,493	2,190	(697)	(32)
Total Non-interest Income	\$ 44,495	\$ 39,783	\$ 4,712	12

Trust and investment product fees increased \$1,813,000, or 31%, during the nine months ended September 30, 2021 compared with the first nine months of 2020. The increase during 2021 was largely attributable to increased assets under management within the Company's wealth management group.

Company owned life insurance revenue declined \$703,000, or 36%, during the nine months ended September 30, 2021 compared with the first nine months of 2020. The decline was largely related to death benefits received from life insurance policies during 2020.

Interchange fee income increased \$1,898,000, or 24%, during the first nine months of 2021 compared with the same period of 2020. The increased level of fees during 2021 compared with 2020 was due to increased economic activity and increased card utilization by customers. Card utilization in 2020 was impacted by the economic impacts of the COVID-19 pandemic.

Other operating income increased \$3,036,000, or 135%, during the first nine months of 2021 compared with the first nine months of 2020. The increase during 2021 was largely attributable to the net gain of approximately \$1.4 million related to the sale of the two branch office locations and fair value adjustments and higher transaction fees associated with interest rate swap transactions with loan customers.

Net gains on sales of loans declined \$961,000, or 13%, during the first nine months of 2021 compared with the same period of 2020. The decline in 2021 compared with 2020 was generally attributable to a lower level of fair value adjustments on commitments to sell loans and a modestly lower level of loans sold, which were partially offset by higher pricing levels on loans sold. Loan sales totaled \$199.7 million during 2021 compared with \$219.4 million during 2020.

The Company realized \$1,493,000 in gains on sales of securities during the first nine months of 2021 compared with \$2,190,000 during the same period of 2020. The sales of securities in both periods was done as part of modest shifts in the allocations within the securities portfolio.

Non-interest Expense:

During the quarter ended September 30, 2021, non-interest expense totaled \$32,444,000, an increase of \$3,024,000, or 10%, compared with the third quarter of 2020. The third quarter of 2021 included approximately \$457,000 of non-recurring acquisition related expenses for the acquisition of Citizens Union.

Non-interest Expense (dollars in thousands)	Three Months Ended September 30,		Change From Prior Period	
	2021	2020	Amount Change	Percent Change
Salaries and Employee Benefits	\$ 17,274	\$ 17,409	\$ (135)	(1) %
Occupancy, Furniture and Equipment Expense	3,453	3,362	91	3
FDIC Premiums	383	326	57	17
Data Processing Fees	2,006	1,693	313	18
Professional Fees	1,357	875	482	55
Advertising and Promotion	897	708	189	27
Intangible Amortization	661	860	(199)	(23)
Other Operating Expenses	6,413	4,187	2,226	53
Total Non-interest Expense	<u>\$ 32,444</u>	<u>\$ 29,420</u>	<u>\$ 3,024</u>	<u>10</u>

Data processing fees increased \$313,000, or 18%, during the third quarter of 2021 compared with the third quarter of 2020. The increase during the third quarter of 2021 was largely attributable to data processing fees related to the branch office sale and the recently announced Citizens Union acquisition.

Professional fees increased \$482,000, or 55%, in the third quarter of 2021 compared with the third quarter of 2020. The increase during the third quarter of 2021 was primarily attributable to professional fees associated with the pending acquisition of Citizens Union.

Advertising and promotion expense increased \$189,000, or 27%, in the third quarter of 2021 compared with the third quarter of 2020. The increase during the third quarter of 2021 was primarily related to corporate sponsorships of events and increased community activities. The opportunities for sponsorships and community activities have increased as the in-person activities of our customers and communities continue to resume as certain COVID-19 restrictions have been eased.

Other operating expenses increased \$2,226,000, or 53%, during the third quarter of 2021 compared with the third quarter of 2020. The increase during the third quarter of 2021 was primarily attributable to the establishment of a settlement reserve for a lawsuit challenging the Company's checking account practices associated with its assessment of overdraft fees for certain debit card transactions. Like many other financial institutions, the Company has been the subject of an overdraft fee related putative class action lawsuit since the third quarter of 2020. This type of litigation is often time consuming and expensive to defend. In order to avoid further costs associated with this type of litigation, the Company determined it was in its best interest to pursue a settlement of this lawsuit during the third quarter of 2021 and therefore accrued a \$3,050,000 settlement reserve. On October 21, 2021, the Company executed a settlement agreement for payment of that amount in connection with this lawsuit which remains subject to court approval.

During the nine months ended September 30, 2021, non-interest expense totaled \$92,740,000, an increase of \$4,904,000, or 6%, compared with the first nine months of 2020. The nine months ended September 30, 2021 included non-recurring expenses totaling \$2,567,000 related to the Company's previously discussed operating optimization plan (see "Management Overview" for additional information) and included \$551,000 of non-recurring acquisition related expenses for the pending acquisition of Citizens Union.

Non-interest Expense (dollars in thousands)	Nine Months Ended September 30,		Change From Prior Period	
	2021	2020	Amount Change	Percent Change
Salaries and Employee Benefits	\$ 51,454	\$ 50,691	\$ 763	2 %
Occupancy, Furniture and Equipment Expense	11,631	10,424	1,207	12
FDIC Premiums	1,046	449	597	133
Data Processing Fees	5,528	5,142	386	8
Professional Fees	4,030	3,041	989	33
Advertising and Promotion	2,384	2,661	(277)	(10)
Intangible Amortization	2,132	2,729	(597)	(22)
Other Operating Expenses	14,535	12,699	1,836	14
Total Non-interest Expense	<u>\$ 92,740</u>	<u>\$ 87,836</u>	<u>\$ 4,904</u>	<u>6</u>

Salaries and benefits increased \$763,000, or 2%, during the first nine months of 2021 compared with the same period of 2020. The increase in salaries and benefits during 2021 was in part attributable to employee severance and related cost associated with the Company's operating optimization plan that totaled \$613,000 during the first nine months of 2021. Also contributing to the increase was a higher level of incentive plan compensation, higher variable compensation related to residential real estate loan production and wealth management revenue and higher health insurance costs, which were partially offset by a higher level of salary deferral related to the origination of PPP loans.

