

SECURITIES AND EXCHANGE COMMISSION  
WASHINGTON, D.C. 20549

FORM 10-Q

(Mark One)

Quarterly report pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934.

For the quarterly period ended June 30, 2014 or

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: 0-26128

**NorthWest Indiana Bancorp**

(Exact name of registrant as specified in its charter)

Indiana

(State or other jurisdiction of incorporation  
or organization)

35-1927981

(I.R.S. Employer Identification Number)

9204 Columbia Avenue  
Munster, Indiana

(Address of principal executive offices)

46321

(ZIP code)

Registrant's telephone number, including area code: (219) 836-4400

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

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§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 the 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  Smaller Reporting Company   
(Do not check if a 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

There were 2,844,167 shares of the registrant's Common Stock, without par value, outstanding at August 1, 2014.

**NorthWest Indiana Bancorp**  
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NorthWest Indiana Bancorp  
Consolidated Balance Sheets

(Dollars in thousands)	June 30, 2014 (unaudited)	December 31, 2013
<b>ASSETS</b>		
Cash and non-interest bearing balances in financial institutions	\$ 13,137	\$ 11,758
Interest bearing balances in financial institutions	17,628	9,256
Federal funds sold	200	110
Total cash and cash equivalents	30,965	21,124
Securities available-for-sale	209,379	194,296
Loans held-for-sale	1,830	136
Loans receivable	489,960	437,821
Less: allowance for loan losses	(6,176)	(7,189)
Net loans receivable	483,784	430,632
Federal Home Loan Bank stock	4,392	3,086
Accrued interest receivable	2,680	2,480
Premises and equipment	17,951	17,260
Foreclosed real estate	1,402	1,084
Cash value of bank owned life insurance	16,601	16,396
Goodwill	1,611	-
Other assets	5,732	6,959
Total assets	\$ 776,327	\$ 693,453
<b>LIABILITIES AND STOCKHOLDERS' EQUITY</b>		
Deposits:		
Non-interest bearing	\$ 84,551	\$ 73,430
Interest bearing	555,079	499,463
Total	639,630	572,893
Repurchase agreements	18,437	14,031
Borrowed funds	38,964	30,898
Accrued expenses and other liabilities	6,586	8,870
Total liabilities	703,617	626,692
Stockholders' Equity:		
Preferred stock, no par or stated value; 10,000,000 shares authorized, none outstanding	-	-
Common stock, no par or stated value; 10,000,000 shares authorized; shares issued: June 30, 2014 - 2,901,377 December 31, 2013 - 2,897,202	361	361
shares outstanding: June 30, 2014 - 2,844,167 December 31, 2013 - 2,841,164		
Additional paid in capital	4,032	4,032
Accumulated other comprehensive income/(loss)	382	(3,151)
Retained earnings	67,935	65,519
Total stockholders' equity	72,710	66,761
Total liabilities and stockholders' equity	\$ 776,327	\$ 693,453

See accompanying notes to consolidated financial statements.

NorthWest Indiana Bancorp  
Consolidated Statements of Income  
(unaudited)

	Three Months Ended June 30,		Six Months Ended June 30,	
	2014	2013	2014	2013
<b>Interest income:</b>				
Loans receivable				
Real estate loans	\$ 4,573	\$ 4,196	\$ 8,644	\$ 8,401
Commercial loans	834	754	1,654	1,549
Consumer loans	5	5	9	11
Total loan interest	<u>5,412</u>	<u>4,955</u>	<u>10,307</u>	<u>9,961</u>
Securities	1,502	1,245	2,890	2,496
Other interest earning assets	<u>2</u>	<u>7</u>	<u>7</u>	<u>13</u>
	<u>1,504</u>	<u>1,252</u>	<u>2,897</u>	<u>2,509</u>
<b>Total interest income</b>	<u>6,916</u>	<u>6,207</u>	<u>13,204</u>	<u>12,470</u>
<b>Interest expense:</b>				
Deposits	307	283	582	586
Repurchase agreements	17	17	32	34
Borrowed funds	<u>130</u>	<u>137</u>	<u>256</u>	<u>279</u>
<b>Total interest expense</b>	<u>454</u>	<u>437</u>	<u>870</u>	<u>899</u>
<b>Net interest income</b>	6,462	5,770	12,334	11,571
Provision for loan losses	<u>165</u>	<u>95</u>	<u>410</u>	<u>230</u>
<b>Net interest income after provision for loan losses</b>	<u>6,297</u>	<u>5,675</u>	<u>11,924</u>	<u>11,341</u>
<b>Noninterest income:</b>				
Fees and service charges	703	625	1,297	1,216
Wealth management operations	441	330	819	697
Gain on sale of securities, net	107	316	457	444
Increase in cash value of bank owned life insurance	103	88	205	175
Gain on sale of loans held-for-sale, net	141	139	216	298
Gain/ (loss) on foreclosed real estate, net	(7)	(18)	5	(1)
Other	<u>72</u>	<u>4</u>	<u>88</u>	<u>18</u>
<b>Total noninterest income</b>	<u>1,560</u>	<u>1,484</u>	<u>3,087</u>	<u>2,847</u>
<b>Noninterest expense:</b>				
Compensation and benefits	2,793	2,628	5,439	5,270
Occupancy and equipment	821	741	1,611	1,523
Data processing	284	232	560	472
Marketing	142	159	260	267
Federal deposit insurance premiums	127	131	218	253
Other	<u>1,138</u>	<u>937</u>	<u>2,046</u>	<u>1,838</u>
<b>Total noninterest expense</b>	<u>5,305</u>	<u>4,828</u>	<u>10,134</u>	<u>9,623</u>
<b>Income before income tax expenses</b>	2,552	2,331	4,877	4,565
Income tax expenses	<u>603</u>	<u>624</u>	<u>1,124</u>	<u>1,188</u>
<b>Net income</b>	<u>\$ 1,949</u>	<u>\$ 1,707</u>	<u>\$ 3,753</u>	<u>\$ 3,377</u>
<b>Earnings per common share:</b>				
Basic	\$ 0.69	\$ 0.60	\$ 1.32	\$ 1.19
Diluted	\$ 0.69	\$ 0.60	\$ 1.32	\$ 1.19
<b>Dividends declared per common share</b>	\$ 0.25	\$ 0.22	\$ 0.47	\$ 0.41

See accompanying notes to consolidated financial statements.

