

ENTERPRISE FINANCIAL SERVICES CORP
Form 10-Q
October 27, 2017

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D. C. 20549

FORM 10-Q

Quarterly Report Pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934
For the quarterly period ended September 30, 2017.

Transition Report Pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934
For the transition period from _____ to _____

Commission file number 001-15373

ENTERPRISE FINANCIAL SERVICES CORP

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

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

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

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

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

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

As of October 25, 2017, the Registrant had 23,064,850 shares of outstanding common stock, \$0.01 par value.

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

ENTERPRISE FINANCIAL SERVICES CORP AND SUBSIDIARIES
TABLE OF CONTENTS

	Page
PART I - FINANCIAL INFORMATION	
Item 1. Financial Statements	
Condensed Consolidated Balance Sheets (Unaudited)	<u>1</u>
Condensed Consolidated Statements of Operations (Unaudited)	<u>2</u>
Condensed Consolidated Statements of Comprehensive Income (Unaudited)	<u>3</u>
Condensed Consolidated Statements of Shareholders' Equity (Unaudited)	<u>4</u>
Condensed Consolidated Statements of Cash Flows (Unaudited)	<u>5</u>
Notes to Condensed Consolidated Financial Statements (Unaudited)	<u>6</u>
Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations	<u>30</u>
Item 3. Quantitative and Qualitative Disclosures About Market Risk	<u>52</u>
Item 4. Controls and Procedures	<u>53</u>

PART II - OTHER
INFORMATION

Item 1. Legal Proceedings 53

Item 1A. Risk Factors 53

Item 2. Unregistered Sales
of Equity Securities and 54
Use of Proceeds

Item 5. Other Information 54

Item 6. Exhibits 55

Signatures 56

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

(in thousands, except share and per share data)	September 30, 2017	December 31, 2016
Assets		
Cash and due from banks	\$ 76,777	\$ 54,288
Federal funds sold	1,155	446
Interest-bearing deposits (including \$2,949 and \$675 pledged as collateral)	105,176	144,068
Total cash and cash equivalents	183,108	198,802
Interest-bearing deposits greater than 90 days	2,645	980
Securities available for sale	603,121	460,797
Securities held to maturity	76,168	80,463
Loans held for sale	6,411	9,562
Loans	4,030,658	3,158,161
Less: Allowance for loan losses	43,191	43,409
Total loans, net	3,987,467	3,114,752
Other real estate	491	980
Other investments, at cost	29,436	14,840
Fixed assets, net	32,803	14,910
Accrued interest receivable	14,213	11,117
State tax credits held for sale (including \$1,274 and \$3,585 carried at fair value)	35,291	38,071
Goodwill	117,345	30,334
Intangible assets, net	11,745	2,151
Other assets	131,244	103,569
Total assets	\$ 5,231,488	\$ 4,081,328
Liabilities and Shareholders' Equity		
Demand deposits	\$ 1,047,910	\$ 866,756
Interest-bearing transaction accounts	814,338	731,539
Money market accounts	1,375,844	1,050,472
Savings	203,923	111,435
Certificates of deposit:		
Brokered	170,701	117,145
Other	446,495	356,014
Total deposits	4,059,211	3,233,361
Subordinated debentures and notes (net of debt issuance cost of \$1,169 and \$1,267)	118,093	105,540
Federal Home Loan Bank advances	248,868	—
Other borrowings	209,104	276,980
Notes payable	10,000	—
Accrued interest payable	2,007	1,105
Other liabilities	37,869	77,244
Total liabilities	4,685,152	3,694,230
Shareholders' equity:		
Preferred stock, \$0.01 par value; 5,000,000 shares authorized; 0 shares issued and outstanding	—	—
Common stock, \$0.01 par value; 30,000,000 shares authorized; 23,754,814 and 20,306,353 shares issued	237	203

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

Treasury stock, at cost; 691,673 and 261,718 shares, respectively	(23,268	) (6,632)
Additional paid in capital	349,485	213,078	
Retained earnings	220,371	182,190	
Accumulated other comprehensive loss	(489	) (1,741)
Total shareholders' equity	546,336	387,098	
Total liabilities and shareholders' equity	\$ 5,231,488	\$ 4,081,328	
See accompanying notes to consolidated financial statements.			

1

ENTERPRISE FINANCIAL SERVICES CORP AND SUBSIDIARIES

Condensed Consolidated Statements of Operations (Unaudited)

(in thousands, except per share data)	Three months ended September 30,		Nine months ended September 30,	
	2017	2016	2017	2016
Interest income:				
Interest and fees on loans	\$48,020	\$34,442	\$135,253	\$101,233
Interest on debt securities:				
Taxable	3,855	2,410	10,670	7,194
Nontaxable	294	322	984	982
Interest on interest-bearing deposits	173	67	537	186
Dividends on equity securities	126	52	306	191
Total interest income	52,468	37,293	147,750	109,786
Interest expense:				
Interest-bearing transaction accounts	523	332	1,721	967
Money market accounts	2,410	1,143	5,841	3,162
Savings accounts	125	68	332	191
Certificates of deposit	1,493	1,319	4,081	3,521
Subordinated debentures and notes	1,316	369	3,768	1,078
Federal Home Loan Bank advances	832	126	1,684	499
Notes payable and other borrowings	144	106	423	327
Total interest expense	6,843	3,463	17,850	9,745
Net interest income	45,625	33,830	129,900	100,041
Provision for portfolio loan losses	2,422	3,038	7,578	4,587
Provision reversal for purchased credit impaired loan losses	—	(1,194)	(355)	(1,603)
Net interest income after provision for loan losses	43,203	31,986	122,677	97,057
Noninterest income:				
Service charges on deposit accounts	2,820	2,200	8,146	6,431
Wealth management revenue	2,062	1,694	5,949	5,000
Card services revenue	1,459	804	3,888	2,236
Gain (loss) on sale of other real estate	—	(226)	17	602
Gain on state tax credits, net	77	228	332	899
Gain on sale of investment securities	22	86	22	86
Miscellaneous income	1,932	2,190	4,928	4,776
Total noninterest income	8,372	6,976	23,282	20,030
Noninterest expense:				
Employee compensation and benefits	15,090	12,091	46,096	37,398
Occupancy	2,434	1,705	6,628	4,997
Data processing	1,389	1,150	4,828	3,441
Professional fees	922	757	2,838	2,160
FDIC and other insurance	882	780	2,356	2,241
Loan legal and other real estate expense	586	416	1,544	1,126
Merger related expenses	315	302	6,462	302
Other	5,786	3,613	16,039	11,264
Total noninterest expense	27,404	20,814	86,791	62,929
Income before income tax expense	24,171	18,148	59,168	54,158
Income tax expense	7,856	6,316	18,507	18,949

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

Net income	\$16,315	\$11,832	\$40,661	\$35,209
Earnings per common share				
Basic	\$0.70	\$0.59	\$1.77	\$1.76
Diluted	0.69	0.59	1.75	1.74

See accompanying notes to consolidated financial statements.

2

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

(in thousands)	Three months ended September 30,		Nine months ended September 30,	
	2017	2016	2017	2016
Net income	\$16,315	\$11,832	\$40,661	\$35,209
Other comprehensive income (loss), net of tax:				
Unrealized gains (losses) on investment securities arising during the period, net of income tax expense (benefit) for three months of \$(493) and \$(494), and for nine months of \$775 and \$2,795, respectively	(805)	(796)	1,265	4,503
Less: Reclassification adjustment for realized gains on sale of securities available for sale included in net income, net of income tax expense for three months of \$8 and \$33, and for nine months of \$8 and \$33, respectively	(13)	(53)	(13)	(53)
Total other comprehensive income (loss)	(818)	(849)	1,252	4,450
Total comprehensive income	\$15,497	\$10,983	\$41,913	\$39,659

See accompanying notes to consolidated financial statements.

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

(in thousands, except per share data)	Preferred Stock	Common Stock	Treasury Stock	Additional paid in capital	Retained earnings	Accumulated other comprehensive income (loss)	Total shareholders' equity
Balance December 31, 2016	\$ —	—\$ 203	\$(6,632)	\$213,078	\$182,190	\$ (1,741)	\$ 387,098
Net income	—	—	—	—	40,661	—	40,661
Reclassification adjustment for realized gain on sale of securities included in net income, net of tax	—	—	—	—	—	1,252	1,252
Total comprehensive income	—	—	—	—	40,661	1,252	41,913
Cash dividends paid on common shares, \$0.33 per share	—	—	—	—	(7,709)	—	(7,709)
Repurchase of common shares	—	—	(16,636)	—	—	—	(16,636)
Issuance under equity compensation plans, 148,597 shares, net	—	1	—	(2,574)	—	—	(2,573)
Share-based compensation	—	—	—	2,514	—	—	2,514
Shares issued in connection with acquisition of Jefferson County Bancshares, Inc.	—	33	—	141,696	—	—	141,729
Reclassification for the adoption of ASU 2016-09	—	—	—	(5,229)	5,229	—	—
Balance September 30, 2017	\$ —	—\$ 237	\$(23,268)	\$349,485	\$220,371	\$ (489)	\$ 546,336

(in thousands, except per share data)	Preferred Stock	Common Stock	Treasury Stock	Additional paid in capital	Retained earnings	Accumulated other comprehensive income (loss)	Total shareholders' equity
Balance December 31, 2015	\$ —	—\$ 201	\$(1,743)	\$210,589	\$141,564	\$ 218	\$ 350,829
Net income	—	—	—	—	35,209	—	35,209
Other comprehensive income	—	—	—	—	—	4,450	4,450
Cash dividends paid on common shares, \$0.30 per share	—	—	—	—	(6,005)	—	(6,005)
Repurchase of common shares	—	—	(4,889)	—	—	—	(4,889)
Issuance under equity compensation plans, 156,592 shares, net	—	2	—	(1,652)	—	—	(1,650)
Share-based compensation	—	—	—	2,410	—	—	2,410
Excess tax benefit related to equity compensation plans	—	—	—	744	—	—	744
Balance September 30, 2016	\$ —	—\$ 203	\$(6,632)	\$212,091	\$170,768	\$ 4,668	\$ 381,098

See accompanying notes to consolidated financial statements.

ENTERPRISE FINANCIAL SERVICES CORP AND SUBSIDIARIES

Condensed Consolidated Statements of Cash Flows (Unaudited)

Nine months ended September 30,

(in thousands, except share data)	2017		2016
Cash flows from operating activities:			
Net income	\$ 40,661		\$ 35,209
Adjustments to reconcile net income to net cash provided by operating activities			
Depreciation	2,426		1,628
Provision for loan losses	7,223		2,984
Deferred income taxes	1,239		3,881
Net amortization of debt securities	2,064		2,350
Amortization of intangible assets	1,920		718
Gain on sale of investment securities	(22)		(86)
Mortgage loans originated for sale	(115,365)		(117,975)
Proceeds from mortgage loans sold	118,798		117,639
Gain on sale of other real estate	(17)		(602)
Gain on state tax credits, net	(332)		(899)
Excess tax benefit of share-based compensation	—		(744)
Share-based compensation	2,514		2,410
Net accretion of loan discount	(3,796)		(8,165)
Changes in:			
Accrued interest receivable	(302)		(127)
Accrued interest payable	249		19
Other assets	755		(2,100)
Other liabilities	(44,398)		(8,057)
Net cash provided by operating activities	13,617		28,083
Cash flows from investing activities:			
Proceeds from JCB acquisition, net of cash purchase price	4,456		—
Net increase in loans	(201,715)		(256,706)
Proceeds from the sale of securities, available for sale	144,076		2,493
Proceeds from the paydown or maturity of securities,	126,073		46,017

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

available for sale			
Proceeds from the paydown			
or maturity of securities,	4,145		2,592
held to maturity			
Proceeds from the			
redemption of other	29,159		44,968
investments			
Proceeds from the sale of			
state tax credits held for sale	4,391		4,918
Proceeds from the sale of			
other real estate	2,513		8,072
Payments for the			
purchase/origination of:			
Available for sale debt and	(263,453	)	(71,309
equity securities)
Other investments	(45,224	)	(48,283
State tax credits held for sale	(145	)	(2,349
Fixed assets	(1,864	)	(1,284
Net cash used in investing	(197,588	)	(270,871
activities)
Cash flows from financing			
activities:			
Net increase in			
noninterest-bearing deposit	20,684		44,695
accounts			
Net increase in			
interest-bearing deposit	39,998		295,539
accounts			
Proceeds from Federal			
Home Loan Bank advances	1,394,181		1,309,000
Repayments of Federal			
Home Loan Bank advances	(1,145,681	)	(1,290,000
Proceeds from notes payable	10,000		—
Net decrease in other			
borrowings	(123,987	)	(80,304
Cash dividends paid on			
common stock	(7,709	)	(6,005
Excess tax benefit of			
share-based compensation	—		744
Payments for the repurchase			
of common stock	(16,636	)	(4,889
Issuance of common stock,			
net	(2,573	)	(1,650
Net cash provided by			
financing activities	168,277		267,130
Net increase (decrease) in			
cash and cash equivalents	(15,694	)	24,342
Cash and cash equivalents,			
beginning of period	198,802		94,157
Cash and cash equivalents,			
end of period	\$ 183,108		\$ 118,499

Supplemental disclosures of
cash flow information:

Cash paid during the period
for:

Interest	\$	16,948	\$	9,726
Income taxes		9,382		19,868

Noncash transactions:

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

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

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

See accompanying notes to consolidated financial statements.