Occupancy, furniture and equipment expense increased \$1,207,000, or 12%, during the first nine months of 2021 compared with the same period of 2020. The increase during 2021 was due to lease termination costs associated with the Company's operating optimization plan that totaled approximately \$1,411,000 during the first nine months of 2021.

FDIC premiums increased \$597,000 during nine months ended September 30, 2021 compared with the same period of 2020. The increase during 2021 compared with 2020 was related to credits received from the FDIC during 2020. There were no credits received during 2021. The credits received in 2020 were due to the reserve ratio of the deposit insurance fund exceeding the FDIC targeted levels.

Professional fees expense increased \$989,000, or 33%, in the first nine months of 2021 compared with the same period of 2020. The increase during 2021 compared with 2020 was largely attributable to professional fees associated with the pending acquisition of Citizens Union and an increase in legal fees related to non acquisition related legal matters.

Other operating expenses increased \$1,836,000, or 14%, during the nine months ended September 30, 2021 compared with the same period of 2020. The increase during 2021 was primarily attributable to the previously discussed establishment of a settlement reserve for a lawsuit challenging the Company's assessment of overdraft fees for certain debit card transactions.

Income Taxes:

The Company's effective income tax rate was 18.6% and 17.8%, respectively, during the three months ended September 30, 2021 and 2020. The Company's effective tax rate was 19.3% and 16.5% during the nine months ended September 30, 2021 and 2020, respectively. The effective tax rate in all periods presented was lower than the blended statutory rate resulting primarily from the Company's tax-exempt investment income on securities, loans and company-owned life insurance, income tax credits generated from affordable housing projects, and income generated by subsidiaries domiciled in a state with no state or local income tax.

FINANCIAL CONDITION

Total assets for the Company totaled \$5.476 billion at September 30, 2021, representing an increase of \$498.2 million, or 13% on an annualized basis, compared with December 31, 2020. The increase in total assets during the first nine months of 2021 compared with December 31, 2020 was primarily driven by increased levels of deposits.

Securities available for sale increased \$478.4 million as of September 30, 2021 compared with year-end 2020. The increase in the securities portfolio in the first nine months of 2021 was the result of increased levels of deposits.

September 30, 2021 total loans declined \$79.0 million, or 3% on an annualized basis, compared with December 31, 2020. The decline in total loans at September 30, 2021 compared with year-end 2020 was primarily due to a decrease in PPP loans and, to a lesser degree, the sale of commercial and agricultural loans as a part of the branch sale completed during the third quarter of 2021. Net PPP loans totaled \$68.0 million (\$71.2 million principal balance and \$3.2 million of net deferred fees) at September 30, 2021 compared with \$182.0 million in net PPP loans at December 31, 2020. As of year-end 2020 the balances of loans sold as a part of the branch sale totaled \$8.4 million.

Excluding PPP loans and the loans sold as a part of the branch sale, total loans increased \$43.3 million, or 2% on an annualized basis, at September 30, 2021 compared with year-end 2020. Commercial real estate loans increased approximately \$67.3 million (excluding loans sold as part of the branch sale) during the first nine months of 2021 compared with year-end 2020 while commercial and industrial loans declined \$11.7 million (excluding PPP loans and loans sold as part of branch sale) largely due to reduced utilization of lines of credit. During the first nine months of 2021 compared with year-end 2020, agricultural loans declined \$26.8 million largely as a result of a reduction in the utilization of lines of credit.

Lower levels of commercial, agricultural and home equity lines of credit balances resulting from lower line utilization rates during the first nine months of 2021 compared to year-end 2020 has been the primary driver to muted overall loan portfolio

growth excluding PPP loans. Outstanding commercial lines of credit balances totaled \$138.9 million, or 27% utilization, at September 30, 2021 compared to \$161.0 million, or 32% utilization, at year-end 2020. Outstanding agricultural lines of credit balances and utilization totaled \$78.5 million, or 50% utilization, at September 30, 2021 compared to \$92.2 million, or 59% utilization, at year-end 2020. Outstanding home equity lines of credit balances totaled \$216.1 million, or 41% utilization, at September 30, 2021 compared to \$218.2 million, or 44% utilization, at year-end 2020.

End of Period Loan Balances: (dollars in thousands)	September 30, 2021	December 31, 2020	Current Period Change
Commercial and Industrial Loans and Leases	\$ 566,769	\$ 694,437	\$ (127,668)
Commercial Real Estate Loans	1,528,493	1,467,397	61,096
Agricultural Loans	349,321	376,186	(26,865)
Home Equity and Consumer Loans	299,000	297,702	1,298
Residential Mortgage Loans	269,406	256,276	13,130
Total Loans	\$ 3,012,989	\$ 3,091,998	\$ (79,009)

The following table indicates the breakdown of the allowance for credit losses for the periods indicated (dollars in thousands):

	September 30, 2021	December 31, 2020
Commercial and Industrial Loans and Leases	\$ 8,257	\$ 6,645
Commercial Real Estate Loans	21,392	29,878
Agricultural Loans	4,695	6,756
Home Equity and Consumer Loans	1,692	1,636
Residential Mortgage Loans	1,762	1,944
Unallocated	—	—
Total Allowance for Credit Losses	\$ 37,798	\$ 46,859

The Company's allowance for credit losses totaled \$37.8 million at September 30, 2021 compared to \$46.9 million at year-end 2020. The allowance for credit losses represented 1.26% of period-end loans at September 30, 2021 compared with 1.52% of period-end loans at December 31, 2020.