NorthWest Indiana Bancorp  
Consolidated Statements of Comprehensive Income  
(unaudited)

(Dollars in thousands)	Three Months Ended June 30,		Six Months Ended June 30,	
	2014	2013	2014	2013
Net income	\$ 1,949	\$ 1,707	\$ 3,753	\$ 3,377
Net change in net unrealized gains and losses on securities available-for-sale:				
Unrealized gains/(losses) arising during the period	2,734	(5,217)	4,901	(6,060)
Less: reclassification adjustment for gains included in net income	(107)	(316)	457	(444)
Net securities gain/(loss) during the period	2,627	(5,533)	5,358	(6,504)
Tax effect	(892)	1,892	(1,821)	2,228
Net of tax amount	1,735	(3,641)	3,537	(4,276)
Net change in unrecognized gain on postretirement benefit:				
Amortization of net actuarial gain	(2)	(1)	(3)	(3)
Net loss during the period	(2)	(1)	(3)	(3)
Tax effect	-	-	-	-
Net of tax amount	(2)	(1)	(3)	(3)
Other comprehensive (loss)/gain, net of tax	1,733	(3,642)	3,534	(4,279)
Comprehensive income/(loss), net of tax	<u>\$ 3,682</u>	<u>\$ (1,935)</u>	<u>\$ 7,287</u>	<u>\$ (902)</u>

See accompanying notes to consolidated financial statements.

NorthWest Indiana Bancorp  
Consolidated Statements of Changes in Stockholders' Equity  
(unaudited)

(Dollars in thousands)	Three Months Ended June 30,		Six Months Ended June 30,	
	2014	2013	2014	2013
Balance at beginning of period	\$ 69,755	\$ 68,115	\$ 66,761	\$ 67,651
Comprehensive income:				
Net income	1,949	1,707	3,753	3,377
Net unrealized change on securities available-for-sale, net of reclassifications and tax effects	1,735	(3,641)	3,537	(4,276)
Amortization of unrecognized gain on postretirement benefit	(2)	(1)	(3)	(3)
Comprehensive income/(loss), net of tax	3,682	(1,935)	7,287	(902)
Stock based compensation expense	15	10	30	16
Sale of treasury stock	-	-	-	22
Stock repurchase	(31)	-	(31)	(57)
Cash dividends	(711)	(626)	(1,337)	(1,166)
Balance at end of period	<u>\$ 72,710</u>	<u>\$ 65,564</u>	<u>\$ 72,710</u>	<u>\$ 65,564</u>

See accompanying notes to consolidated financial statements.

NorthWest Indiana Bancorp  
Consolidated Statements of Cash Flows  
(unaudited)

(Dollars in thousands)	Six Months Ended June 30,	
	2014	2013
<b>CASH FLOWS FROM OPERATING ACTIVITIES:</b>		
Net income	\$ 3,753	\$ 3,377
Adjustments to reconcile net income to net cash (used in)/provided by operating activities:		
Origination of loans for sale	(11,629)	(9,463)
Sale of loans originated for sale	10,147	9,494
Depreciation and amortization, net of accretion	984	1,099
Amortization of mortgage servicing rights	41	84
Stock based compensation expense	30	16
Gain on sale of securities, net	(457)	(444)
Gain on sale of loans held-for-sale, net	(216)	(298)
(Gain)/ loss on foreclosed real estate, net	(5)	1
Provision for loan losses	410	230
Net change in:		
Interest receivable	(200)	149
Other assets	(427)	904
Accrued expenses and other liabilities	(2,919)	(2,328)
Total adjustments	(4,241)	(556)
Net cash - operating activities	(488)	2,821
<b>CASH FLOWS FROM INVESTING ACTIVITIES:</b>		
Proceeds from maturities and pay downs of securities available-for-sale	8,634	23,772
Proceeds from sales of securities available-for-sale	28,737	12,475
Purchases of securities available-for-sale	(43,061)	(40,006)
Loan participations purchased	(427)	-
Net change in loans receivable	(24,131)	253
Proceeds from sales of foreclosed real estate	507	1,609
Cash and cash equivalents from acquisition activity	2,630	-
Purchase of Federal Home Loan Bank Stock	(881)	101
Purchase of premises and equipment, net	(426)	(302)
Increase in cash value of bank owned life insurance	(205)	(175)
Net cash - investing activities	(28,623)	(2,273)
<b>CASH FLOWS FROM FINANCING ACTIVITIES:</b>		
Net change in deposits	29,762	6,319
Proceeds from FHLB advances	47,000	11,000
Repayment of FHLB advances	(39,000)	(11,000)
Change in other borrowed funds	2,472	3,261
Proceeds from sale of treasury stock	-	22
Common stock repurchased	(31)	(57)
Dividends paid	(1,251)	(1,078)
Net cash - financing activities	38,952	8,467
Net change in cash and cash equivalents	9,841	9,015
Cash and cash equivalents at beginning of period	21,124	33,751
Cash and cash equivalents at end of period	\$ 30,965	\$ 42,766
<b>SUPPLEMENTAL DISCLOSURES OF CASH FLOW INFORMATION:</b>		
Cash paid during the period for:		
Interest	\$ 868	\$ 906
Income taxes	793	744
Acquisition activity:		
Fair value of assets acquired, including cash and cash equivalents	\$ 37,906	\$ -
Value of goodwill and other intangible assets	1,704	-
Fair value of liabilities assumed	39,610	-
Noncash activities:		
Transfers from loans to foreclosed real estate	\$ 832	\$ 95

See accompanying notes to consolidated financial statements.