ENTERPRISE FINANCIAL SERVICES CORP AND SUBSIDIARIES

Notes to Condensed Consolidated Financial Statements (Unaudited)

NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

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

Business and Consolidation

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

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

Basis of Financial Statement Presentation

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

Acquisitions

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

The purchase price allocation process requires an estimation of the fair values of the assets acquired and the liabilities assumed. When a business combination agreement provides for an adjustment to the cost of the combination contingent on future events, the Company includes an estimate of the acquisition-date fair value as part of the cost of the combination. To determine the fair values, the Company relies on third party valuations, such as appraisals, or internal valuations based on discounted cash flow analyses or other valuation techniques. The results of operations of the

6

acquired business are included in the Company's consolidated financial statements from the date of acquisition. Merger-related costs are costs the Company incurs to effect a business combination. In 2017, the Company changed its presentation of Merger related expenses as a separate component of Noninterest expenses on the Condensed Consolidated Statements of Operations. Merger related expenses include costs directly related to merger or acquisition activity and include legal and professional fees, system consolidation and conversion costs, and compensation costs such as severance and retention incentives for employees impacted by acquisition activity. The Company accounts for merger-related costs as expenses in the periods in which the costs are incurred and the services are received.

Purchased Credit Impaired ("PCI") Loans

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

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

Allowance for Loan Losses on PCI Loans

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

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

NOTE 2 - ACQUISITIONS

Acquisition of Jefferson County Bancshares, Inc.

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

JCB shareholders received, based on their election, cash consideration in an amount of \$85.39 per share of JCB common stock or 2.75 shares of EFSC common stock per share of JCB common stock, subject to allocation and proration procedures. Aggregate consideration at closing was 3.3 million shares of EFSC common stock and \$29.3 million cash paid to JCB shareholders and holders of JCB stock options. Based on EFSC's closing stock price of \$42.95 on February 10, 2017, the overall transaction had a value of \$171.0 million, including JCB's common stock and stock options. The Company also recognized \$6.5 million and \$1.4 million of merger related costs that were recorded in noninterest expense in the statement of operations for the nine months ended September 30, 2017, and year ended December 31, 2016, respectively.

The acquisition of JCB has been accounted for as a business combination using the acquisition method of accounting which requires assets acquired and liabilities assumed to be recognized at fair value as of the acquisition date. Goodwill of \$87.0 million arising from the acquisition consists largely of the synergies and economies of scale expected from combining the operations of JCB into Enterprise. The goodwill is assigned as part of the Company's Banking reporting unit. None of the goodwill recognized is expected to be deductible for income tax purposes.

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

(in thousands)	As Recorded by JCB	Adjustments	As Recorded by EFSC
Assets acquired:			
Cash and cash equivalents	\$ 33,739	\$ —	\$ 33,739
Interest-bearing deposits	1,715	—	1,715
Securities	148,670	—	148,670
Portfolio loans, net	685,905	(11,094)	(a) 674,811
Other real estate owned	6,762	(5,082)	(b) 1,680
Other investments	2,695	—	2,695
Fixed assets, net	21,780	(3,325)	(c) 18,455
Accrued interest receivable	2,794	—	2,794
Goodwill	7,806	(7,806)	(d) —
Other intangible assets	25	11,489	(e) 11,514
Deferred tax assets	4,634	3,991	(f) 8,625
Other assets	19,107	(296)	(g) 18,811
Total assets acquired	\$ 935,632	\$ (12,123)	\$ 923,509
Liabilities assumed:			
Deposits	\$ 764,539	\$ 629	(h) \$ 765,168
Other borrowings	55,430	681	(i) 56,111
Trust preferred securities	12,887	(382)	(j) 12,505
Accrued interest payable	653	—	653
Other liabilities	5,006	65	(k) 5,071
Total liabilities assumed	\$ 838,515	\$ 993	\$ 839,508
Net assets acquired	\$ 97,117	\$ (13,116)	\$ 84,001
Consideration paid:			
Cash			\$ 29,283
Common stock			141,729
Total consideration paid			\$ 171,012
Goodwill			\$ 87,011

Fair value adjustments based on the Company's evaluation of the acquired loan portfolio, write-off of net deferred (a) loan costs, reclassification from other real estate owned, and elimination of the allowance for loan losses recorded by JCB. The fair value discount recorded to the loan portfolio is \$24.7 million.

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

Fair value adjustments based on the Company's evaluation of the acquired premises and equipment. A decrease of (c) \$1.1 million was recorded during the third quarter of 2017 due to continued refinement of the purchase accounting calculations.

(d) Eliminate JCB's recorded goodwill.

(e) Record the core deposit intangible asset on the acquired core deposit accounts. Amount to be amortized using a sum of years digits method over a 10 year useful life.

(f)

Adjustment for deferred taxes at the acquisition date. The adjustment decreased by \$0.2 million during the current quarter due to continued refinement of the purchase accounting calculations.

- (g) Fair value adjustment based on evaluation of other assets.
 (h) Fair value adjustment to time deposits based on current interest rates.
 (i) Fair value adjustment to the FHLB advances based on current interest rates.
 (j) Fair value adjustment based on the Company's evaluation of the trust preferred securities.
 (k) A decrease of \$0.1 million was recorded during the current quarter due to further refinement of the purchase accounting calculations.

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

	Pro Forma	
	Nine months ended	
	September 30,	
(in thousands, except per share data)	2017	2016
Total revenues (net interest income plus noninterest income)	\$ 155,907	\$ 146,623
Net income	40,151	42,298
Diluted earnings per common share	1.70	1.80

NOTE 3 - EARNINGS PER SHARE

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

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

	Three months		Nine months	
	ended September		ended September	
	30,		30,	
(in thousands, except per share data)	2017	2016	2017	2016
Net income as reported	\$ 16,315	\$ 11,832	\$ 40,661	\$ 35,209
Weighted average common shares outstanding	23,324	19,997	22,914	20,002
Additional dilutive common stock equivalents	250	227	295	229
Weighted average diluted common shares outstanding	23,574	20,224	23,209	20,231
Basic earnings per common share:	\$ 0.70	\$ 0.59	\$ 1.77	\$ 1.76
Diluted earnings per common share:	\$ 0.69	\$ 0.59	\$ 1.75	\$ 1.74

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

NOTE 4 - INVESTMENTS

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

(in thousands)	September 30, 2017			
	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
Available for sale securities:				
Obligations of U.S. Government-sponsored enterprises	\$99,866	\$ 271	\$ (14)	\$100,123
Obligations of states and political subdivisions	32,684	887	(229)	33,342
Agency mortgage-backed securities	470,941	1,760	(3,045)	469,656
Total securities available for sale	\$603,491	\$ 2,918	\$ (3,288)	\$603,121
Held to maturity securities:				
Obligations of states and political subdivisions	\$14,704	\$ 159	\$ (15)	\$14,848
Agency mortgage-backed securities	61,464	93	(145)	61,412
Total securities held to maturity	\$76,168	\$ 252	\$ (160)	\$76,260
(in thousands)	December 31, 2016			
	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
Available for sale securities:				
Obligations of U.S. Government-sponsored enterprises	\$107,312	\$ 348	\$ —	\$107,660
Obligations of states and political subdivisions	36,486	630	(485)	36,631
Agency mortgage-backed securities	319,345	1,101	(3,940)	316,506
Total securities available for sale	\$463,143	\$ 2,079	\$ (4,425)	\$460,797
Held to maturity securities:				
Obligations of states and political subdivisions	\$14,759	\$ 11	\$ (242)	\$14,528
Agency mortgage-backed securities	65,704	45	(638)	65,111
Total securities held to maturity	\$80,463	\$ 56	\$ (880)	\$79,639

At September 30, 2017, and December 31, 2016, there were no holdings of securities of any one issuer in an amount greater than 10% of shareholders' equity, other than U.S. Government agencies and sponsored enterprises. The agency mortgage-backed securities are all issued by U.S. Government-sponsored enterprises. Available for sale securities having a fair value of \$449.8 million and \$407.3 million at September 30, 2017, and December 31, 2016, respectively, were pledged as collateral to secure deposits of public institutions and for other purposes as required by law or contract provisions.

The amortized cost and estimated fair value of debt securities at September 30, 2017, by contractual maturity, are shown below. Expected maturities may differ from contractual maturities because borrowers may have the right to call or prepay obligations with or without call or prepayment penalties. The weighted average life of the mortgage-backed securities is approximately 4 years.

(in thousands)	Available for sale		Held to maturity	
	Amortized Cost	Estimated Fair Value	Amortized Cost	Estimated Fair Value
Due in one year or less	\$2,940	\$2,960	\$—	\$—
Due after one year through five years	110,538	111,122	184	194
Due after five years through ten years	15,710	16,241	12,996	13,126
Due after ten years	3,362	3,142	1,524	1,528
Agency mortgage-backed securities	470,941	469,656	61,464	61,412
	\$603,491	\$603,121	\$76,168	\$76,260

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

(in thousands)	September 30, 2017					
	Less than 12 months		12 months or more		Total	
	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses
Obligations of U.S. Government-sponsored enterprises	\$10,127	\$ 14	\$—	\$ —	\$10,127	\$ 14
Obligations of states and political subdivisions	4,907	244	—	—	4,907	244
Agency mortgage-backed securities	332,037	2,721	11,307	469	343,344	3,190
	\$347,071	\$ 2,979	\$11,307	\$ 469	\$358,378	\$ 3,448

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

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

NOTE 5 - LOANS

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

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

(in thousands)	September 30, December 31,	
	2017	2016
Loans not accounted for as ASC 310-30	\$ 3,948,676	\$ 3,118,392
Loans accounted for as ASC 310-30	81,982	39,769
Total loans	\$ 4,030,658	\$ 3,158,161

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

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

(in thousands)	September 30, December 31,	
	2017	2016
Commercial and industrial	\$ 1,861,285	\$ 1,632,714
Real estate:		
Commercial - investor owned	737,986	544,808
Commercial - owner occupied	553,512	350,148
Construction and land development	302,182	194,542
Residential	339,377	240,760
Total real estate loans	1,933,057	1,330,258
Consumer and other	155,514	156,182
Loans, before unearned loan fees	3,949,856	3,119,154
Unearned loan fees, net	(1,180)	(762)
Loans, including unearned loan fees	\$ 3,948,676	\$ 3,118,392