The Company adopted ASU No. 2016-13, Financial Instruments - Credit Losses (Topic 326) ("CECL") on January 1, 2020. Under the CECL model, certain acquired loans continue to carry a fair value discount as well as an allowance for credit losses. As of September 30, 2021, the Company held net discounts on acquired loans of \$5.5 million.

The allowance for credit losses declined during the nine months ended September 30, 2021, as a result of the Company recording a negative \$8.5 million provision for credit losses while recording modest net charge-offs. During 2020, the allowance for credit losses increased through elevated provision for credit losses primarily due to the developments during 2020 related to the COVID-19 pandemic and the resulting impact on the economic assumptions used in the CECL model.

In response to requests from borrowers who had experienced pandemic-related business or personal cash flow interruptions, and in accordance with regulatory guidance, the Company began making short-term loan modifications involving both partial and full payment deferrals in April 2020. As of September 30, 2021, the Company has just one commercial real estate loan, in the principal amount of \$3.5 million, with a payment modification that is still in effect, with such credit relationship making full interest payments.

The Company tracks lending exposure by industry classification to determine potential risk associated with industry concentrations, if any, that could lead to additional credit loss exposure. As a result of the COVID-19 pandemic, the Company initially identified loan segments that could represent a potentially higher level of credit risk, as many of these customers may have incurred a significant negative impact to their businesses as a result of governmental stay-at-home orders and travel restrictions. At September 30, 2021, the Company had the following exposure to these potentially sensitive COVID-19 identified loan segments:

Industry Segment (dollars in thousands)	Number of Loans	Outstanding Balance	% of Total Loans (excludes PPP Loans)	% of Industry Segment Under Deferral
Lodging / Hotels	39	\$ 121,612	4.1 %	2.9 %
Retail Shopping / Strip Centers	64	98,651	3.4 %	— %
Restaurants	173	53,662	1.8 %	— %

The following is an analysis of the Company's non-performing assets at September 30, 2021 and December 31, 2020:

Non-performing Assets: (dollars in thousands)	September 30, 2021	December 31, 2020
Non-accrual Loans	\$ 18,434	\$ 21,507
Past Due Loans (90 days or more)	—	—
Total Non-performing Loans	18,434	21,507
Other Real Estate	112	325
Total Non-performing Assets	\$ 18,546	\$ 21,832
Restructured Loans	\$ 106	\$ 111
Non-performing Loans to Total Loans	0.61 %	0.70 %
Allowance for Credit Loss to Non-performing Loans	205.05 %	217.88 %

The following table presents non-accrual loans and loans past due 90 days or more still on accrual by class of loans:

	Non-Accrual Loans		Loans Past Due 90 Days or More & Still Accruing	
	September 30, 2021	December 31, 2020	September 30, 2021	December 31, 2020
Commercial and Industrial Loans and Leases	\$ 13,852	\$ 8,133	\$ —	\$ —
Commercial Real Estate Loans	2,766	10,188	—	—
Agricultural Loans	1,174	1,915	—	—
Home Equity Loans	22	271	—	—
Consumer Loans	78	170	—	—
Residential Mortgage Loans	542	830	—	—
Total	\$ 18,434	\$ 21,507	\$ —	\$ —

Non-performing assets totaled \$18.5 million at September 30, 2021 compared to \$21.8 million at December 31, 2020. Non-performing assets represented 0.34% of total assets at September 30, 2021 and 0.44% at December 31, 2020. Non-performing loans totaled \$18.4 million at September 30, 2021 compared to \$21.5 million at December 31, 2020. Non-performing loans represented 0.61% of total loans at September 30, 2021 compared to 0.70% at December 31, 2020.

The increase in the level of commercial and industrial non-performing loans at September 30, 2021 compared with year-end 2020 was primarily attributable to a single commercial manufacturing relationship that totaled approximately \$8.7 million that was moved to non-performing status in the third quarter of 2021. The decline in the level of commercial real estate non-performing loans at September 30, 2021 compared with year-end 2020 was largely attributable to the payoff of a commercial real estate credit in the lodging industry that was in non-accrual status during the third quarter of 2021.

September 30, 2021 total deposits increased \$486.4 million, or 16% on an annualized basis, compared to December 31, 2020. The increase in total deposits at September 30, 2021 compared with year-end 2020 was impacted by participation in the PPP, continued stimulus payments provided by the federal government and general inflows of customer deposits.

End of Period Deposit Balances: (dollars in thousands)	September 30, 2021	December 31, 2020	Current Period Change
Non-interest-bearing Demand Deposits	\$ 1,453,197	\$ 1,183,442	\$ 269,755
Interest-bearing Demand, Savings, & Money Market Accounts	2,762,328	2,428,636	333,692
Time Deposits < \$100,000	214,359	255,941	(41,582)
Time Deposits of \$100,000 or more	163,067	238,511	(75,444)
Total Deposits	\$ 4,592,951	\$ 4,106,530	\$ 486,421

Capital Resources:

As of September 30, 2021, shareholders' equity increased by \$25.4 million to \$650.1 million compared with \$624.7 million at year-end 2020. The increase in shareholders' equity was attributable to increased retained earnings of \$48.2 million due to net income of \$64.9 million during the first nine months of 2021 which was partially offset by the payment of \$16.7 million in shareholder dividends. Partially mitigating the increase in retained earnings was a decline in accumulated other comprehensive income of \$24.1 million related to the decrease in value of the Company's available-for-sale securities portfolio.