**NorthWest Indiana Bancorp**  
**Notes to Consolidated Financial Statements**

**Note 1 - Basis of Presentation**

The consolidated financial statements include the accounts of NorthWest Indiana Bancorp (the "Bancorp"), its wholly-owned subsidiary, Peoples Bank SB (the "Bank"), and the Bank's wholly-owned subsidiaries, Peoples Service Corporation, NWIN, LLC, NWIN Funding, Incorporated, and Columbia Development Company, LLC. The Bancorp has no other business activity other than being a holding company for the Bank. The Bancorp's earnings are dependent upon the earnings of the Bank. The accompanying unaudited consolidated financial statements were prepared in accordance with instructions for Form 10-Q and, therefore, do not include all disclosures required by U.S. generally accepted accounting principles for complete presentation of consolidated financial statements. In the opinion of management, the consolidated financial statements contain all adjustments necessary to present fairly the consolidated balance sheets of the Bancorp as of June 30, 2014 and December 31, 2013, and the consolidated statements of income, comprehensive income, and changes in stockholders' equity for the three and six months ended June 30, 2014 and 2013 and consolidated statements of cash flows for the six months ended June 30, 2014 and 2013. The income reported for the six month period ended June 30, 2014 is not necessarily indicative of the results to be expected for the full year.

**Note 2 - Use of Estimates**

Preparing financial statements in conformity with U.S. generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets, liabilities and disclosure of contingent assets and liabilities at the date of the consolidated financial statements and the reported amounts of revenue and expenses during the reporting period, as well as the disclosures provided. Actual results could differ from those estimates. Estimates associated with the allowance for loan losses, fair values of foreclosed real estate, loan servicing rights, investment securities, deferred tax assets, goodwill, and the status of contingencies are particularly susceptible to material change in the near term.

**Note 3 - Acquisition Activity**

On April 1, 2014, the Bank acquired First Federal Savings and Loan Association of Hammond ("First Federal"), a federal mutual savings association headquartered in Hammond, Indiana. First Federal operated two banking locations in Hammond and Highland, Indiana. The Bank acquired First Federal by merging First Federal with and into the Bank immediately following First Federal's voluntary supervisory conversion to stock form. The Bank was not required to issue or pay any shares, cash, or other consideration in the merger. The First Federal acquisition added assets with a fair value of \$37.9 million, including securities with a fair value of \$3.8 million, loans receivable with a fair value of \$29.1 million, premises and equipment with a fair value of \$967 thousand, and foreclosed real estate of \$690 thousand. The First Federal acquisition also added liabilities with a fair value of \$39.6 million, including core deposits with a fair value of \$7.2 million and certificates of deposit with a fair value of \$29.8 million. As a result of the differences in the fair value of assets and liabilities, goodwill of \$1.6 million and intangible assets of \$93,000 were also added.

As part of the fair value of loans receivable, a net fair value discount was established for residential real estate, including home equity lines of credit, of \$1.1 million that is being amortized over 55 months on a straight line basis. Approximately \$67,000 of amortization was taken during the quarter ended June 30, 2014. It is estimated that \$134,000 of amortization will occur during the remainder of 2014, \$268,000 of amortization will occur annually through to 2017, and amortization of \$95,000 will occur during 2018.

As part of the fair value of certificates of deposit, a fair value premium was established of \$276,000 that is being amortized over 17 months on a straight line basis. Approximately \$50,000 of amortization was taken during the quarter ended June 30, 2014. It is estimated that \$100,000 of amortization will occur during the remainder of 2014 and \$126,000 of amortization will occur during 2015.

**Note 4 - Securities**

The estimated fair value of available-for-sale securities and the related gross unrealized gains and losses recognized in accumulated other comprehensive income (loss) were as follows:

(Dollars in thousands)	Cost Basis	Gross Unrealized Gains	Gross Unrealized Losses	Estimated Fair Value
<b>June 30, 2014</b>				
U.S. government sponsored entities	\$ 12,500	\$ -	\$ (187)	\$ 12,313
Collateralized mortgage obligations and residential mortgage-backed securities	112,191	1,455	(812)	112,834
Municipal securities	78,951	3,136	(299)	81,788
Collateralized debt obligations	5,208	-	(2,764)	2,444
Total securities available-for-sale	<u>\$ 208,850</u>	<u>\$ 4,591</u>	<u>\$ (4,062)</u>	<u>\$ 209,379</u>
<b>December 31, 2013</b>				
U.S. government sponsored entities	\$ 18,997	\$ -	\$ (637)	\$ 18,360
Collateralized mortgage obligations and residential mortgage-backed securities	101,056	1,181	(1,922)	100,315
Municipal securities	73,864	1,499	(1,710)	73,653
Collateralized debt obligations	5,208	-	(3,240)	1,968
Total securities available-for-sale	<u>\$ 199,125</u>	<u>\$ 2,680</u>	<u>\$ (7,509)</u>	<u>\$ 194,296</u>

The estimated fair value of available-for-sale debt securities at June 30, 2014, by contractual maturity, were as follows. Securities not due at a single maturity date, primarily mortgage-backed securities, are shown separately.