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

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

(in thousands)	Commercial and industrial	CRE - investor owned	CRE - owner occupied	Construction and land development	Residential real estate	Consumer and other	Total
Allowance for loan losses:							
Balance at December 31, 2016	\$ 26,996	\$ 3,420	\$ 2,890	\$ 1,304	\$ 2,023	\$ 932	\$ 37,565
Provision (provision reversal) for loan losses	1,835	(105)	(249)	(11)	(3)	66	1,533
Losses charged off	(133)	—	—	—	(9)	(29)	(171)
Recoveries	80	9	89	9	25	9	221
Balance at March 31, 2017	\$ 28,778	\$ 3,324	\$ 2,730	\$ 1,302	\$ 2,036	\$ 978	\$ 39,148
Provision (provision reversal) for loan losses	2,955	(39)	354	(51)	451	(47)	3,623
Losses charged off	(6,035)	—	(45)	(5)	(265)	(39)	(6,389)
Recoveries	57	102	1	49	62	20	291
Balance at June 30, 2017	\$ 25,755	\$ 3,387	\$ 3,040	\$ 1,295	\$ 2,284	\$ 912	\$ 36,673
Provision (provision reversal) for loan losses	1,126	376	245	305	299	71	2,422
Losses charged off	(613)	—	(45)	—	(503)	(75)	(1,236)
Recoveries	205	12	6	25	172	13	433
Balance at September 30, 2017	\$ 26,473	\$ 3,775	\$ 3,246	\$ 1,625	\$ 2,252	\$ 921	\$ 38,292
(in thousands)	Commercial and industrial	CRE - investor owned	CRE - owner occupied	Construction and land development	Residential real estate	Consumer and other	Total
Balance September 30, 2017							
Allowance for loan losses - Ending balance:							
Individually evaluated for impairment	\$ 2,063	\$ 120	\$ —	\$ 186	\$ 48	\$ —	\$ 2,417
Collectively evaluated for impairment	24,410	3,655	3,246	1,439	2,204	921	35,875
Total	\$ 26,473	\$ 3,775	\$ 3,246	\$ 1,625	\$ 2,252	\$ 921	\$ 38,292
Loans - Ending balance:							
Individually evaluated for impairment	\$ 7,646	\$ 544	\$ 1,513	\$ 323	\$ 667	\$ —	\$ 10,693
Collectively evaluated for impairment	1,853,639	737,442	551,999	301,859	338,710	154,334	3,937,983
Total	\$ 1,861,285	\$ 737,986	\$ 553,512	\$ 302,182	\$ 339,377	\$ 154,334	\$ 3,948,676
Balance December 31, 2016							
Allowance for loan losses - Ending balance:							
Individually evaluated for impairment	\$ 2,909	\$ —	\$ —	\$ 155	\$ —	\$ —	\$ 3,064
Collectively evaluated for impairment	24,087	3,420	2,890	1,149	2,023	932	34,501
Total	\$ 26,996	\$ 3,420	\$ 2,890	\$ 1,304	\$ 2,023	\$ 932	\$ 37,565
Loans - Ending balance:							
	\$ 12,523	\$ 430	\$ 1,854	\$ 1,903	\$ 62	\$ —	\$ 16,772

Individually evaluated for
impairment

Collectively evaluated for
impairment

Total

1,620,191	544,378	348,294	192,639	240,698	155,420	3,101,620
\$ 1,632,714	\$ 544,808	\$ 350,148	\$ 194,542	\$ 240,760	\$ 155,420	\$ 3,118,392

A summary of nonperforming loans individually evaluated for impairment by category at September 30, 2017 and December 31, 2016, and the income recognized on impaired loans is as follows:

(in thousands)	September 30, 2017					
	Unpaid Contractual Principal Balance	Recorded Investment With Allowance	Recorded Investment With Allowance	Total Recorded Investment	Related Allowance	Average Recorded Investment
Commercial and industrial	\$13,981	\$ 6,407	\$ 1,044	\$ 7,451	\$ 2,020	\$ 11,735
Real estate:						
Commercial - investor owned	562	259	285	544	120	542
Commercial - owner occupied	—	—	—	—	—	—
Construction and land development	444	322	—	322	186	337
Residential	673	668	—	668	48	676
Consumer and other	—	—	—	—	—	—
Total	\$15,660	\$ 7,656	\$ 1,329	\$ 8,985	\$ 2,374	\$ 13,290

(in thousands)	December 31, 2016					
	Unpaid Contractual Principal Balance	Recorded Investment With Allowance	Recorded Investment With Allowance	Total Recorded Investment	Related Allowance	Average Recorded Investment
Commercial and industrial	\$12,341	\$ 566	\$ 11,791	\$ 12,357	\$ 2,909	\$ 4,489
Real estate:						
Commercial - investor owned	525	435	—	435	—	668
Commercial - owner occupied	225	231	—	231	—	227
Construction and land development	1,904	1,947	359	2,306	155	1,918
Residential	62	62	—	62	—	64
Consumer and other	—	—	—	—	—	—
Total	\$15,057	\$ 3,241	\$ 12,150	\$ 15,391	\$ 3,064	\$ 7,366

(in thousands)	Three months ended		Nine months ended	
	September 30, 2017	September 30, 2016	September 30, 2017	September 30, 2016
Total interest income that would have been recognized under original terms	\$306	\$226	\$961	\$703
Total cash received and recognized as interest income on non-accrual loans	117	203	156	253
Total interest income recognized on accruing, impaired loans	8	32	55	63

There were no loans over 90 days past due and still accruing interest at September 30, 2017 or December 31, 2016. The recorded investment in nonperforming loans by category at September 30, 2017 and December 31, 2016, is as follows:

(in thousands)	September 30, 2017		
	Non-accrual	Restructured, non-accrual	Total
Commercial and industrial	\$6,730	\$ 721	\$7,451
Real estate:			
Commercial - investor owned	544	—	544
Commercial - owner occupied	—	—	—
Construction and land development	322	—	322
Residential	668	—	668
Consumer and other	—	—	—
Total	\$8,264	\$ 721	\$8,985
(in thousands)	December 31, 2016		
	Non-accrual	Restructured, non-accrual	Total
Commercial and industrial	\$10,046	\$ 2,311	\$12,357
Real estate:			
Commercial - investor owned	435	—	435
Commercial - owner occupied	231	—	231
Construction and land development	2,286	20	2,306
Residential	62	—	62
Consumer and other	—	—	—
Total	\$13,060	\$ 2,331	\$15,391

There were no portfolio loans restructured during the three months ended September 30, 2017 and 2016. The recorded investment by category for the portfolio loans that have been restructured during the nine months ended September 30, 2017 and 2016, is as follows:

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

As of September 30, 2017, the Company had \$2.2 million in specific reserves allocated to \$9.5 million of loans that have been restructured. During the three and nine months ended September 30, 2016, there were no portfolio loans that subsequently defaulted. There were no portfolio loans restructured that subsequently defaulted during the three months ended September 30, 2017. Portfolio loans restructured that subsequently defaulted during the nine months ended September 30, 2017, are as follows:

(in thousands, except for number of loans)	Nine months ended September 30, 2017 Number of Recorded loans Balance
Commercial and industrial	2 \$ 343
Real estate:	
Commercial - investor owned	— —
Commercial - owner occupied	— —
Construction and land development	— —
Residential	1 5
Consumer and other	— —
Total	3 \$ 348

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

(in thousands)	September 30, 2017				
	30-89 Days Past Due	90 or More Days Past Due	Total Past Due	Current	Total
Commercial and industrial	\$9,147	\$283	\$9,430	\$1,851,855	\$1,861,285
Real estate:					
Commercial - investor owned	986	—	986	737,000	737,986
Commercial - owner occupied	266	—	266	553,246	553,512
Construction and land development	—	323	323	301,859	302,182
Residential	485	668	1,153	338,224	339,377
Consumer and other	1,542	—	1,542	152,792	154,334
Total	\$12,426	\$1,274	\$13,700	\$3,934,976	\$3,948,676

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

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

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

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

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

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

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

17

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

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

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

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

(in thousands)	September 30, 2017				Total
	Pass (1-6)	Watch (7)	Substandard (8)	Doubtful (9)	
Commercial and industrial	\$1,708,153	\$90,885	\$ 62,247	\$	—\$1,861,285
Real estate:					
Commercial - investor owned	720,912	12,592	4,482	—	737,986
Commercial - owner occupied	513,939	33,249	6,324	—	553,512
Construction and land development	298,613	2,558	1,011	—	302,182
Residential	328,434	3,989	6,954	—	339,377
Consumer and other	153,113	375	846	—	154,334
Total	\$3,723,164	\$143,648	\$ 81,864	\$	—\$3,948,676

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

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

(in thousands)	September 30, 2017		December 31, 2016	
	Weighted-Average Risk Rating ¹	Recorded Investment PCI Loans	Weighted-Average Risk Rating ¹	Recorded Investment PCI Loans
Commercial and industrial	6.26	\$ 3,676	5.87	\$ 3,523
Real estate:				
Commercial - investor owned	7.29	45,865	6.95	8,162
Commercial - owner occupied	6.50	11,786	6.39	11,863
Construction and land development	5.93	7,927	5.80	4,365
Residential	6.05	12,661	5.64	11,792
Total real estate loans		78,239		36,182
Consumer and other	2.99	67	1.64	64
Purchased credit impaired loans		\$ 81,982		\$ 39,769

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

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

(in thousands)	September 30, 2017				
	30-89 Days Past Due	90 or More Days Past Due	Total Past Due	Current	Total
Commercial and industrial	\$—	\$—	\$—	\$3,676	\$3,676
Real estate:					
Commercial - investor owned	429	396	825	45,040	45,865
Commercial - owner occupied	46	909	955	10,831	11,786
Construction and land development	—	478	478	7,449	7,927
Residential	748	992	1,740	10,921	12,661
Consumer and other	—	—	—	67	67
Total	\$1,223	\$2,775	\$3,998	\$77,984	\$81,982

(in thousands)	December 31, 2016				
	30-89 Days Past Due	90 or More Days Past Due	Total Past Due	Current	Total
Commercial and industrial	\$—	\$—	\$—	\$3,523	\$3,523
Real estate:					
Commercial - investor owned	—	—	—	8,162	8,162
Commercial - owner occupied	—	—	—	11,863	11,863
Construction and land development	—	—	—	4,365	4,365
Residential	169	51	220	11,572	11,792
Consumer and other	—	—	—	64	64

Total	\$169	\$51	\$220	\$39,549	\$39,769
-------	-------	------	-------	----------	----------

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

(in thousands)	Contractual Cashflows	Non-accretable Difference	Accretable Yield	Carrying Amount
Balance December 31, 2016	\$ 66,003	\$ 18,902	\$ 13,176	\$ 33,925
Acquisitions	68,763	14,296	5,312	49,155
Principal reductions and interest payments	(16,319)	—	—	(16,319)
Accretion of loan discount	—	—	(5,473)	5,473
Changes in contractual and expected cash flows due to remeasurement	11,110	(702)	3,776	8,036
Reductions due to disposals	(6,393)	(1,612)	(1,595)	(3,186)
Balance September 30, 2017	\$ 123,164	\$ 30,884	\$ 15,196	\$ 77,084
Balance December 31, 2015	\$ 116,689	\$ 26,765	\$ 25,341	\$ 64,583
Principal reductions and interest payments	(20,417)	—	—	(20,417)
Accretion of loan discount	—	—	(4,984)	4,984
Changes in contractual and expected cash flows due to remeasurement	9,194	975	(1,043)	9,262
Reductions due to disposals	(27,888)	(6,779)	(3,713)	(17,396)
Balance September 30, 2016	\$ 77,578	\$ 20,961	\$ 15,601	\$ 41,016

The accretable yield is recognized in interest income over the estimated life of the acquired loans using the effective yield method. Outstanding customer balances on PCI loans were \$107.8 million and \$54.6 million as of September 30, 2017, and December 31, 2016, respectively.