Shareholders' equity represented 11.9% of total assets at September 30, 2021 and 12.6% of total assets at December 31, 2020. Shareholders' equity included \$128.3 million of goodwill and other intangible assets at September 30, 2021 compared to \$130.9 million of goodwill and other intangible assets at December 31, 2020.

On January 25, 2021, the Company's Board of Directors approved a plan to repurchase up to one million shares of the Company's outstanding common stock. On a share basis, the amount of common stock subject to the repurchase plan represented approximately 4% of the Company's outstanding shares on the date it was approved. The Company is not obligated to purchase any shares under the plan, and the plan may be discontinued at any time. The actual timing, number and share price of shares purchased under the repurchase plan will be determined by the Company at its discretion and will depend upon such factors as the market price of the stock, general market and economic conditions and applicable legal requirements. At the time it approved the new plan, the Board also terminated a similar plan that had been adopted in January 2020. At the time of its termination, the Company had been authorized to purchase up to 778,088 shares of common stock under the 2020 repurchase plan. The Company has not repurchased any shares of common stock under the 2021 repurchase plan.

Federal banking regulations provide guidelines for determining the capital adequacy of bank holding companies and banks. These guidelines provide for a more narrow definition of core capital and assign a measure of risk to the various categories of assets. The Company is required to maintain minimum levels of capital in proportion to total risk-weighted assets and off-balance sheet exposures.

The current risk-based capital rules, as adopted by federal banking regulators, are based upon guidelines developed by the Basel Committee on Banking Supervision and reflect various requirements of the Dodd-Frank Act (the "Basel III Rules"). The Basel III Rules require banking organizations to, among other things, maintain a minimum ratio of Total Capital to risk-weighted assets, a minimum ratio of Tier 1 Capital to risk-weighted assets, a minimum ratio of "Common Equity Tier 1 Capital" to risk-weighted assets, and a minimum leverage ratio (calculated as the ratio of Tier 1 Capital to adjusted average consolidated assets). In addition, under the Basel III Rules, in order to avoid limitations on capital distributions, including dividend payments, the Company is required to maintain a 2.5% capital conservation buffer above the adequately capitalized regulatory capital ratios. At September 30, 2021, the capital levels for the Company and its subsidiary bank remained well in excess of the minimum amounts needed for capital adequacy purposes and the Bank's capital levels met the necessary requirements to be considered well-capitalized.

The table below presents the Company's consolidated and the subsidiary bank's capital ratios under regulatory guidelines:

	9/30/2021 Ratio	12/31/2020 Ratio	Minimum for Capital Adequacy Purposes ⁽¹⁾	Well-Capitalized Guidelines
Total Capital (to Risk Weighted Assets)				
Consolidated	16.21 %	15.86 %	8.00 %	N/A
Bank	13.69 %	14.00 %	8.00 %	10.00 %
Tier 1 (Core) Capital (to Risk Weighted Assets)				
Consolidated	14.56 %	13.93 %	6.00 %	N/A
Bank	13.13 %	13.21 %	6.00 %	8.00 %
Common Tier 1, (CET 1) Capital Ratio (to Risk Weighted Assets)				
Consolidated	14.13 %	13.48 %	4.50 %	N/A
Bank	13.13 %	13.21 %	4.50 %	6.50 %
Tier 1 Capital (to Average Assets)				
Consolidated	10.16 %	10.07 %	4.00 %	N/A
Bank	9.16 %	9.56 %	4.00 %	5.00 %

⁽¹⁾ Excludes capital conservation buffer.

In December 2018, the federal banking regulators approved a final rule to address changes to credit loss accounting under GAAP, including banking organizations' implementation of CECL. The final rule provides banking organizations the option to phase in over a three-year period the day-one adverse effects on regulatory capital that may result from the adoption of the new accounting standard. On March 27, 2020, in an action related to the CARES Act, the federal banking regulators announced an interim final rule to delay the estimated impact on regulatory capital stemming from the implementation of CECL. The interim final rule, which was finalized effective September 30, 2020, maintains the three-year transition option in the previous rule and provides banks the option to delay for two years an estimate of CECL's effect on regulatory capital, relative to the incurred loss methodology's effect on regulatory capital, followed by a three-year transition period (five-year transition option). The Company has elected to adopt the five-year transition option.

On April 9, 2020, federal banking regulators issued an interim final rule to modify the Basel III regulatory capital rules applicable to banking organizations to allow those organizations participating in the PPP to neutralize the regulatory capital effects of participating in the program. Specifically, the agencies have clarified that banking organizations, including the Company and the Bank, are permitted to assign a zero percent risk weight to PPP loans for purposes of determining risk-weighted assets and risk-based capital ratios. Additionally, in order to facilitate use of the Paycheck Protection Program Liquidity Facility (the "PPPL Facility"), the agencies further clarified that, for purposes of determining leverage ratios, a banking organization is permitted to exclude from total average assets PPP loans that have been pledged as collateral for a PPPL Facility.