(Dollars in thousands)	Available-for-sale	
	Estimated Fair Value	Tax-Equivalent Yield (%)
<b>June 30, 2014</b>		
Due in one year or less	\$ 1,256	6.55
Due from one to five years	18,602	3.28
Due from five to ten years	23,843	5.40
Due over ten years	52,844	4.71
Collateralized mortgage obligations and residential mortgage-backed securities	112,834	2.66
Total	<u>\$ 209,379</u>	<u>3.57</u>

Sales of available-for-sale securities were as follows for the six months ended:

(Dollars in thousands)	June 30, 2014	June 30, 2013
Proceeds	\$ 28,737	\$ 12,475
Gross gains	728	444
Gross losses	(271)	-

Accumulated other comprehensive income/(loss) balances, net of tax, related to available-for-sale securities, were as follows:

(Dollars in thousands)	Unrealized gain/(loss)
Beginning balance, December 31, 2013	\$ (3,209)
Current period change	3,537
Ending balance, June 30, 2014	<u>\$ 328</u>



Securities with carrying values of approximately \$32,244,000 and \$31,231,000 were pledged as of June 30, 2014 and December 31, 2013, respectively, as collateral for repurchase agreements, public funds, and for other purposes as permitted or required by law.

Securities with unrealized losses at June 30, 2014 and December 31, 2013 not recognized in income are as follows:

(Dollars in thousands)	Less than 12 months		12 months or longer		Total	
	Estimated Fair Value	Unrealized Losses	Estimated Fair Value	Unrealized Losses	Estimated Fair Value	Unrealized Losses
	June 30, 2014					
U.S. government sponsored entities	\$ 995	\$ (5)	\$ 11,318	\$ (182)	\$ 12,313	\$ (187)
Collateralized mortgage obligations and residential mortgage-backed securities	14,036	(48)	32,747	(764)	46,783	(812)
Municipal securities	2,633	(13)	8,901	(286)	11,534	(299)
Collateralized debt obligations	-	-	2,444	(2,764)	2,444	(2,764)
Total temporarily impaired	\$ 17,664	\$ (66)	\$ 55,410	\$ (3,996)	\$ 73,074	\$ (4,062)
Number of securities		16		55		71

(Dollars in thousands)	Less than 12 months		12 months or longer		Total	
	Estimated Fair Value	Unrealized Losses	Estimated Fair Value	Unrealized Losses	Estimated Fair Value	Unrealized Losses
	December 31, 2013					
U.S. government sponsored entities	\$ 18,360	\$ (637)	\$ -	\$ -	\$ 18,360	\$ (637)
Collateralized mortgage obligations and residential mortgage-backed securities	62,748	(1,922)	-	-	62,748	(1,922)
Municipal securities	27,890	(1,571)	1,478	(139)	29,368	(1,710)
Collateralized debt obligations	-	-	1,968	(3,240)	1,968	(3,240)
Total temporarily impaired	\$ 108,998	\$ (4,130)	\$ 3,446	\$ (3,379)	\$ 112,444	\$ (7,509)
Number of securities		117		8		125

Unrealized losses on securities have not been recognized into income because the securities are of high credit quality or have undisrupted cash flows. Management has the intent and ability to hold those securities for the foreseeable future, and the decline in fair value is largely due to changes in interest rates and volatility in securities markets. The fair values are expected to recover as the securities approach maturity.

#### Note 5 - Loans Receivable

	(Dollars in thousands)	
	June 30, 2014	December 31, 2013
	Loans secured by real estate:	
Residential, including home equity	\$ 190,446	\$ 161,932
Commercial real estate, construction & land development, and other dwellings	205,639	195,423
Commercial participations purchased	2,335	1,273
Total loans secured by real estate	398,420	358,628
Consumer loans	436	237
Commercial business	63,530	57,716
Government and other	27,957	21,587
Subtotal	490,343	438,168
Less:		
Net deferred loan origination fees	(210)	(252)
Undisbursed loan funds	(173)	(95)
Loans receivables	\$ 489,960	\$ 437,821

(Dollars in thousands)	Residential Real Estate, Including Home Equity		Commercial Real Estate, Construction & Land Development, and Other Dwellings		Commercial Participations Purchased		Commercial Business Loans		Government Loans		Total

The Bancorp's activity in the allowance for loan losses, by loan segment, is summarized below for the six months ended June 30, 2014:

Allowance for loan losses:	Residential Real Estate, Including Home Equity	Consumer Loans	Commercial Real Estate, Construction & Land Development, and Other Dwellings	Commercial Participations Purchased	Commercial Business Loans	Government Loans	Total
Beginning Balance	\$ 1,444	\$ 12	\$ 4,789	\$ 31	\$ 859	\$ 54	\$ 7,189
Charge-offs	(13)	(12)	(1,418)	-	-	-	(1,443)
Recoveries	2	1	12	2	3	-	20
Provisions	15	28	342	(8)	7	26	410
Ending Balance	\$ 1,448	\$ 29	\$ 3,725	\$ 25	\$ 869	\$ 80	\$ 6,176

The Bancorp's activity in the allowance for loan losses, by loan segment, is summarized below for the six months ended June 30, 2013:

Allowance for loan losses:	Residential Real Estate, Including Home Equity	Consumer Loans	Commercial Real Estate, Construction & Land Development, and Other Dwellings	Commercial Participations Purchased	Commercial Business Loans	Government Loans	Total
Beginning Balance	\$ 1,024	\$ 19	\$ 4,550	\$ 1,608	\$ 1,220	\$ -	\$ 8,421
Charge-offs	(117)	(6)	(333)	-	(438)	-	(894)
Recoveries	1	3	-	-	3	-	7
Provisions	542	(1)	122	(757)	297	27	230
Ending Balance	\$ 1,450	\$ 15	\$ 4,339	\$ 851	\$ 1,082	\$ 27	\$ 7,764