NOTE 6 - COMMITMENTS AND CONTINGENCIES

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

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

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

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

(in thousands)	September 30, 2017	December 31, 2016
Commitments to extend credit	\$ 1,263,809	\$ 1,075,170
Letters of credit	74,007	78,954

Commitments to extend credit are agreements to lend to a customer as long as there is no violation of any condition established in the contract. Commitments usually have fixed expiration dates or other termination clauses, may have significant usage restrictions, and may require payment of a fee. Of the total commitments to extend credit at September 30, 2017, and December 31, 2016, approximately \$113 million and \$90 million, respectively, represent fixed rate loan commitments. Since certain of the commitments may expire without being drawn upon or may be revoked, the total commitment amounts do not necessarily represent future cash requirements. The Company evaluates each customer's credit worthiness on a case-by-case basis. The amount of collateral obtained, if deemed necessary by the Company upon extension of credit, is based on management's credit evaluation of the borrower. Collateral held varies, but may include accounts receivable, inventory, premises and equipment, and real estate. Other liabilities includes \$0.4 million for estimated losses attributable to the unadvanced commitments at September 30, 2017, and December 31, 2016.

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

Contingencies

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

NOTE 7 - DERIVATIVE FINANCIAL INSTRUMENTS

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

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

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

(in thousands)	Notional Amount		Asset Derivatives (Other Assets) Fair Value		Liability Derivatives (Other Liabilities) Fair Value	
	September 30, 2017	December 31, 2016	September 30, 2017	December 31, 2016	September 30, 2017	December 31, 2016
Non-designated hedging instruments						
Interest rate swap contracts	\$270,542	\$124,322	\$1,902	\$982	\$1,902	\$982
Foreign exchange forward contracts	1,376	3,034	1,376	3,034	1,376	3,034

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

NOTE 8 - FAIR VALUE MEASUREMENTS

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

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

(in thousands)	September 30, 2017			Total Fair Value
	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)	
Assets				
Securities available for sale				
Obligations of U.S. Government-sponsored enterprises	\$ 100,123	\$ —	\$ —	\$ 100,123
Obligations of states and political subdivisions	33,341	—	—	33,341
Residential mortgage-backed securities	469,657	—	—	469,657
Total securities available for sale	\$ 603,121	\$ —	\$ —	\$ 603,121
State tax credits held for sale	—	1,274	—	1,274
Derivative financial instruments	3,278	—	—	3,278
Total assets	\$ 606,399	\$ 1,274	\$ —	\$ 607,673
Liabilities				
Derivative financial instruments	\$ 3,278	\$ —	\$ —	\$ 3,278
Total liabilities	\$ 3,278	\$ —	\$ —	\$ 3,278

(in thousands)	December 31, 2016			Total Fair Value
	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)	
Assets				
Securities available for sale				

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

Obligations of U.S. Government-sponsored enterprises	\$-107,660	\$ —	\$107,660
Obligations of states and political subdivisions	—33,542	3,089	36,631
Residential mortgage-backed securities	—316,506	—	316,506
Total securities available for sale	\$-457,708	\$ 3,089	\$460,797
State tax credits held for sale	—	3,585	3,585
Derivative financial instruments	—4,016	—	4,016
Total assets	\$-461,724	\$ 6,674	\$468,398
 Liabilities			
Derivative financial instruments	\$-4,016	\$ —	\$4,016
Total liabilities	\$-4,016	\$ —	\$4,016

Securities available for sale. Securities classified as available for sale are reported at fair value utilizing Level 2 and Level 3 inputs. Fair values for Level 2 securities are based upon dealer quotes, market spreads, the U.S. Treasury yield curve, trade execution data, market consensus prepayment speeds, credit information and the bond's terms and conditions at the security level. At September 30, 2017, there were no Level 3 Auction Rate Securities. Auction Rate Securities at September 30, 2017 were valued using a Level 2 pricing source similar to our other securities available for sale.

State tax credits held for sale. At September 30, 2017, of the \$35.3 million of state tax credits held for sale on the condensed consolidated balance sheet, approximately \$1.3 million were carried at fair value. The remaining \$34.0 million of state tax credits were accounted for at cost.

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

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

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

Level 3 financial instruments

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

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

Transfers in and/or out of Level 3. There were no Level 3 transfers during the quarters ended September 30, 2017 and 2016.

	Securities available for sale, at fair value		
	Three months ended September 30, 2017	Nine months ended September 30, 2017	2016
(in thousands)			
Beginning balance	\$-\$3,093	\$3,089	\$3,077
Total gains:			
Included in other comprehensive income	—1	4	17
Purchases, sales, issuances and settlements:			
Purchases	—	—	—
Transfer in and/or out of Level 3	—	(3,093)	—
Ending balance	\$-\$3,094	\$—	\$3,094
Change in unrealized gains relating to assets still held at the reporting date	\$-\$1	\$—	\$17

	State tax credits held for sale			
	Three months ended September 30, 2017	Nine months ended September 30, 2016	2017	2016
(in thousands)				
Beginning balance	\$1,274	\$4,774	\$3,585	\$5,941
Total gains:				
Included in earnings	—	27	49	144
Purchases, sales, issuances and settlements:				
Sales	—	—	(2,360)	(1,284)
Ending balance	\$1,274	\$4,801	\$1,274	\$4,801
Change in unrealized gains (losses) relating to assets still held at the reporting date	\$—	\$27	\$(655)	\$(237)

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

(in thousands)	(1) Total Fair Value	(1) Quoted Prices in Active Markets for Identical Assets (Level 1)	(1) Significant Other Observable Inputs (Level 2)	(1) Significant Unobservable Inputs (Level 3)	Total losses for the three months ended September 30, 2017	Total losses for the nine months ended September 30, 2017
Impaired loans	\$2,743	\$	—\$	—\$ 2,743	\$ 613	\$ 5,876
Other real estate	26	—	—	26	38	38
Total	\$2,769	\$	—\$	—\$ 2,769	\$ 651	\$ 5,914

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

Impaired loans are reported at the fair value of the underlying collateral for collateral dependent loans. Fair values for impaired loans are obtained from current appraisals by qualified licensed appraisers or independent valuation specialists. At September 30, 2017, impaired loans measured on a non-recurring basis had a principal balance of \$3.9 million, with a valuation allowance of \$1.2 million.

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

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

(in thousands)	September 30, 2017		December 31, 2016	
	Carrying Amount	Estimated fair value	Carrying Amount	Estimated fair value
Balance sheet assets				
Cash and due from banks	\$76,777	\$ 76,777	\$54,288	\$ 54,288
Federal funds sold	1,155	1,155	446	446
Interest-bearing deposits	107,821	107,821	145,048	145,048
Securities available for sale	603,121	603,121	460,797	460,797
Securities held to maturity	76,168	76,260	80,463	79,639
Other investments, at cost	29,436	29,436	14,840	14,840
Loans held for sale	6,411	6,411	9,562	9,562
Derivative financial instruments	3,278	3,278	4,016	4,016
Loans, net	3,987,467	4,009,071	3,114,752	3,125,701
State tax credits, held for sale	35,291	37,781	38,071	41,264
Accrued interest receivable	14,213	14,213	11,117	11,117
Balance sheet liabilities				
Deposits	4,059,214	4,057,561	3,233,363	3,232,414
Subordinated debentures and notes	118,093	100,062	105,540	86,052
Federal Home Loan Bank advances	248,868	249,168	—	—
Other borrowings	219,104	219,012	276,980	276,905
Derivative financial instruments	3,278	3,278	4,016	4,016
Accrued interest payable	2,007	2,007	1,105	1,105

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

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

(in thousands)	Estimated Fair Value			Balance at September 30, 2017
	Measurement at Reporting Date Using		Level 3	
	Level 1	Level 2		
Financial Assets:				
Securities held to maturity	\$-\$76,260	\$	—	\$ 76,260
Portfolio loans, net	—		4,009,071	4,009,071
State tax credits, held for sale	—		36,508	36,508
Financial Liabilities:				
Deposits	3,442,015		615,546	4,057,561
Subordinated debentures and notes	—100,062	—		100,062
Federal Home Loan Bank advances	—249,168	—		249,168
Other borrowings	—219,012	—		219,012

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

NOTE 9 - NEW AUTHORITATIVE ACCOUNTING GUIDANCE

Financial Accounting Standards Board (the "FASB") Accounting Standards Update (the "ASU") 2017-12 "Derivatives and Hedging (Topic 815): Targeted Improvements to Accounting for Hedging Activities" In August 2017, the FASB issued ASU 2017-12, "Targeted Improvement to Accounting for Hedging Activities". The objective of ASU 2017-12 is to improve the financial reporting of hedging relationships by better aligning an entity's risk management activity with the economic objectives in undertaking those activities. In addition, the amendments in this update simplify the application of hedge accounting for preparers of financial statements, as well as improve the understandability of an entity's risk management activities being conveyed to financial statement users. The new guidance becomes effective for periods beginning after December 15, 2018. Early adoption is permitted. The Company is currently evaluating the new guidance and timing of adoption to determine the impact this standard may have on its financial statements.

FASB ASU 2017-09 "Compensation - Stock Compensation (Topic 718): Scope of Modification Accounting" In May 2017, the FASB issued ASU 2017-09, "Compensation - Stock Compensation (Topic 718): Scope of Modification Accounting" which amends the scope of modification accounting for share-based payment awards. The amendments provide guidance on the types of changes to the terms or conditions of share-based payment awards to which an entity would be required to apply modification accounting with an intent to simplify the accounting under ASC 718. The amendments are effective for public business entities for annual periods beginning after December 15, 2017, including

interim periods within those annual periods, with early adoption being permitted. The Company has evaluated the new guidance and does not expect it to have a material impact on the Company's consolidated financial statements.

FASB ASU 2017-08 "Receivables - Nonrefundable Fees and Other Costs (Subtopic 310-20), Premium Amortization on Purchased Callable Debt Securities" In March 2017, the FASB issued ASU 2017-08, "Receivables - Nonrefundable Fees and Other Costs (Subtopic 310-20)" which shortens the amortization period of certain callable debt securities held at a premium to the earliest call date. The amendments are effective for public business entities for annual periods beginning after December 15, 2018, including interim periods within those annual periods, with early adoption being

permitted. The Company is currently evaluating the new guidance and has not determined the impact this standard may have on its financial statements.

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

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

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

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

FASB ASU 2016-01 "Financial Instruments-Overall (Subtopic 825-10): Recognition and Measurement of Financial Assets and Financial Liabilities" In January 2016, the FASB issued ASU 2016-01, "Financial Instruments-Overall (Subtopic 825-10): Recognition and Measurement of Financial Assets and Financial Liabilities." ASU 2016-01 requires equity investments to be measured at fair value through earnings, and eliminates the available-for-sale classification for equity securities with readily determinable fair values. For financial liabilities where the fair value

option has been elected, changes in fair value due to instrument-specific credit risk must be recognized in other comprehensive income. When measuring the fair value of financial instruments at amortized cost, the exit price must be used for disclosure purposes. The ASU also requires that financial assets and liabilities be presented separately in the notes to the financial statements. This ASU becomes effective for fiscal years beginning after December 15, 2017,

including interim periods therein. Early adoption is permitted with some exceptions. The Company has evaluated its applicable equity investments and determined that they qualify for the measurement exception which allows those investments to be measured at their cost minus impairment. Any valuation adjustments will be recorded prospectively through net income, and the related disclosure will be included in the Notes to the Consolidated Financial Statements.