Liquidity:

The Consolidated Statement of Cash Flows details the elements of changes in the Company's consolidated cash and cash equivalents. Total cash and cash equivalents increased \$103.0 million during the nine months ended September 30, 2021 ending at \$448.7 million. During the nine months ended September 30, 2021, operating activities resulted in net cash inflows of \$74.6 million. Investing activities resulted in net cash outflows of \$450.7 million during the nine months ended September 30, 2021 primarily resulting from the investment of excess liquidity into the available for sale securities portfolio. Financing activities resulted in net cash inflows for the nine months ended September 30, 2021 of \$479.1 million primarily related to growth in the Company's deposit portfolio.

The parent company is a corporation separate and distinct from its bank and other subsidiaries. The Company uses funds at the parent-company level to pay dividends to its shareholders, to acquire or make other investments in other businesses or their securities or assets, to repurchase its stock from time to time, and for other general corporate purposes including debt service. The parent company does not have access at the parent-company level to the deposits and certain other sources of funds that are available to its bank subsidiary to support its operations. Instead, the parent company has historically derived most of its revenues from dividends paid to the parent company by its bank subsidiary. The Company's banking subsidiary is subject to statutory restrictions on its ability to pay dividends to the parent company. The parent company has in recent years supplemented the dividends received from its subsidiaries with borrowings. As of September 30, 2021, the parent company had approximately \$73.9 million of cash and cash equivalents available to meet its cash flow needs.

FORWARD-LOOKING STATEMENTS AND ASSOCIATED RISKS

The Company from time to time in its oral and written communications makes statements relating to its expectations regarding the future. These types of statements are considered "forward-looking statements" within the meaning of the Private Securities Litigation Reform Act of 1995. The Company may include forward-looking statements in filings with the Securities and Exchange Commission ("SEC"), such as this Form 10-Q, in other written materials, and in oral statements made by senior management to analysts, investors, representatives of the media, and others. Such forward looking statements can include statements about the Company's net interest income or net interest margin; its adequacy of allowance for credit losses, levels of provisions for credit losses, and the quality of the Company's loans, investment securities and other assets; simulations of changes in interest rates; expected results from mergers with or acquisitions of other businesses; litigation results; tax estimates and recognition; dividend policy; parent company cash resources and cash requirements, and parent company capital resources; estimated cost savings, plans and objectives for future operations; and expectations about the Company's financial and business performance and other business matters as well as economic and market conditions and trends. They often can be identified by the use of words like "plan," "expect," "can," "might," "may," "will," "would," "could," "should," "intend," "project," "estimate," "believe" or "anticipate," or similar expressions.

Forward-looking statements speak only as of the date they are made, and the Company undertakes no obligation to update any forward-looking statement to reflect events or circumstances after the date on which the forward-looking statement is made.

Readers are cautioned that, by their nature, all forward-looking statements are based on assumptions and are subject to risks, uncertainties, and other factors. Actual results may differ materially and adversely from the expectations of the Company that are expressed or implied by any forward-looking statement. The discussions in this Item 2 list some of the factors that could cause the Company's actual results to vary materially from those expressed or implied by any forward-looking statements. Other 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:

- the unknown future direction of interest rates and the timing and magnitude of any changes in interest rates;
- changes in competitive conditions;
- the introduction, withdrawal, success and timing of asset/liability management strategies or of mergers and acquisitions and other business initiatives and strategies;
- changes in customer borrowing, repayment, investment and deposit practices;
- changes in fiscal, monetary and tax policies;
- changes in financial and capital markets;
- deterioration in general economic conditions, either nationally or locally, resulting in, among other things, credit quality deterioration;
- the severity and duration of the COVID-19 pandemic and its impact on general economic and financial market conditions and our business, results of operations, and financial condition;
- our participation as a lender in the PPP;
- capital management activities, including possible future sales of new securities, or possible repurchases or redemptions by the Company of outstanding debt or equity securities;
- factors driving impairment charges on investments;
- the impact, extent and timing of technological changes;
- potential cyber-attacks, information security breaches and other criminal activities;
- litigation liabilities, including related costs, expenses, settlements and judgments, or the outcome of matters before regulatory agencies, whether pending or commencing in the future;
- actions of the Federal Reserve Board;
- changes in accounting principles and interpretations;
- potential increases of federal deposit insurance premium expense, and possible future special assessments of FDIC premiums, either industry wide or specific to the Company's banking subsidiary;
- actions of the regulatory authorities under the Dodd-Frank Wall Street Reform and Consumer Protection Act (the "Dodd-Frank Act") and the Federal Deposit Insurance Act and other possible legislative and regulatory actions and reforms;
- impacts resulting from possible amendments or revisions to the Dodd-Frank Act and the regulations promulgated thereunder, or to Consumer Financial Protection Bureau rules and regulations;
- the continued availability of earnings and excess capital sufficient for the lawful and prudent declaration and payment of cash dividends; and
- with respect to the proposed merger with CUB: (i) failure to obtain necessary regulatory approvals when expected or at all (and the risk that such approvals may result in the imposition of conditions that could adversely affect the combined company or the expected benefits of the transaction), or the failure of either company to satisfy any of the other closing conditions to the transaction on a timely basis or at all; (ii) the occurrence of any event, change or other circumstances that could give rise to the right of one or both of the parties to terminate the merger agreement; and (iii) the possibility that the anticipated benefits of the transaction, including anticipated cost savings and strategic gains, are not realized when expected or at all, including as a result of the impact of, or problems arising from, the integration of the two companies, unexpected credit quality problems of the acquired loans or other assets, or unexpected attrition of the customer base of the acquired institution or branches, or as a result of the strength of the economy, competitive factors in the areas where the Company and CUB do business, or as a result of other unexpected factors or events.