The Bancorp's allowance for loan losses impairment evaluation and loan receivables are summarized below at June 30, 2014:

Ending balance: individually evaluated for impairment	\$ -	\$ -	\$ 367	\$ -	\$ 39	\$ -	\$ 406
Ending balance: collectively evaluated for impairment	\$ 1,448	\$ 29	\$ 3,358	\$ 25	\$ 830	\$ 80	\$ 5,770
<b>LOAN RECEIVABLES</b>							
Ending balance	\$ 190,208	\$ 432	\$ 205,498	\$ 2,335	\$ 63,530	\$ 27,957	\$ 489,960
Ending balance: individually evaluated for impairment	\$ 153	\$ -	\$ 6,470	\$ -	\$ 540	\$ -	\$ 7,163
Ending balance: purchased credit impaired individually evaluated for impairment	\$ 647	\$ -	\$ -	\$ -	\$ -	\$ -	\$ 647
Ending balance: collectively evaluated for impairment	\$ 189,408	\$ 432	\$ 199,028	\$ 2,335	\$ 62,990	\$ 27,957	\$ 482,150

The Bancorp's allowance for loan losses impairment evaluation and loan receivables are summarized below at December 31, 2013:

Ending balance: individually evaluated for impairment	\$ 16	\$ -	\$ 1,657	\$ -	\$ 30	\$ -	\$ 1,703
Ending balance: collectively evaluated for impairment	\$ 1,428	\$ 12	\$ 3,132	\$ 31	\$ 829	\$ 54	\$ 5,486
<b>LOAN RECEIVABLES</b>							
Ending balance	\$ 161,664	\$ 232	\$ 195,349	\$ 1,273	\$ 57,716	\$ 21,587	\$ 437,821
Ending balance: individually evaluated for impairment	\$ 887	\$ -	\$ 8,446	\$ -	\$ 534	\$ -	\$ 9,867
Ending balance: collectively evaluated for impairment	\$ 160,777	\$ 232	\$ 186,903	\$ 1,273	\$ 57,182	\$ 21,587	\$ 427,954

The Bancorp's credit quality indicators, are summarized below at June 30, 2014 and December 31, 2013:

(Dollars in thousands)

Corporate Credit Exposure - Credit Risk Portfolio By Creditworthiness Category

Loan Grades	Commercial Real Estate, Construction & Land Development, and Other Dwellings		Commercial Participations Purchased		Commercial Business Loans		Government Loans	
	2014	2013	2014	2013	2014	2013	2014	2013
2 Moderate risk	\$ -	\$ -	\$ -	\$ -	\$ 4,285	\$ 4,279	\$ -	\$ -
3 Acceptable risk	164,266	150,303	2,109	1,013	46,127	41,474	27,957	21,587
4 Pass/monitor	31,201	33,153	122	260	11,305	11,173	-	-
Special mention (watch)	3,567	3,348	-	-	1,273	88	-	-
5 Substandard	6,464	8,545	104	-	540	702	-	-
6 Doubtful	-	-	-	-	-	-	-	-
7 Total	\$ 205,498	\$ 195,349	\$ 2,335	\$ 1,273	\$ 63,530	\$ 57,716	\$ 27,957	\$ 21,587

(Dollars in thousands)

Consumer Credit Exposure - Credit Risk Profile Based On Payment Activity

	Residential Real Estate, Including Home Equity		Consumer Loans	
	2014	2013	2014	2013
Performing	\$ 187,268	\$ 158,963	\$ 432	\$ 232
Non-performing	2,940	2,701	-	-
Total	\$ 190,208	\$ 161,664	\$ 432	\$ 232

The Bancorp has established a standard loan grading system to assist management, lenders and review personnel in their analysis and supervision of the loan portfolio. The use and application of these grades by the Bancorp is uniform and conforms to regulatory definitions. The loan grading system is as follows:

**2 – Moderate risk**

Borrower consistently internally generates sufficient cash flow to fund debt service, working assets, and some capital expenditures. Risk of default considered low.

**3 – Acceptable risk**

Borrower generates sufficient cash flow to fund debt service, but most working asset and all capital expansion needs are provided from external sources. Profitability ratios and key balance sheet ratios are usually close to peers but one or more ratios (e.g. leverage) may be higher than peer. Earnings may be trending down over the last three years. Borrower may be able to obtain similar financing from other banks with comparable or less favorable terms. Risk of default is acceptable but requires collateral protection.

**4 – Pass/monitor**

The borrower has significant weaknesses resulting from performance trends or management concerns. The financial condition of the company has taken a negative turn and may be temporarily strained. Cash flow may be weak but cash reserves remain adequate to meet debt service. Management weaknesses are evident. Borrowers in this category will warrant more than the normal level of supervision and more frequent reporting.

5 – Special mention (watch)

Special mention credits are considered bankable assets with no apparent loss of principal or interest envisioned but requiring a high level of management attention. Assets in this category are currently protected but are potentially weak. These borrowers are subject to economic, industry, or management factors having an adverse impact upon their prospects for orderly service of debt. The perceived risk in continued lending is considered to have increased beyond the level where such loans would normally be granted. These assets constitute an undue and unwarranted credit risk, but not to the point of justifying a classification of Substandard.

6 – Substandard

This classification consists of loans which are inadequately protected by the current sound worth and paying capacity of the obligor or of the collateral pledged. Financial statements normally reveal some or all of the following: poor trends, lack of earnings and cash flow, excessive debt, lack of liquidity, and the absence of creditor protection. Loans are still considered collectible, but due to increased risks and defined weaknesses of the credit, some loss could be incurred in collection if the deficiencies are not corrected.