FASB ASU 2014-09, "Revenue from Contracts with Customers (Topic 606)" In May 2014, the FASB issued ASU 2014-09, "Revenue from Contracts with Customers". The objective of ASU 2014-09 is to establish a single comprehensive model for entities to use in accounting for revenue arising from contracts with customers and will supersede most of the existing revenue recognition guidance, including industry-specific guidance. The core principle of ASU 2014-09 is that an entity recognizes revenue to depict the transfer of promised goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods or services. In applying the new guidance, an entity will (1) identify the contract(s) with a customer; (2) identify the performance obligations in the contract; (3) determine the transaction price; (4) allocate the transaction price to the contract's performance obligations; and (5) recognize revenue when (or as) the entity satisfies a performance obligation. ASU 2014-09 applies to all contracts with customers except those that are within the scope of other topics in the FASB Accounting Standards Codification. The new guidance was originally effective for annual reporting periods (including interim periods within those periods) beginning after December 15, 2016 for public companies. In August 2015, the FASB issued ASU 2015-14, which defers the effective date of this guidance to annual reporting periods beginning after December 15, 2017 for public companies, and permits early adoption on a limited basis. The Company has conducted its initial assessment and is currently evaluating contracts to assess and quantify accounting methodology changes resulting from the adoption of ASU 2014-09. The majority of the Company's revenues are derived from loans which are excluded from the new standard; therefore, the new guidance is not expected to have a material impact on the Company's consolidated financial position, results of operations or cash flows. The Company has decided upon the modified retrospective adoption method.

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

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

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

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

Introduction

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

Executive Summary

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

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

(in thousands, except per share data)	For the Three Months ended/At			For the Nine Months ended		
	September 30, 2017	June 30, 2017	September 30, 2016	September 30, 2017	September 30, 2016	
EARNINGS						
Total interest income	\$52,468	\$51,542	\$ 37,293	\$147,750	\$ 109,786	
Total interest expense	6,843	5,909	3,463	17,850	9,745	
Net interest income	45,625	45,633	33,830	129,900	100,041	
Provision for portfolio loans	2,422	3,623	3,038	7,578	4,587	
Provision reversal for PCI loans	—	(207)	(1,194)	(355)	(1,603)	
Net interest income after provision for loan losses	43,203	42,217	31,986	122,677	97,057	
Total noninterest income	8,372	7,934	6,976	23,282	20,030	
Total noninterest expense	27,404	32,651	20,814	86,791	62,929	
Income before income tax expense	24,171	17,500	18,148	59,168	54,158	
Income tax expense	7,856	5,545	6,316	18,507	18,949	
Net income	\$16,315	\$11,955	\$ 11,832	\$40,661	\$ 35,209	
Basic earnings per share	\$0.70	\$0.51	\$ 0.59	\$1.77	\$ 1.76	
Diluted earnings per share	0.69	0.50	0.59	1.75	1.74	
Return on average assets	1.27	% 0.96	% 1.23	% 1.11	% 1.26	%
Return on average common equity	11.69	% 8.78	% 12.46	% 10.37	% 12.83	%
Return on average tangible common equity	15.23	% 11.49	% 13.64	% 13.25	% 14.10	%
Net interest margin (fully tax equivalent)	3.88	% 3.98	% 3.80	% 3.87	% 3.87	%
Efficiency ratio	50.75	% 60.95	% 51.01	% 56.66	% 52.41	%
Tangible book value per common share	\$18.09	\$17.89	\$ 17.43			
ASSET QUALITY ⁽¹⁾						
Net charge-offs (recoveries)	\$803	\$6,104	\$ 1,038	\$6,851	\$ 530	
Nonperforming loans	8,985	13,081	19,942			
Classified assets	80,757	93,795	101,545			
Nonperforming loans to portfolio loans	0.23	% 0.34	% 0.66	%		
Nonperforming assets to total assets ⁽¹⁾	0.18	% 0.27	% 0.59	%		
Allowance for loan losses to portfolio loans	0.97	% 0.96	% 1.23	%		
Net charge-offs to average loans (annualized)	0.08	% 0.64	% 0.14	% 0.24	% 0.02	%

(1) Excludes purchased credit impaired loans and related assets, except for their inclusion in total assets.

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

(in thousands)	For the Three Months ended			For the Nine Months ended		
	September 30, 2017	June 30, 2017	September 30, 2016	September 30, 2017	September 30, 2016	
CORE PERFORMANCE MEASURES (1)						
Net interest income	\$44,069	\$43,049	\$ 31,534	\$124,685	\$ 91,340	
Provision for portfolio loans	2,422	3,623	3,038	7,578	4,587	
Noninterest income	8,350	7,934	6,828	23,260	18,938	
Noninterest expense	27,070	27,798	20,242	79,814	61,123	
Income before income tax expense	22,927	19,562	15,082	60,553	44,568	
Income tax expense	7,391	6,329	5,142	18,636	15,276	
Net income	\$15,536	\$13,233	\$ 9,940	\$41,917	\$ 29,292	
Earnings per share	\$0.66	\$0.56	\$ 0.49	\$ 1.81	\$ 1.45	
Return on average assets	1.21	% 1.06	% 1.04	% 1.14	% 1.05	%
Return on average common equity	11.13	% 9.72	% 10.47	% 10.69	% 10.67	%
Return on average tangible common equity	14.50	% 12.72	% 11.46	% 13.66	% 11.73	%
Net interest margin (fully tax equivalent)	3.75	% 3.76	% 3.54	% 3.71	% 3.53	%
Efficiency ratio	51.64	% 54.52	% 52.77	% 53.95	% 55.43	%

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

For the nine months ended September 30, 2017 compared to the nine months ended September 30, 2016, the Company noted the following trends:

The Company reported net income of \$40.7 million, or \$1.75 per diluted share, for the nine months ended September 30, 2017, compared to \$35.2 million, or \$1.74 per diluted share, for the same period in 2016. The \$0.01 increase in earnings per share primarily resulted from increases in net interest income and noninterest income including growth from the JCB acquisition, offset by a decline in contribution from non-core acquired assets and the impact of merger related expenses in 2017.

On a core basis¹, net income was \$41.9 million, or \$1.81 per share, for the nine months ended September 30, 2017, compared to \$29.3 million, or \$1.45 per share, in the prior year period. The earnings per share increase of \$0.36 was primarily due to higher levels of core net interest income from continued growth in earning asset balances combined with 18 basis points of core net interest margin expansion. This increase was partially offset by an increase in core noninterest expense primarily from employee compensation and benefits as a result of the JCB acquisition.

- Net interest income for the first nine months of 2017 increased \$29.9 million or 30%, from the prior year period due to strong portfolio loan growth, net interest margin expansion and the acquisition of JCB.

Net interest margin for the first nine months of 2017 remained stable at 3.87% when compared to the prior year period. Core net interest margin¹, which excludes incremental accretion on non-core acquired loans, increased 18 basis points for the first nine months of 2017 from the prior year primarily due to core deposit-funded portfolio loan growth improving the earning asset mix, increased yield on portfolio loans, controlled increases in deposit costs, and the acquisition of JCB.

Noninterest income for the first nine months of 2017 increased \$3.3 million or 16%, compared to the prior year period due primarily to the acquisition of JCB (\$3.6 million). This increase was partially offset by prior year non-core gain on sale of other real estate and other non-core income from acquired assets.

Noninterest expenses were \$86.8 million for the nine months ended September 30, 2017, compared to \$62.9 million for the nine months ended September 30, 2016. Noninterest expenses for the nine months included \$6.5 million of merger related expenses. Core noninterest expenses¹ were \$79.8 million for the nine months ended September 30, 2017, compared to \$61.1 million for the prior year period due to the JCB acquisition and two full quarters of JCB's expense base.

Balance sheet highlights:

Loans – Portfolio loans increased to \$4.0 billion at September 30, 2017, increasing \$878 million when compared to December 31, 2016. Excluding the acquisition of JCB, portfolio loans organically grew by \$200 million in the first nine months of 2017. On a year-over-year basis, portfolio loans increased \$959 million of which \$281 million was organic loan growth and \$678 million was from the acquisition of JCB. See Item 1, Note 5 – Portfolio Loans for more information.

Deposits – Total deposits at September 30, 2017 were \$4.1 billion, an increase of \$826 million, or 26% from December 31, 2016, and \$934 million, or 30%, from September 30, 2016. \$774 million of the increase in both periods is attributed to the acquisition of JCB. Core deposits, defined as total deposits excluding time deposits, were \$3.4 billion at September 30, 2017, an increase of \$114 million, or 3% , and \$805 million, or 31%, from the linked quarter and prior year period, respectively. The trends in deposits reflect continued progress across our business lines, \$636 million of core deposits from JCB, and some seasonality.

Asset quality – Nonperforming loans were \$9.0 million at September 30, 2017, compared to \$14.9 million at December 31, 2016. Nonperforming loans represented 0.23% of portfolio loans at September 30, 2017 versus 0.48% at December 31, 2016. There were no portfolio loans that were over 90 days delinquent and still accruing at September 30, 2017 or December 31, 2016.

Provision for portfolio loan losses was \$7.6 million for the nine months ended September 30, 2017, compared to \$4.6 million for the nine months ended September 30, 2016. See Item 1, Note 5 – Portfolio Loans, and Provision and Allowance for Loan Losses in this section for more information.

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

33

RESULTS OF OPERATIONS

Net Interest Income

Average Balance Sheet

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

(in thousands)	Three months ended September 30, 2017			2016		
	Average Balance	Interest Income/Expense	Average Yield/ Rate	Average Balance	Interest Income/Expense	Average Yield/ Rate
Assets						
Interest-earning assets:						
Taxable portfolio loans (1)	\$3,866,434	\$ 45,526	4.67 %	\$2,916,678	\$ 30,980	4.23 %
Tax-exempt portfolio loans (2)	38,202	623	6.47	41,495	611	5.86
Non-core acquired loans - contractual	35,120	553	6.25	53,198	789	5.90
Non-core acquired loans - incremental accretion		1,556	17.57		2,296	17.17
Total loans	3,939,756	48,258	4.86	3,011,371	34,676	4.58
Taxable investments in debt and equity securities	667,520	3,981	2.37	479,755	2,462	2.04
Non-taxable investments in debt and equity securities (2)	43,537	475	4.33	47,761	521	4.34
Short-term investments	61,859	173	1.11	50,193	67	0.53
Total securities and short-term investments	772,916	4,629	2.38	577,709	3,050	2.10
Total interest-earning assets	4,712,672	52,887	4.45	3,589,080	37,726	4.18
Noninterest-earning assets:						
Cash and due from banks	76,661			58,178		
Other assets	348,100			213,352		
Allowance for loan losses	(41,939)			(45,692)		
Total assets	\$5,095,494			\$3,814,918		
Liabilities and Shareholders' Equity						
Interest-bearing liabilities:						
Interest-bearing transaction accounts	\$805,073	\$ 523	0.26 %	\$600,707	\$ 332	0.22 %
Money market accounts	1,314,274	2,410	0.73	1,075,747	1,143	0.42
Savings	200,394	125	0.25	108,075	68	0.25
Certificates of deposit	580,951	1,493	1.02	516,159	1,319	1.02
Total interest-bearing deposits	2,900,692	4,551	0.62	2,300,688	2,862	0.49
Subordinated debentures	118,086	1,316	4.42	56,807	369	2.59
Other borrowed funds	455,995	976	0.85	286,896	232	0.32
Total interest-bearing liabilities	3,474,773	6,843	0.78	2,644,391	3,463	0.52
Noninterest bearing liabilities:						
Demand deposits	1,031,346			768,468		
Other liabilities	35,662			24,198		
Total liabilities	4,541,781			3,437,057		

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

Shareholders' equity	553,713	377,861	
Total liabilities & shareholders' equity	\$5,095,494	\$3,814,918	
Net interest income	\$ 46,044		\$ 34,263
Net interest spread		3.67 %	3.66 %
Net interest margin		3.88 %	3.80 %
Core net interest margin (3)		3.75 %	3.54 %

(1) Average balances include non-accrual loans. The income on such loans is included in interest but is recognized only upon receipt. Loan fees, net of amortization of deferred loan origination fees and costs, included in interest income are approximately \$0.9 million and \$0.8 million for the three months ended September 30, 2017 and 2016 respectively.