Such statements reflect our views with respect to future events and are subject to these and other risks, uncertainties and assumptions relating to the operations, results of operations, growth strategy and liquidity of the Company. Readers are cautioned not to place undue reliance on these forward-looking statements.

Investors should consider these risks, uncertainties, and other factors, in addition to those mentioned by the Company in its Annual Report on Form 10-K for its fiscal year ended December 31, 2020, this Quarterly Report on Form 10-Q, and other SEC filings from time to time, when considering any forward-looking statement.

Item 3. Quantitative and Qualitative Disclosures About Market Risk

The Company's exposure to market risk is reviewed on a regular basis by the Asset/Liability Committee and Boards of Directors of the parent company and its subsidiary bank. Primary market risks which impact the Company's operations are liquidity risk and interest rate risk.

The liquidity of the parent company is dependent upon the receipt of dividends from its subsidiary bank, which is subject to certain regulatory limitations. The Bank's source of funding is predominately core deposits, maturities of securities, repayments of loan principal and interest, federal funds purchased, securities sold under agreements to repurchase and borrowings from the Federal Home Loan Bank.

The Company monitors interest rate risk by the use of computer simulation modeling to estimate the potential impact on its net interest income under various interest rate scenarios, and by estimating its static interest rate sensitivity position. Another method by which the Company's interest rate risk position can be estimated is by computing estimated changes in its net portfolio value ("NPV"). This method estimates interest rate risk exposure from movements in interest rates by using interest rate sensitivity analysis to determine the change in the NPV of discounted cash flows from assets and liabilities. NPV represents the market value of portfolio equity and is equal to the estimated market value of assets minus the estimated market value of liabilities.

Computations for measuring both net interest income and NPV are based on a number of assumptions, including the relative levels of market interest rates and prepayments in mortgage loans and certain types of investments. These computations do not contemplate any actions management may undertake in response to changes in interest rates, and should not be relied upon as indicative of actual results. In addition, certain shortcomings are inherent in the method of computing both net interest income and NPV. Should interest rates remain or decrease below current levels, the proportion of adjustable rate loans could decrease in future periods due to refinancing activity. In the event of an interest rate change, prepayment levels would likely be different from those assumed in the modeling. Lastly, the ability of many borrowers to repay their adjustable rate debt may decline during a rising interest rate environment.

The Company from time to time utilizes derivatives to manage interest rate risk. Management continuously evaluates the merits of such interest rate risk products but does not anticipate the use of such products to become a major part of the Company's risk management strategy.

The table below provides an assessment of the risk to net interest income over the next 12 months in the event of a sudden and sustained 1% and 2% increase and decrease in prevailing interest rates (dollars in thousands).

Interest Rate Sensitivity as of September 30, 2021 - Net Interest Income

Changes in Rates	Net Interest Income	
	Amount	% Change
+2%	\$ 149,636	0.16 %
+1%	148,974	(0.29)%
Base	149,402	—
-1%	144,706	(3.14)%
-2%	142,872	(4.37)%

The above table is a measurement of the Company's net interest income at risk, assuming a static balance sheet as of September 30, 2021 and instantaneous parallel changes in interest rates. The Company also monitors interest rate risk under other scenarios including a more gradual movement in market interest rates. This type of scenario can at times produce different modeling results in measuring interest rate risk sensitivity.

The table below provides an assessment of the risk to NPV in the event of a sudden and sustained 1% and 2% increase and decrease in prevailing interest rates (dollars in thousands).

Interest Rate Sensitivity as of September 30, 2021 - Net Portfolio Value

Changes in Rates	Net Portfolio Value		Net Portfolio Value as a % of Present Value of Assets	
	Amount	% Change	NPV Ratio	Change
+2%	\$ 574,920	(8.19)%	11.37 %	(31) b.p.
+1%	604,406	(3.48)%	11.61 %	(7) b.p.
Base	626,210	—	11.68 %	—
-1%	608,065	(2.90)%	11.01 %	(67) b.p.
-2%	508,443	(18.81)%	9.18 %	(250) b.p.

This Item 3 includes forward-looking statements. See “Forward-looking Statements and Associated Risks” included in Part I, Item 2 of this Report for a discussion of certain factors that could cause the Company’s actual exposure to market risk to vary materially from that expressed or implied above. These factors include possible changes in economic conditions; interest rate fluctuations, competitive product and pricing pressures within the Company’s markets; and equity and fixed income market fluctuations. Actual experience may also vary materially to the extent that the Company’s assumptions described above prove to be inaccurate.

Item 4. Controls and Procedures

As of September 30, 2021, the Company carried out an evaluation, under the supervision and with the participation of its principal executive officer and principal financial officer, of the effectiveness of the design and operation of its disclosure controls and procedures. Based on this evaluation, the Company’s principal executive officer and principal financial officer concluded that the Company’s disclosure controls and procedures were, as of that date, effective in timely alerting them to material information required to be included in the Company’s periodic reports filed with the Securities and Exchange Commission. There are inherent limitations to the effectiveness of systems of disclosure controls and procedures, including the possibility of human error and the circumvention or overriding of the controls and procedures. Accordingly, even effective systems of disclosure controls and procedures can provide only reasonable assurances of achieving their control objectives.

There was no change in the Company’s internal control over financial reporting that occurred during the Company’s third fiscal quarter of 2021 that has materially affected, or is reasonably likely to materially affect, the Company’s internal control over financial reporting.