7 – Doubtful

This classification consists of loans where the possibility of loss is high after collateral liquidation based upon existing facts, market conditions, and value. Loss is deferred until certain important and reasonably specific pending factors which may strengthen the credit can be exactly determined. These factors may include proposed acquisitions, liquidation procedures, capital injection and receipt of additional collateral, mergers or refinancing plans.

Performing loans are loans that are paying as agreed and are less than ninety days past due on payments of interest and principal.

No loans were modified in a troubled debt restructuring, nor have any previous troubled debt restructurings subsequently defaulted, during the six months ended June 30, 2014. Four residential real estate loans with a pre-modification outstanding recorded investment of \$549 thousand and a post-modification outstanding recorded investment of \$533 thousand qualified as troubled debt restructurings during the first six months of 2013.

<i>(Dollars in thousands)</i>	As of June 30, 2014			For the six months ended June 30, 2014	
	<i>Recorded Investment</i>	<i>Unpaid Principal Balance</i>	<i>Related Allowance</i>	<i>Average Recorded Investment</i>	<i>Interest Income Recognized</i>
<b>With no related allowance recorded:</b>					
Residential real estate, including home equity	\$ 800	\$ 812	\$ -	\$ 160	\$ 9
Commercial real estate, construction & land development, and other dwellings	1,683	2,919	-	956	38
Commercial participations purchased	-	-	-	-	-
Commercial business loans	228	228	-	256	1
<b>With an allowance recorded:</b>					
Residential real estate, including home equity	-	-	-	519	-
Commercial real estate, construction & land development, and other dwellings	4,787	4,787	367	6,795	46
Commercial participations purchased	-	-	-	-	-
Commercial business loans	312	580	39	278	1
<b>Total:</b>					
Residential real estate, including home equity	\$ 800	\$ 812	\$ -	\$ 679	\$ 9
Commercial real estate, construction & land development, and other dwellings	\$ 6,470	\$ 7,706	\$ 367	\$ 7,751	\$ 84
Commercial participations purchased	\$ -	\$ -	\$ -	\$ -	\$ -
Commercial business loans	\$ 540	\$ 808	\$ 39	\$ 534	\$ 2

(Dollars in thousands)	As of December 31, 2013			For the six months ended June 30, 2013	
	Recorded Investment	Unpaid Principal Balance	Related Allowance	Average Recorded Investment	Interest Income Recognized
<b>With no related allowance recorded:</b>					
Residential real estate, including home equity	\$ -	\$ -	\$ -	\$ -	\$ -
Commercial real estate, construction & land development, and other dwellings	617	617	-	791	15
Commercial participations purchased	-	-	-	5,507	29
Commercial business loans	228	228	-	1,037	4
<b>With an allowance recorded:</b>					
Residential real estate, including home equity	887	899	16	831	12
Commercial real estate, construction & land development, and other dwellings	7,829	7,829	1,657	10,004	142
Commercial participations purchased	-	-	-	189	-
Commercial business loans	306	574	30	652	4
<b>Total:</b>					
Residential real estate, including home equity	\$ 887	\$ 899	\$ 16	\$ 831	\$ 12
Commercial real estate, construction & land development, and other dwellings	\$ 8,446	\$ 8,446	\$ 1,657	\$ 10,795	\$ 157
Commercial participations purchased	\$ -	\$ -	\$ -	\$ 5,696	\$ 29
Commercial business loans	\$ 534	\$ 802	\$ 30	\$ 1,689	\$ 8

As part of the acquisition of First Federal, the Bancorp acquired loans for which there was evidence of credit quality deterioration since origination and it was determined that it was probable that the Bancorp would be unable to collect all contractually required principal and interest payments. At June 30, 2014, purchased credit impaired loans with unpaid principal balances totaled \$1.8 million with a recorded investment of \$647,000.

The Bancorp's age analysis of past due loans is summarized below:

	(Dollars in thousands)						Recorded Investments Greater than 90 Days and Accruing
	30-59 Days Past Due	60-89 Days Past Due	Greater Than 90 Days Past Due	Total Past Due	Current	Total Loans	
<b>June 30, 2014</b>							
Residential real estate, including home equity	\$ 4,046	\$ 1,326	\$ 2,422	\$ 7,794	\$ 182,414	\$ 190,208	\$ 64
Consumer loans	-	-	-	-	432	432	-
Commercial real estate, construction & land development, and other dwellings	1,428	147	1,218	2,793	202,705	205,498	529
Commercial participations purchased	-	-	-	-	2,335	2,335	-
Commercial business loans	268	30	443	741	62,789	63,530	-
Government loans	-	-	-	-	27,957	27,957	-
<b>Total</b>	<b>\$ 5,742</b>	<b>\$ 1,503</b>	<b>\$ 4,083</b>	<b>\$ 11,328</b>	<b>\$ 478,632</b>	<b>\$ 489,960</b>	<b>\$ 592</b>
<b>December 31, 2013</b>							
Residential real estate, including home equity	\$ 3,721	\$ 1,090	\$ 1,502	\$ 6,313	\$ 155,351	\$ 161,664	\$ 174
Consumer loans	1	-	-	1	231	232	-
Commercial real estate, construction & land development, and other dwellings	1,083	2,626	768	4,477	190,872	195,349	-
Commercial participations purchased	-	-	-	-	1,273	1,273	-
Commercial business loans	1,032	25	447	1,504	56,212	57,716	-
Government loans	-	-	-	-	21,587	21,587	-
<b>Total</b>	<b>\$ 5,837</b>	<b>\$ 3,741</b>	<b>\$ 2,717</b>	<b>\$ 12,295</b>	<b>\$ 425,526</b>	<b>\$ 437,821</b>	<b>\$ 174</b>