(2) Non-taxable income is presented on a fully tax-equivalent basis using a 38.0% and 38.3% tax rate in 2017 and 2016, respectively. The tax-equivalent adjustments were \$0.4 million for the three months ended September 30, 2017 and 2016, respectively.

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

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

(in thousands)	Nine months ended September 30, 2017			2016		
	Average Balance	Interest Income/Expense	Average Yield/ Rate	Average Balance	Interest Income/Expense	Average Yield/ Rate
Assets						
Interest-earning assets:						
Taxable portfolio loans (1)	\$3,713,188	\$ 127,046	4.57 %	\$2,830,365	\$ 88,667	4.18 %
Tax-exempt portfolio loans (2)	41,703	1,998	6.41	41,526	1,899	6.11
Non-core acquired loans - contractual	37,043	1,753	6.33	60,420	2,693	5.95
Non-core acquired loans - incremental accretion		5,215	18.82		8,701	19.24
Total loans	3,791,934	136,012	4.80	2,932,311	101,960	4.64
Taxable investments in debt and equity securities	624,126	10,976	2.35	474,981	7,385	2.08
Non-taxable investments in debt and equity securities (2)	48,165	1,588	4.41	48,475	1,591	4.38
Short-term investments	75,125	537	0.96	47,771	186	0.52
Total securities and short-term investments	747,416	13,101	2.34	571,227	9,162	2.14
Total interest-earning assets	4,539,350	149,113	4.39	3,503,538	111,122	4.24
Noninterest-earning assets:						
Cash and due from banks	76,086			56,618		
Other assets	325,808			214,860		
Allowance for loan losses	(43,901)			(44,567)		
Total assets	\$4,897,343			\$3,730,449		
Liabilities and Shareholders' Equity						
Interest-bearing liabilities:						
Interest-bearing transaction accounts	\$786,945	\$ 1,721	0.29 %	\$578,373	\$ 967	0.22 %
Money market accounts	1,272,939	5,841	0.61	1,056,565	3,162	0.40
Savings	185,218	332	0.24	102,589	191	0.25
Certificates of deposit	576,906	4,081	0.95	460,667	3,521	1.02
Total interest-bearing deposits	2,822,008	11,975	0.57	2,198,194	7,841	0.48
Subordinated debentures	116,239	3,768	4.33	56,807	1,078	2.53
Other borrowed funds	421,176	2,107	0.67	339,849	826	0.32
Total interest-bearing liabilities	3,359,423	17,850	0.71	2,594,850	9,745	0.50
Noninterest bearing liabilities:						
Demand deposits	982,788			739,705		
Other liabilities	30,809			29,196		
Total liabilities	4,373,020			3,363,751		
Shareholders' equity	524,323			366,698		
Total liabilities & shareholders' equity	\$4,897,343			\$3,730,449		
Net interest income		\$ 131,263			\$ 101,377	
Net interest spread			3.68 %			3.74 %
Net interest margin			3.87 %			3.87 %
Core net interest margin (3)			3.71 %			3.53 %

(1) Average balances include non-accrual loans. The income on such loans is included in interest but is recognized only upon receipt. Loan fees, net of amortization of deferred loan origination fees and costs, included in interest

income are approximately \$2.5 million and \$1.6 million for the nine months ended September 30, 2017 and 2016 respectively.

Non-taxable income is presented on a fully tax-equivalent basis using a 38.0% and 38.3% tax rate in 2017 and (2) 2016, respectively. The tax-equivalent adjustments were \$1.4 million and \$1.3 million for the nine months ended September 30, 2017 and 2016, respectively.

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

Rate/Volume

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

(in thousands)	2017 compared to 2016					
	Three months ended September 30, Increase (decrease) due to			Nine months ended September 30, Increase (decrease) due to		
	Volume(1)	Rate(2)	Net	Volume(1)	Rate(2)	Net
Interest earned on:						
Taxable portfolio loans	\$10,986	\$3,560	\$14,546	\$29,551	\$8,828	\$38,379
Tax-exempt portfolio loans (3)	(50)	62	12	8	91	99
Non-core acquired loans	(1,075)	99	(976)	(4,408)	(18)	(4,426)
Taxable investments in debt and equity securities	1,081	438	1,519	2,527	1,064	3,591
Non-taxable investments in debt and equity securities (3)	(45)	(1)	(46)	(11)	8	(3)
Short-term investments	19	87	106	142	209	351
Total interest-earning assets	\$10,916	\$4,245	\$15,161	\$27,809	\$10,182	\$37,991
Interest paid on:						
Interest-bearing transaction accounts	\$127	\$64	\$191	\$406	\$348	\$754
Money market accounts	298	969	1,267	742	1,937	2,679
Savings	58	(1)	57	148	(7)	141
Certificates of deposit	170	4	174	835	(275)	560
Subordinated debentures	573	374	947	1,603	1,087	2,690
Borrowed funds	197	547	744	235	1,046	1,281
Total interest-bearing liabilities	1,423	1,957	3,380	3,969	4,136	8,105
Net interest income	\$9,493	\$2,288	\$11,781	\$23,840	\$6,046	\$29,886

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

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

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

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

Net interest income (on a tax equivalent basis) was \$46.0 million for the three months ended September 30, 2017, compared to \$34.3 million for the same period of 2016, an increase of \$11.8 million, or 34%. The tax-equivalent net interest margin was 3.88% for the third quarter of 2017, compared to 3.98% for the second quarter of 2017, and 3.80% in the third quarter of 2016. Portfolio loan growth and higher rates, combined with the acquisition of JCB, supported the \$15.2 million increase in interest income over the prior year period. The yield on taxable portfolio loans increased 44 basis points from the prior year period to 4.67% for the three months ended September 30, 2017. The increase was due to the impact of interest rate increases which increased yields on variable rate loans and an improved earning asset mix. The run-off of higher yielding non-core acquired loans continues to negatively impact net interest margin and resulted in a \$1.0 million decrease in interest income for the three months ended September 30, 2017 compared to the prior year period.

Net interest income (on a tax equivalent basis) was \$131.3 million for the nine months ended September 30, 2017, compared to \$101.4 million for the same period of 2016, an increase of \$29.9 million, or 29%. The tax-equivalent net interest margin was 3.87% for the nine months ended September 30, 2017, consistent with 3.87% for the prior year period. The increase in net interest income was primarily due to the impact of rising interest rates which increased yields on variable rate loans and to an improved earning asset mix, partially offset by a decline in contributions from non-core acquired assets and higher rates on interest bearing liabilities.

Core net interest margin¹ expanded 18 basis points from the prior year to 3.71% for the nine months ended September 30, 2017, primarily due to loan growth improving the earning asset mix, combined with increased yield on portfolio loans out-pacing the increase to borrowing costs. Core net interest margin also increased modestly from JCB purchase accounting adjustments. The Company continues to manage its balance sheet to grow core net interest income and expects to maintain core net interest margin over the coming quarters; however, pressure on funding costs could negate the expected trends in core net interest margin.

Non-Core Acquired Assets Contribution

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

(in thousands)	For the Three Months ended		For the Nine Months ended	
	September 30, 2017	September 30, 2016	September 30, 2017	September 30, 2016
Accelerated cash flows and other incremental accretion	\$1,556	\$ 2,296	\$5,215	\$ 8,701
Provision reversal for non-core acquired loan losses	—	1,194	355	1,603
Gain (loss) on sale of other real estate	—	(225)	—	480
Other income from other real estate	—	287	—	526
Other expenses	(19)	(270)	(126)	(922)
Non-core acquired assets income before income tax expense	\$1,537	\$ 3,282	\$5,444	\$ 10,388

Accelerated cash flows and other incremental accretion consists of the interest income on non-core acquired loans in excess of contractual interest on the loans. The contractual amount of interest is included in the Company's core results. At September 30, 2017, the remaining accretable yield on the remaining non-core acquired portfolio was estimated to be \$10 million and the non-accretable difference was approximately \$15 million. Accelerated cash flows and other incremental accretion from these was \$5.2 million for the nine months ended September 30, 2017, and \$8.7 million for the same period in 2016. The Company estimates income from accelerated cash flows and other incremental accretion to be between \$6 million and \$8 million in total for 2017 and between \$3 million and \$5 million in 2018.

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

37

Noninterest Income

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

(in thousands)	Three months ended September 30,			
	2017	2016	Increase (decrease)	
Service charges on deposit accounts	\$2,820	\$2,200	\$620	28 %
Wealth management revenue	2,062	1,694	368	22 %
Card services revenue	1,459	804	655	81 %
Gain on state tax credits, net	77	228	(151)	(66)%
Miscellaneous income - core	1,932	1,902	30	2 %
Core noninterest income (1)	8,350	6,828	1,522	22 %
Loss on sale of other real estate from non-core acquired loans	—	(225)	225	100 %
Gain on sale of investment securities	22	86	(64)	(74)%
Other income from non-core acquired assets	—	287	(287)	(100)%
Total noninterest income	\$8,372	\$6,976	\$1,396	20 %

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

(in thousands)	Nine months ended September 30,			
	2017	2016	Increase (decrease)	
Service charges on deposit accounts	\$8,146	\$6,431	\$1,715	27 %
Wealth management revenue	5,949	5,000	949	19 %
Card services revenue	3,888	2,236	1,652	74 %
Gain on state tax credits, net	332	899	(567)	(63)%
Gain on sale of other real estate - core	17	122	(105)	(86)%
Miscellaneous income - core	4,928	4,250	678	16 %
Core noninterest income (1)	23,260	18,938	4,322	23 %
Gain on sale of other real estate from non-core acquired loans	—	480	(480)	(100)%
Gain on sale of investment securities	22	86	(64)	(74)%
Other income from non-core acquired assets	—	526	(526)	(100)%
Total noninterest income	\$23,282	\$20,030	\$3,252	16 %

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

Noninterest income increased \$3.3 million, or 16% in the first nine months of 2017 compared to the first nine months of 2016. Core noninterest income¹ grew 23% in the first nine months of 2017 due primarily to the JCB acquisition contributing approximately \$3.6 million. In addition, the Company's customer swap, card services and wealth management businesses all experienced growth due to increased customer activity and new customer additions. The Company expects continued growth in fee income of 5% - 7% for 2018.

Noninterest Expense

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

(in thousands)	Three months ended September 30,			
	2017	2016	Increase (decrease)	
Core expenses (1):				
Employee compensation and benefits - core	\$15,090	\$11,910	\$3,180	27 %
Occupancy - core	2,434	1,679	755	45 %
Data processing - core	1,389	1,135	254	22 %
FDIC and other insurance	731	780	(49)	(6)%
Professional fees - core	920	540	380	70 %
Loan, legal and other real estate expense - core	567	310	257	83 %
Other - core	5,939	3,888	2,051	53 %
Core noninterest expense (1)	27,070	20,242	6,828	34 %
Merger related expenses	315	302	13	4 %
Other expenses related to non-core acquired loans	19	270	(251)	(93)%
Total noninterest expense	\$27,404	\$20,814	\$6,590	32 %

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

(in thousands)	Nine months ended September 30,			
	2017	2016	Increase (decrease)	
Core expenses (1):				
Employee compensation and benefits - core	\$46,096	\$36,560	\$9,536	26 %
Occupancy - core	6,628	4,920	1,708	35 %
Data processing - core	4,828	3,396	1,432	42 %
FDIC and other insurance	2,356	2,241	115	5 %
Professional fees - core	2,833	1,942	891	46 %
Loan, legal and other real estate expense - core	1,418	782	636	81 %
Other - core	15,655	11,282	4,373	39 %
Core noninterest expense (1)	79,814	61,123	18,691	31 %
Executive severance	—	332	(332)	(100)%
Merger related expenses	6,462	302	6,160	2,040 %
Other non-core expenses	389	250	139	56 %
Other expenses related to non-core acquired loans	126	922	(796)	(86)%
Total noninterest expense	\$86,791	\$62,929	\$23,862	38 %

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

Noninterest expenses were \$86.8 million for the nine months ended September 30, 2017, compared to \$62.9 million for the nine months ended September 30, 2016. The increase was primarily due to the acquisition of JCB including merger related expenses. Core noninterest expenses¹ increased \$18.7 million to \$79.8 million for the nine months ended September 30, 2017, from \$61.1 million for the prior year period. Core expenses increased from the acquisition as well as from increases in Employee compensation and benefits from investments in revenue producing personnel.