PART II. OTHER INFORMATION

Item 1. Legal Proceedings

In July 2020, the Company was named in a putative class action lawsuit filed in Marion County, Indiana Superior Court challenging the Company's checking account practices associated with its assessment of overdraft fees for certain debit card transactions. The relief sought by the plaintiff includes restitution, other monetary damages, and injunctive and declaratory relief. The plaintiff also seeks to have the case certified by the Court as a class action on behalf all citizens of Indiana who are checking account holders at German American Bank and who were assessed overdraft fees on certain debit card transactions. The Company believes the plaintiff's claims are unfounded and has vehemently defended against them, including by filing a motion to dismiss the plaintiff's amended complaint. On August 25, 2021, while the Company's motion to dismiss remained pending, the parties participated in a mediation conference. The mediation conference resulted in a settlement in principle, subject to execution of a definitive settlement agreement which would be subject to the Court's approval. On October 21, 2021, the Company executed a Settlement Agreement and Release, pursuant to which the Company would pay the amount of \$3,050,000 in full and complete settlement of plaintiff's putative class action. The Settlement Agreement and Release has not yet been submitted to and remains subject to the Court's approval.

There are no other pending legal proceedings, other than routine litigation incidental to the business of the Company's subsidiaries, to which the Company or any of its subsidiaries is a party or of which any of their property is the subject.

Item 1A. Risk Factors

There have been no material changes to the risk factors previously disclosed in German American Bancorp, Inc.'s Annual Report on Form 10-K for the year ended December 31, 2020.

Item 2. Unregistered Sales of Equity Securities and Use of Proceeds

Issuer Purchases of Equity Securities

The following table sets forth information regarding the Company's purchases of its common shares during each of the three months ended September 30, 2021.

Period	Total Number of Shares (or Units) Purchased	Average Price Paid Per Share (or Unit)	Total Number of Shares (or Units) Purchased as Part of Publicly Announced Plans or Programs ⁽¹⁾	Maximum Number (or Approximate Dollar Value) of Shares (or Units) that May Yet Be Purchased under the Plans or Programs ⁽¹⁾
July 2021	—	—	—	1,000,000
August 2021	—	—	—	1,000,000
September 2021	—	—	—	1,000,000
Total	—	—	—	—

⁽¹⁾ On January 25, 2021, the Company's Board of Directors approved a plan to repurchase up to 1.0 million shares of the Company's outstanding common stock. On a share basis, the amount of common stock subject to the repurchase plan represented approximately 4% of the Company's outstanding shares on the date it was approved. The Company is not obligated to purchase any shares under the plan, and the plan may be discontinued at any time. The actual timing, number and share price of shares purchased under the repurchase plan will be determined by the Company at its discretion and will depend upon such factors as the market price of the stock, general market and economic conditions and applicable legal requirements. The Company has not repurchased any shares of common stock under the 2021 repurchase plan.

Item 3. Defaults Upon Senior Securities

None.

Item 4. Mine Safety Disclosures

Not applicable.

Item 5. Other Information

None.

Item 6. Exhibits

The following exhibits are included with this Report or incorporated herein by reference.

Exhibit No.	Description
<u>2.1*</u>	<u>Agreement and Plan of Reorganization by and among German American Bancorp, Inc., German American Bank, Citizens Union Bancorp of Shelbyville, Inc. and Citizens Union Bank of Shelbyville, Inc., dated as of September 20, 2021, is incorporated by reference to Exhibit 2.1 of the Registrant's Current Report on Form 8-K filed September 21, 2021 (SEC File No. 001-15877).</u>
<u>3.1</u>	<u>Amended and Restated Articles of Incorporation of German American Bancorp, Inc., are incorporated by reference to Exhibit 3.1 of the Registrant's Current Report on Form 8-K filed May 26, 2020 (SEC File No. 001-15877).</u>
<u>3.2</u>	<u>Amended and Restated Bylaws of German American Bancorp, Inc. are incorporated by reference to Exhibit 3.1 of the Registrant's Current Report on Form 8-K filed July 1, 2020 (SEC File No. 001-15877).</u>
<u>4.1</u>	<u>Terms of Common Shares and Preferred Shares of the Registrant (included in Restatement of Articles of Incorporation) are incorporated by reference to Exhibit 3.1 to the Registrant's Current Report on Form 8-K filed May 26, 2020 (SEC File No. 001-15877).</u>
<u>4.2</u>	<u>Specimen stock certificate for Common Shares of the Registrant is incorporated by reference to Exhibit 99.1 to the Registrant's Current Report on Form 8-K filed October 21, 2010 (SEC File No. 001-15877).</u>
<u>4.3</u>	<u>Indenture, dated as of June 25, 2019, by and between German American Bancorp, Inc. and U.S. Bank National Association, as trustee, is incorporated by reference to Exhibit 4.1 of the Registrant's Current Report on Form 8-K filed June 25, 2019 (SEC File No. 001-15877).</u>
<u>4.4</u>	<u>Form of 4.50% Fixed-to-Floating Subordinated Note due 2029 of German American Bancorp, Inc. is incorporated by reference to Exhibit 4.2 of the Registrant's Current Report on Form 8-K filed June 25, 2019 (SEC File No. 001-15877).</u>
<u>10.1</u>	<u>Voting Agreement, dated as of September 20, 2021, among German American Bancorp, Inc. and each member of the Board of Directors of Citizens Union Bancorp of Shelbyville, Inc. is incorporated by reference to Exhibit 10.1 of the Registrant's Current Report on Form 8-K filed September 21, 2021 (SEC File No. 001-15877).</u>
<u>31.1+</u>	<u>Sarbanes-Oxley Act of 2002, Section 302 Certification for Chairman of the Board and Chief Executive Officer.</u>
<u>31.2+</u>	<u>Sarbanes-Oxley Act of 2002, Section 302 Certification for Executive Vice President and Chief Financial Officer.</u>
<u>32.1++</u>	<u>Sarbanes-Oxley Act of 2002, Section 906 Certification for Chairman of the Board and Chief Executive Officer.</u>
<u>32.2++</u>	<u>Sarbanes-Oxley Act of 2002, Section 906 Certification for Executive Vice President and Chief Financial Officer.</u>
101.INS+	Inline XBRL Instance Document (The instance document does not appear in the Interactive Data File because its XBRL tags are embedded within the Inline XBRL document.)
101.SCH+	Inline XBRL Taxonomy Extension Schema Document
101.CAL+	Inline XBRL Taxonomy Extension Calculation Linkbase Document
101.DEF+	Inline XBRL Taxonomy Extension Definition Linkbase Document
101.LAB+	Inline XBRL Taxonomy Extension Label Linkbase Document
101.PRE+	Inline XBRL Taxonomy Extension Presentation Linkbase Document
104	Cover Page Interactive Data File (formatted as Inline XBRL and contained in Exhibit 101).