The Bancorp's loans on nonaccrual status are summarized below:

	(Dollars in thousands)	
	June 30, 2014	December 31, 2013
Residential real estate, including home equity	\$ 2,940	\$ 2,526
Consumer loans	-	-
Commercial real estate, construction & land development, and other dwellings	1,253	807
Commercial participations purchased	-	-
Commercial business loans	443	447
Government loans	-	-
<b>Total</b>	<b>\$ 4,636</b>	<b>\$ 3,780</b>

**Note 6 - Foreclosed Real Estate**

Foreclosed real estate at period-end is summarized below:

	(Dollars in thousands)	
	June 30, 2014	December 31, 2013
Residential real estate	\$ 527	\$ 94
Commercial real estate and other dwellings	716	716
Construction and land development	159	274
Total	<u>\$ 1,402</u>	<u>\$ 1,084</u>

**Note 7 – Goodwill and Other Intangible Assets**

The Bancorp established a goodwill balance of \$1.6 million with the acquisition of First Federal. In addition to goodwill, a core deposit intangible of \$93,000 was established and is being amortized over 7.9 years on a straight line basis. Approximately \$3,000 of amortization was taken during the quarter ended June 30, 2014. It is estimated that \$6,000 of amortization will occur during the remainder of 2014 and \$12,000 of amortization will occur annually through to 2020.

**Note 8 - Concentrations of Credit Risk**

The primary lending area of the Bancorp encompasses all of Lake County in northwest Indiana, where a majority of loan activity is concentrated. The Bancorp is also an active lender in Porter County, and to a lesser extent, LaPorte, Newton and Jasper counties in Indiana, and Lake, Cook and Will counties in Illinois. Substantially all loans are secured by specific items of collateral including residences, commercial real estate, land development, business assets and consumer assets.

**Note 9 - Earnings per Share**

Earnings per common share is computed by dividing net income by the weighted-average number of common shares outstanding. A reconciliation of the numerators and denominators of the basic and diluted earnings per common share computations for the three and six months ended June 30, 2014 and 2013 are as follows:

(Dollars in thousands, except per share data)	Three Months Ended June 30,		Six Months Ended June 30,	
	2014	2013	2014	2013
Basic earnings per common share:				
Net income as reported	\$ 1,949	\$ 1,707	\$ 3,753	\$ 3,377
Weighted average common shares outstanding	<u>2,844,218</u>	<u>2,842,820</u>	<u>2,843,897</u>	<u>2,841,308</u>
Basic earnings per common share	<u>\$ 0.69</u>	<u>\$ 0.60</u>	<u>\$ 1.32</u>	<u>\$ 1.19</u>
Diluted earnings per common share:				
Net income as reported	\$ 1,949	\$ 1,707	\$ 3,753	\$ 3,377
Weighted average common shares outstanding	2,844,218	2,842,820	2,843,897	2,841,308
Add: Dilutive effect of assumed stock option exercises	-	-	-	-
Weighted average common and dilutive potential common shares outstanding	<u>2,844,218</u>	<u>2,842,820</u>	<u>2,843,897</u>	<u>2,841,308</u>
Diluted earnings per common share	<u>\$ 0.69</u>	<u>\$ 0.60</u>	<u>\$ 1.32</u>	<u>\$ 1.19</u>

**Note 10 - Stock Based Compensation**

The Bancorp's 2004 Stock Option Plan (the Plan), which is stockholder-approved, permits the grant of share options to its employees for up to 250,000 shares of common stock. Awards granted under the Plan may be in the form of incentive stock options, non-incentive stock options, or restricted stock awards.

As required by the Stock Compensation Topic, companies are required to record compensation cost for stock options and awards provided to employees in return for employment service. For the six months ended June 30, 2014, stock based compensation expense of \$30 thousand was recorded, compared to \$16 thousand for the six months ended June 30, 2013. It is anticipated that current outstanding vested and unvested options and awards will result in additional compensation expense of approximately \$30 thousand in 2014 and \$60 thousand in 2015.

There were no incentive stock options granted during the first six months of 2014 or 2013. When options are granted, the cost is measured at the fair value of the options when granted, and this cost is expensed over the employment service period, which is normally the vesting period of the options or awards. Compensation cost will also be recorded for prior option grants that vest after the date of adoption. A summary of incentive option activity under the Bancorp's incentive stock option plan for the six months ended June 30, 2014 follows:

Incentive options	Shares	Weighted-Average Exercise Price	Weighted-Average Remaining Contractual Term	Aggregate Intrinsic Value
Outstanding at January 1, 2014	6,350	\$ 29.82		
Granted	-	-		
Exercised	-	-		
Forfeited	-	-		
Expired	(5,600)	\$ 30.00		
Outstanding at June 30, 2014	750	\$ 28.50	3.7	-
Exercisable at June 30, 2014	750	\$ 28.50	3.7	-

There were 4,175 shares of restricted stock granted during the first six months of 2014 compared to 6,800 shares granted during the first six months of 2013. Restricted stock awards are issued with an award price equal to the market price of the Bancorp's common stock on the award date and with a five year vesting period. Forfeiture provisions exist for personnel that separate employment before the vesting period expires. A summary of restricted stock activity under the Bancorp's incentive stock option plan for the six months ended June 30, 2014 follows:

Restricted stock	Shares	Weighted-Average Exercise Price	Weighted-Average Grant Date Fair Value	Aggregate Intrinsic Value
Nonvested at January 1, 2014	\$ 11,100	\$ 21.54	\$ 21.54	\$ 55,075
Granted	4,175	26.32	23.33	750
Vested	(2,000)	18.95	18.95	(15,100)
Forfeited	-	-	-	-
Nonvested at June 30, 2014	\$ 13,275	\$ 23.43	\$ 22.77	\$ 40,725