The Company's Core efficiency ratio¹ decreased to 54.0% for the nine months ended September 30, 2017, compared to 55.4% for the prior year period, and reflects continuing efforts to leverage its expense base and execution of the initiatives necessary to realize the expected cost savings from the JCB acquisition. The conversion of JCB's core

systems was completed late in the second quarter of 2017. The Company expects to continue to invest in revenue producing associates and other infrastructure that supports additional growth. These investments are expected to result in expense growth, at a rate of 35% - 45% of projected revenue growth for 2018, resulting in modest improvement to the Company's efficiency ratio.

Income Taxes

The Company's income tax expense for the nine months ended September 30, 2017, which includes both federal and state taxes, was \$7.9 million compared to \$6.3 million for the same period of 2016. The combined federal and state effective income tax rate for the nine months ended September 30, 2017 was 31.3%, compared to 35.0% for the same period in 2016. The decrease in the effective tax rate over the prior year period was caused by additional tax credit investments and a change in accounting guidance that requires recording excess tax benefits on equity compensation awards to the income statement. For additional discussion of this guidance, refer to Note 1, Summary of Significant Accounting Policies.

Summary Balance Sheet

(in thousands)	September 30, 2017	December 31, 2016	Increase (decrease)	
Total cash and cash equivalents	\$ 183,108	\$ 198,802	(15,694)	(7.9)%
Securities	679,289	541,260	138,029	25.5 %
Loans	4,030,658	3,158,161	872,497	27.6 %
Non-core acquired loans	34,157	39,769	(5,612)	(14.1)%
Total assets	5,231,488	4,081,328	1,150,160	28.2 %
Deposits	4,059,211	3,233,361	825,850	25.5 %
Total liabilities	4,685,152	3,694,230	990,922	26.8 %
Total shareholders' equity	546,336	387,098	159,238	41.1 %

Assets

Loans by Type

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

(in thousands)	September 30, December 31,		Increase (decrease)	
	2017	2016		
Commercial and industrial	\$ 1,861,935	\$ 1,632,714	\$229,221	14.0 %
Commercial real estate - investor owned	776,425	544,808	231,617	42.5 %
Commercial real estate - owner occupied	555,686	350,148	205,538	58.7 %
Construction and land development	306,410	194,542	111,868	57.5 %
Residential real estate	341,695	240,760	100,935	41.9 %
Consumer and other	154,350	155,420	(1,070)	(0.7)%
Portfolio loans	3,996,501	3,118,392	878,109	28.2 %
Non-core acquired loans	34,157	39,769	(5,612)	(14.1)%
Total loans	\$ 4,030,658	\$ 3,158,161	\$ 872,497	27.6 %

Portfolio loans grew by \$878.1 million, (\$678 million from JCB) to \$4.0 billion at September 30, 2017, when compared to December 31, 2016. Non-core acquired loans totaled \$34.2 million at September 30, 2017, a decrease of \$5.6 million, or 14%, from December 31, 2016, primarily as a result of principal paydowns and accelerated loan payoffs.

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

(in thousands)	At the quarter ended		Increase (decrease)	
	September 30, 2017	December 31, 2016		
Enterprise value lending	\$455,983	\$ 388,798	\$67,185	17.3 %
C&I - general	886,498	794,451	92,047	11.6 %
Life insurance premium financing	330,957	305,779	25,178	8.2 %
Tax credits	188,497	143,686	44,811	31.2 %
CRE, Construction, and land development	1,638,521	1,089,498	549,023	50.4 %
Residential real estate	341,695	240,760	100,935	41.9 %
Consumer and other	154,350	155,420	(1,070)	(0.7)%
Portfolio loans	\$3,996,501	\$ 3,118,392	\$ 878,109	28.2 %

Specialized lending products, especially Enterprise value lending, Life insurance premium financing, and Tax credits, consist of primarily C&I loans, and have contributed significantly to the Company's loan growth. These loans are sourced through relationships developed with estate planning firms and private equity funds, and are not bound geographically by our traditional three markets. These specialized loan products offer opportunities to expand and diversify geographically by entering into new markets. The Company continues to focus on originating high-quality C&I relationships as they typically have variable interest rates and allow for cross selling opportunities involving other banking products. C&I loan growth also supports our efforts to maintain the Company's asset sensitive interest rate risk position. The Company continues to expect portfolio loan growth, excluding the acquisition of JCB, at or above 10% for 2017. For 2018, the Company expects organic loan growth in dollars to be at least equivalent to 2017 levels. With continued organic growth and the impact of the JCB acquisition increasing portfolio loan balances, 2018 portfolio loan growth is expected to be approximately 7% - 9%.

Provision and Allowance for Loan Losses

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

(in thousands)	Three months ended		Nine months ended		
	September 30,		September 30,		
	2017	2016	2017	2016	
Allowance at beginning of period, for portfolio loans	\$36,673	\$35,498	\$37,565	\$33,441	
Loans charged off:					
Commercial and industrial	(613)	(2,044)	(6,781)	(2,269)	
Real estate:					
Commercial	(45)	—	(90)	—	
Construction and land development	—	—	(5)	—	
Residential	(503)	(25)	(777)	(25)	
Consumer and other	(75)	(4)	(143)	(15)	
Total loans charged off	(1,236)	(2,073)	(7,796)	(2,309)	
Recoveries of loans previously charged off:					
Commercial and industrial	205	69	342	624	
Real estate:					
Commercial	18	25	219	123	
Construction and land development	25	913	83	927	
Residential	172	26	259	96	
Consumer and other	13	2	42	9	
Total recoveries of loans	433	1,035	945	1,779	
Net loan charge-offs	(803)	(1,038)	(6,851)	(530)	
Provision for loan losses	2,422	3,038	7,578	4,587	
Allowance at end of period, for portfolio loans (1)	\$38,292	\$37,498	\$38,292	\$37,498	
Allowance at beginning of period, for purchased credit impaired loans	\$5,126	\$8,551	\$5,844	\$10,175	
Loans charged off	(175)	(312)	(223)	(1,295)	
Recoveries of loans	—	—	—	—	
Other	(52)	(612)	(367)	(844)	
Net loan charge-offs	(227)	(924)	(590)	(2,139)	
Provision reversal for purchased credit impaired loan losses	—	(1,194)	(355)	(1,603)	
Allowance at end of period, for purchased credit impaired loans	\$4,899	\$6,433	\$4,899	\$6,433	
Total allowance at end of period	\$43,191	\$43,931	\$43,191	\$43,931	
Portfolio loans, average	\$3,904,636	\$2,947,949	\$3,754,891	\$2,864,916	
Portfolio loans, ending (1)	3,948,676	3,037,705	3,948,676	3,037,705	
Net charge-offs to average portfolio loans (1)	0.08	% 0.14	% 0.24	% 0.02	%
Allowance for portfolio loan losses to loans (1)	0.97	% 1.23	% 0.97	% 1.23	%

(1) Excludes PCI loans.

The provision for loan losses on portfolio loans for the nine months ended September 30, 2017 was \$7.6 million, compared to \$4.6 million for same period in 2016. The provision is reflective of a chargeoff and reserve increase on a single nonperforming relationship, growth in the portfolio, and maintaining a prudent credit risk posture.

There was \$0.4 million of provision reversal for loan losses on PCI loans for the nine months ended September 30, 2017, compared to provision reversal of \$1.6 million for the comparable 2016 period.

The allowance for loan losses on portfolio loans was 0.97% of portfolio loans at September 30, 2017 compared to 1.23% at September 30, 2016. The decrease year over year was due to the addition of the JCB loan portfolio at fair value. Management believes the allowance for loan losses is adequate to absorb inherent losses in the loan portfolio.

Nonperforming assets

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

(in thousands)	September 30, 2017	December 31, 2016	September 30, 2016	
Non-accrual loans	\$8,264	\$12,585	\$17,622	
Restructured loans	721	2,320	2,320	
Total nonperforming loans (1)	8,985	14,905	19,942	
Other real estate from originated loans	251	740	2,719	
Other real estate from acquired loans	240	240	240	
Total nonperforming assets (1) (2)	\$9,476	\$15,885	\$22,901	
Total assets	\$5,231,488	\$4,081,328	\$3,909,644	
Portfolio loans (1)	3,948,676	3,158,161	3,037,705	
Portfolio loans plus other real estate (1)	3,949,167	3,159,141	3,040,664	
Nonperforming loans to portfolio loans (1)	0.23	% 0.47	% 0.66	%
Nonperforming assets to total loans plus other real estate (1) (2)	0.24	0.50	0.75	
Nonperforming assets to total assets (1) (2)	0.18	0.39	0.59	
Allowance for loans to nonperforming loans (1)	426	% 252	% 188	%

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

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

Nonperforming loans

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

Nonperforming loans based on loan type were as follows:

(in thousands)	September 30, 2017	December 31, 2016	September 30, 2016
Commercial and industrial	\$ 7,451	\$ 12,284	\$ 13,160
Commercial real estate	544	655	252
Construction and land development	322	1,904	1,907
Residential real estate	—	62	124
Consumer and other	668	—	4,499
Total	\$ 8,985	\$ 14,905	\$ 19,942

The following table summarizes the changes in nonperforming loans:

(in thousands)	Nine months ended September 30,	
	2017	2016
Nonperforming loans beginning of period	\$ 14,905	\$ 9,100
Additions to nonaccrual loans	8,680	18,354
Additions to restructured loans	676	2,320
Charge-offs	(7,678)	(2,104)
Other principal reductions	(7,315)	(6,058)
Moved to other real estate	(283)	(283)
Moved to performing	—	(1,387)
Loans past due 90 days or more and still accruing interest	—	—
Nonperforming loans end of period	\$ 8,985	\$ 19,942

Other real estate

Other real estate at September 30, 2017, was \$0.5 million, compared to \$3.0 million at September 30, 2016.

The following table summarizes the changes in Other real estate:

(in thousands)	Nine months ended September 30,	
	2017	2016
Other real estate beginning of period	\$ 980	\$ 8,366
Additions and expenses capitalized to prepare property for sale	2,063	2,203
Writedowns in value	(56)	—
Sales	(2,496)	(7,610)
Other real estate end of period	\$ 491	\$ 2,959

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

Liabilities

Liabilities totaled \$4.7 billion at September 30, 2017, compared to \$3.7 billion at December 31, 2016. The increase in liabilities was largely due to a \$826 million increase in total deposits and a \$249 million increase in Federal Home Loan Bank advances, partially offset by a decrease of \$68 million in other borrowings.

Deposits

(in thousands)	September 30, 2017	December 31, 2016	Increase (decrease)	
Demand deposits	\$ 1,047,910	\$ 866,756	181,154	20.9 %
Interest-bearing transaction accounts	814,338	731,539	82,799	11.3 %
Money market accounts	1,375,844	1,050,472	325,372	31.0 %
Savings	203,923	111,435	92,488	83.0 %
Certificates of deposit:				
Brokered	170,701	117,145	53,556	45.7 %
Other	446,495	356,014	90,481	25.4 %
Total deposits	\$ 4,059,211	\$ 3,233,361	825,850	25.5 %
Non-time deposits / total deposits	85	% 85	%	
Demand deposits / total deposits	26	% 27	%	

Total deposits at September 30, 2017 were \$4.1 billion, an increase of 26%, from December 31, 2016, primarily from the acquisition of JCB (\$675 million). The composition of our noninterest bearing deposits remained relatively stable at 26% of total deposits at September 30, 2017 compared to 27% at December 31, 2016.