Note: No long-term debt instrument issued by the Registrant exceeds 10% of consolidated total assets or is registered. In accordance with paragraph 4 (iii) of Item 601(b) of Regulation S-K, the Registrant will furnish the Securities and Exchange Commission copies of long-term debt instruments and related agreements upon request.

* Schedules to the subject agreement have been omitted pursuant to Item 601(b)(2) of Regulation S-K. A copy of any omitted schedule will be furnished to the Securities and Exchange Commission upon request.

+Filed with this Report (other than through incorporation by reference to other disclosures or exhibits).

++Furnished with this Report.

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.

GERMAN AMERICAN BANCORP, INC.

Date: November 9, 2021

By: /s/Mark A. Schroeder

Mark A. Schroeder
Chairman and Chief Executive Officer
(Principal Executive Officer)

Date: November 9, 2021

By: /s/Bradley M. Rust

Bradley M. Rust
Senior Executive Vice President and Chief Financial Officer
(Principal Financial and Accounting Officer)

Sarbanes-Oxley Act of 2002, Section 302 Certification for Chairman and Chief Executive Officer

I, Mark A. Schroeder, Chairman and Chief Executive Officer of German American Bancorp, Inc., certify that:

1. I have reviewed this Quarterly Report on Form 10-Q of German American Bancorp, Inc. (the “registrant”):
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;
4. The registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:
 - a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
 - b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;
 - c) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
 - d) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and
5. The registrant's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):
 - a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and
 - b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

November 9, 2021

Date

/s/ Mark A. Schroeder

Mark A. Schroeder
Chairman and Chief Executive Officer
(principal executive officer)

Sarbanes-Oxley Act of 2002, Section 302 Certification for Senior Executive Vice President and Chief Financial Officer

I, Bradley M. Rust, Senior Executive Vice President and Chief Financial Officer of German American Bancorp, Inc. certify that:

1. I have reviewed this Quarterly Report on Form 10-Q of German American Bancorp, Inc. (the "registrant"):
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;
4. The registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:
 - a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
 - b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;
 - c) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
 - d) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and
5. The registrant's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):
 - a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and
 - b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

November 9, 2021

Date

/s/ Bradley M. Rust

Bradley M. Rust

Senior Executive Vice President and Chief Financial Officer

(principal accounting officer and principal financial officer)

Sarbanes-Oxley Act of 2002, Section 906 Certification for Chairman and Chief Executive Officer

I, Mark A. Schroeder, Chairman and Chief Executive Officer of German American Bancorp, Inc. certify, pursuant to Section 906 of the Sarbanes-Oxley Act of 2002 (18 U.S.C. 1350), that:

1. The Quarterly Report on Form 10-Q for the quarter ended September 30, 2021 (the "Periodic Report"), which this statement accompanies, fully complies with the requirements of Section 13(a) of the Securities Exchange Act of 1934 (15 U.S.C. 78m); and
2. Information contained in the Periodic Report fairly presents, in all material respects, the financial condition and results of operations of German American Bancorp, Inc.

This certificate is being furnished solely for purposes of Section 906 and is not being filed as part of the Periodic Report.

November 9, 2021

Date

/s/ Mark A. Schroeder

Mark A. Schroeder
Chairman and Chief Executive Officer
(principal executive officer)

Sarbanes-Oxley Act of 2002, Section 906 Certification for Senior Executive Vice President and Chief Financial Officer

I, Bradley M. Rust, Senior Executive Vice President and Chief Financial Officer of German American Bancorp, Inc. certify, pursuant to Section 906 of the Sarbanes-Oxley Act of 2002 (18 U.S.C. 1350), that:

1. The Quarterly Report on Form 10-Q for the quarter ended September 30, 2021 (the “Periodic Report”), which this statement accompanies, fully complies with the requirements of Section 13(a) of the Securities Exchange Act of 1934 (15 U.S.C. 78m); and
2. Information contained in the Periodic Report fairly presents, in all material respects, the financial condition and results of operations of German American Bancorp, Inc.

This certificate is being furnished solely for purposes of Section 906 and is not being filed as part of the Periodic Report.

November 9, 2021

Date

/s/ Bradley M. Rust

Bradley M. Rust

Senior Executive Vice President and Chief Financial Officer

(principal accounting officer and principal financial officer)