Shareholders' Equity

Shareholders' equity totaled \$546 million at September 30, 2017, an increase of \$159.2 million from December 31, 2016. Significant activity during the nine months ended September 30, 2017 was as follows:

- Issuance of 3.3 million shares common stock for the JCB acquisition of \$141.7 million,
- Repurchase of 429,955 shares at an average price of \$38.69, or \$16.6 million pursuant to its publicly announced program,
- Net income of \$40.7 million, and
- Dividends paid on common shares of \$7.7 million.

Liquidity and Capital Resources

Liquidity

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

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

The Bank's Asset-Liability Management Committee oversees our liquidity position, the parameters of which are approved by the Bank's Board of Directors. Our liquidity position is monitored monthly by producing a liquidity

report, which measures the amount of liquid versus non-liquid assets and liabilities. Our liquidity management framework includes measurement of several key elements, such as the loan to deposit ratio, a liquidity ratio, and a dependency ratio. The Company's liquidity framework also incorporates contingency planning to assess the nature

and volatility of funding sources and to determine alternatives to these sources. While core deposits and loan and investment repayments are principal sources of liquidity, funding diversification is another key element of liquidity management and is achieved by strategically varying depositor types, terms, funding markets, and instruments.

Parent Company liquidity

The parent company's liquidity is managed to provide the funds necessary to pay dividends to shareholders, service debt, invest in subsidiaries as necessary, and satisfy other operating requirements. The parent company's primary funding sources to meet its liquidity requirements are dividends and payments from the Bank and proceeds from the issuance of equity (i.e. stock option exercises, stock offerings). A \$15 million dividend was paid to the parent company from the Bank in October of 2017. Another source of funding for the parent company includes the issuance of subordinated debentures and other debt instruments.

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

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

The Company has a senior unsecured revolving credit agreement (the "Revolving Agreement") with another bank allowing for borrowings up to \$20 million which is renewed through February 2018. The proceeds can be used for general corporate purposes. The Revolving Agreement is subject to ongoing compliance with a number of customary affirmative and negative covenants as well as specified financial covenants. As of September 30, 2017, there was \$10 million in outstanding balances under the Revolving Agreement, which has subsequently been paid off.

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

Management believes our current level of cash at the holding company of \$13.9 million will be sufficient to meet all projected cash needs for the remainder of 2017.

Bank liquidity

The Bank has a variety of funding sources available to increase financial flexibility. In addition to amounts currently borrowed, at September 30, 2017 the Bank has borrowing capacity of \$423.3 million from the FHLB of Des Moines under blanket loan pledges, and has an additional \$861.2 million available from the Federal Reserve Bank under a pledged loan agreement. The Bank has unsecured federal funds lines with five correspondent banks totaling \$75 million.

Investment securities are another important tool to the Bank's liquidity objectives. Of the \$603.1 million of the securities available for sale at September 30, 2017, \$449.8 million was pledged as collateral for deposits of public institutions, treasury, loan notes, and other requirements. The remaining \$153.3 million could be pledged or sold to

enhance liquidity, if necessary.

In the normal course of business, the Bank enters into certain forms of off-balance sheet transactions, including unfunded loan commitments and letters of credit. These transactions are managed through the Bank's various risk management

45

processes. Management considers both on-balance sheet and off-balance sheet transactions in its evaluation of the Company's liquidity. The Bank has \$1.3 billion in unused commitments as of September 30, 2017. While this commitment level would exhaust the majority of the Company's current liquidity resources, the nature of these commitments is such that the likelihood of funding them in the aggregate at any one time is low.

Capital Resources

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

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

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

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

(in thousands)	September 30, 2017	December 31, 2016	Well Capitalized Minimum %		
Total capital to risk-weighted assets	12.33	% 13.48	% 10.00	%	
Tier 1 capital to risk-weighted assets	10.36	% 10.99	% 8.00	%	
Common equity tier 1 capital to risk-weighted assets	8.93	% 9.52	% 6.50	%	
Leverage ratio (Tier 1 capital to average assets)	9.88	% 10.42	% 5.00	%	
Tangible common equity to tangible assets ¹	8.18	% 8.76	% N/A		
Tier 1 capital	\$ 491,315	\$ 412,865			
Total risk-based capital	584,931	506,349			

¹ Not a required regulatory capital ratio

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

Use of Non-GAAP Financial Measures:

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

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

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

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

Core Performance Measures

(in thousands)	For the Three Months ended			For the Nine Months ended		
	September 30, 2017	June 30, 2017	September 30, 2016	September 30, 2017	September 30, 2016	
Net interest income	\$45,625	\$45,633	\$ 33,830	\$129,900	\$ 100,041	
Less: Incremental accretion income	1,556	2,584	2,296	5,215	8,701	
Core net interest income	44,069	43,049	31,534	124,685	91,340	
Total noninterest income	8,372	7,934	6,976	23,282	20,030	
Less: Gain (loss) on sale of other real estate from non-core acquired loans	—	—	(225)	—	480	
Less: Gain on sale of investment securities	22	—	86	22	86	
Less: Other income from non-core acquired assets	—	—	287	—	526	
Core noninterest income	8,350	7,934	6,828	23,260	18,938	
Total core revenue	52,419	50,983	38,362	147,945	110,278	
Provision for portfolio loans	2,422	3,623	3,038	7,578	4,587	
Total noninterest expense	27,404	32,651	20,814	86,791	62,929	
Less: Other expenses related to non-core acquired loans	19	(16)	270	126	922	
Less: Merger related expenses	315	4,480	302	6,462	302	
Less: Facilities disposal charge	—	389	—	389	—	
Less: Executive severance	—	—	—	—	332	
Less: Other non-core expenses	—	—	—	—	250	
Core noninterest expense	27,070	27,798	20,242	79,814	61,123	
Core income before income tax expense	22,927	19,562	15,082	60,553	44,568	
Total income tax expense	7,856	5,545	6,316	18,507	18,949	
Less: Non-core income tax expense ¹	465	(784)	1,174	(129)	3,673	
Core income tax expense	7,391	6,329	5,142	18,636	15,276	
Core net income	\$15,536	\$13,233	\$ 9,940	\$41,917	\$ 29,292	
Core diluted earnings per share	\$0.66	\$0.56	\$ 0.49	\$1.81	\$ 1.45	
Core return on average assets	1.21	% 1.06	% 1.04	% 1.14	% 1.05	%
Core return on average common equity	11.13	% 9.72	% 10.47	% 10.69	% 10.67	%
Core return on average tangible common equity	14.50	% 12.72	% 11.46	% 13.66	% 11.73	%
Core efficiency ratio	51.64	% 54.52	% 52.77	% 53.95	% 55.43	%

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

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

(in thousands)	Three months ended		Nine months ended		
	September 30,		September 30,		
	2017	2016	2017	2016	
Net interest income	\$46,047	\$34,263	\$131,290	\$101,377	
Less: Incremental accretion income	1,556	2,296	5,215	8,701	
Core net interest income	\$44,491	\$31,967	\$126,075	\$92,676	
Average earning assets	\$4,712,672	\$3,589,080	\$4,539,350	\$3,503,538	
Reported net interest margin	3.88	% 3.80	% 3.87	% 3.87	%
Core net interest margin	3.75	% 3.54	% 3.71	% 3.53	%

Tangible common equity ratio

(in thousands)	September 30, December 31,		
	2017	2016	
Total shareholders' equity	\$546,336	\$387,098	
Less: Goodwill	117,345	30,334	
Less: Intangible assets	11,745	2,151	
Tangible common equity	\$417,246	\$354,613	
Total assets	\$5,231,488	\$4,081,328	
Less: Goodwill	117,345	30,334	
Less: Intangible assets	11,745	2,151	
Tangible assets	\$5,102,398	\$4,048,843	
Tangible common equity to tangible assets	8.18	% 8.76	%

Regulatory Capital to Risk-Weighted Assets

(in thousands)	September 30, 2017	December 31, 2016		
Total shareholders' equity	\$ 546,336	\$ 387,098		
Less: Goodwill	117,345	30,334		
Less: Intangible assets, net of deferred tax liabilities	5,825	800		
Less: Unrealized gains (losses)	(489	) (1,741))
Plus: Other	12	24		
Common equity Tier 1 capital	423,667	357,729		
Plus: Qualifying trust preferred securities	67,600	55,100		
Plus: Other	48	36		
Tier 1 capital	491,315	412,865		
Plus: Tier 2 capital	93,616	93,484		
Total risk-based capital	584,931	506,349		
Total risk-weighted assets determined in accordance with prescribed regulatory requirements	\$ 4,743,393	\$ 3,757,161		
Common equity tier 1 to risk-weighted assets	8.93	%	9.52	%
Tier 1 capital to risk-weighted assets	10.36	%	10.99	%
Total risk-based capital to risk-weighted assets	12.33	%	13.48	%

Critical Accounting Policies

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

Acquisitions

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

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

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

50

Purchased Credit Impaired ("PCI") Loans

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

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

Allowance for Loan Losses on PCI Loans

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

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

ITEM 3: QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

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

Interest Rate Risk

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

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

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

Rate Shock	Annual % change in net interest income
+ 300 bp	4.7%
+ 200 bp	3.2%
+ 100 bp	1.6%
- 100 bp	-6.1%

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

ITEM 4: CONTROLS AND PROCEDURES

Evaluation of Disclosure Controls and Procedures

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

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

Changes to Internal Controls

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

PART II - OTHER INFORMATION

ITEM 1: LEGAL PROCEEDINGS

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

ITEM 1A: RISK FACTORS

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

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

Issuer Purchases of Equity Securities

The following table provides information on repurchases by the Company of its common stock in each month of the quarter ended September 30, 2017.

Period	Total number of shares purchased (a)	Weighted-average price paid per share	Total number of shares purchased as part of publicly announced plans or programs	Maximum number of shares that may yet be purchased under the plans or programs
July 1, 2017 through July 31, 2017	67,201	39.84	67,201	1,747,081
August 1, 2017 through August 31, 2017	123,179	38.70	123,179	1,623,902
September 1, 2017 through September 30, 2017	239,575	38.37	239,575	1,384,327
Total	429,955	\$ 38.69	429,955	1,384,327

(a) In May 2015, the Company's board of directors authorized the repurchase of up to two million shares of the Company's common stock. The repurchases may be made in open market or privately negotiated transactions and the repurchase program will remain in effect until fully utilized or until modified, superseded or terminated. The timing and exact amount of common stock repurchases will depend on a number of factors including, among others, market and general economic conditions, economic capital and regulatory capital considerations, alternative uses of capital, the potential impact on our credit ratings, and contractual and regulatory limitations.

ITEM 5: OTHER INFORMATION

Appointment to the Board of Directors

On October 27, 2017, the Enterprise Board of Directors appointed Michael T. Normile as a Director, filling the current vacancy on the Board. Effective immediately, Mr. Normile will serve as a Director of the Board until the Company's 2018 annual meeting of stockholders (when he is expected to be nominated for election by the stockholders of the Company). The Board of Directors has not yet determined on which board committees Mr. Normile will serve. There are no transactions between the Company and Mr. Normile that would be required to be reported under Item 404(a) of Regulation S-K.

The press release announcing the appointment of Michael T. Normile to the Board is being furnished as Exhibit 99.1 to this Quarterly Statement on Form 10-Q.

ITEM 6: EXHIBITS

Exhibit No. Description

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

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

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

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

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

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

**99.1 Press Release, dated October 27, 2017, entitled "Enterprise Financial Services Corp Names Michael Normile to Board"

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

* Filed herewith

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

SIGNATURES

Pursuant to the requirements of the Securities Exchange Act of 1934, as amended, the Registrant has duly caused this report to be signed on its behalf by the undersigned, thereunto duly authorized, in the City of Clayton, State of Missouri on the day of October 27, 2017.

ENTERPRISE FINANCIAL
SERVICES CORP

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

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