#### Note 11 - Adoption of New Accounting Standards

Update Number 2014-04 – Receivables—Troubled Debt Restructurings by Creditors (Subtopic 310-40): Reclassification of Residential Real Estate Collateralized Consumer Mortgage Loans upon Foreclosure. This amendment is intended to clarify when a creditor should be considered to have received physical possession of residential real estate property collateralizing a consumer mortgage loan such that the loan should be derecognized and the real estate recognized. These amendments clarify that an in substance repossession or foreclosure occurs, and a creditor is considered to have received physical possession of residential real estate property collateralizing a consumer mortgage loan, upon either: (a) the creditor obtaining legal title to the residential real estate property upon completion of a foreclosure; or (b) the borrower conveying all interest in the residential real estate property to the creditor to satisfy that loan through completion of a deed in lieu of foreclosure or through a similar legal agreement. Additional disclosures are required. The amendments are effective for the Bancorp for annual periods and interim periods within those annual periods beginning after December 15, 2014.

#### Note 12 - Fair Value

The Fair Value Measurements Topic establishes a hierarchy that requires an entity to maximize the use of observable inputs and minimize the use of unobservable inputs when measuring fair value. The Topic describes three levels of inputs that may be used to measure fair value:

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

Level 2: Significant other observable inputs other than Level 1 prices such as quoted prices for similar assets or liabilities; quoted prices in markets that are not active; or other inputs that are observable or can be corroborated by observable market data.

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

The fair values of securities available-for-sale are determined on a recurring basis by obtaining quoted prices on nationally recognized securities exchanges or pricing models utilizing significant observable inputs such as matrix pricing, which is a mathematical technique widely used in the industry to value debt securities without relying exclusively on quoted prices for the specific securities but rather by relying on the securities' relationship to other benchmark quoted securities. Different judgments and assumptions used in pricing could result in different estimates of value. In certain cases where market data is not readily available because of a lack of market activity or little public disclosure, values may be based on unobservable inputs and classified in Level 3 of the fair value hierarchy.

At the end of each reporting period, securities held in the investment portfolio are evaluated on an individual security level for other-than-temporary impairment in accordance with the Investments – Debt and Equity Securities Topic. Impairment is other-than-temporary if the decline in the fair value is below its amortized cost and it is probable that all amounts due according to the contractual terms of a debt security will not be received. Significant judgments are required in determining impairment, which include making assumptions regarding the estimated prepayments, loss assumptions and the change in interest rates. The Bancorp considers the following factors when determining an other-than-temporary impairment for a security: the length of time and the extent to which the market value has been less than amortized cost; the financial condition and near-term prospects of the issuer; the underlying fundamentals of the relevant market and the outlook for such market for the near future; an assessment of whether the Bancorp (1) has the intent to sell the debt securities or (2) more likely than not will be required to sell the debt securities before their anticipated market recovery. If either of these conditions is met, management will recognize other-than-temporary impairment. If, in management's judgment, an other-than-temporary impairment exists, the cost basis of the security will be written down for the credit loss, and the unrealized loss will be transferred from accumulated other comprehensive loss as an immediate reduction of current earnings.

For the quarter ended June 30, 2014, the Bancorp's management utilized a specialist to perform an other-than-temporary impairment analysis for each of its four pooled trust preferred securities. The analysis utilizes analytical models used to project future cash flows for the pooled trust preferred securities based on current assumptions for prepayments, default and deferral rates, and recoveries. The projected cash flows are then tested for impairment consistent with the Investments – Other Topic and the Investments – Debt and Equity Securities Topic. The other-than-temporary impairment testing compares the present value of the cash flows from quarter to quarter to determine if there is a "favorable" or "adverse" change. Other-than-temporary impairment is recorded if the projected present value of cash flows is lower than the book value of the security. To perform the quarterly other-than-temporary impairment analysis, management utilizes current reports issued by the trustee, which contain principal and interest tests, waterfall distributions, note valuations, collection detail and credit ratings for each pooled trust preferred security. In addition, a detailed review of the performing collateral was performed. The review of the collateral began with a review of financial information provided by SNL Financial, a comprehensive database, widely used in the industry, which gathers financial data on banks and thrifts from U.S. GAAP financial statements for public companies (annual and quarterly reports on Forms 10-K and 10-Q, respectively), as well as regulatory reports for private companies, including consolidated financial statements for bank holding companies (FR Y-9C reports) and parent company-only financial statements for bank holding companies (FR Y-9LP reports) filed with the Federal Reserve, and bank call reports filed with the FDIC and the Office of the Comptroller of Currency. Using the information sources described above, for each bank and thrift examined the following items were examined: nature of the issuer's business, years of operating history, corporate structure, loan composition and loan concentrations, deposit mix, asset growth rates, geographic footprint and local economic environment. The issuers' historical financial performance was reviewed and their financial ratios were compared to appropriate peer groups of regional banks or thrifts with similar asset sizes. The analysis focused on six broad categories: profitability (revenue streams and earnings quality, return on assets and shareholder's equity, net interest margin and interest rate sensitivity), credit quality (charge-offs and recoveries, non-current loans and total non-performing assets as a percentage of total loans, loan loss reserve coverage and the adequacy of the loan loss provision), operating efficiency (non-interest expense compared to total revenue), capital adequacy (Tier-1, total capital and leverage ratios and equity capital growth), leverage (tangible equity as a percentage of tangible assets, short-term and long-term borrowings and double leverage at the holding company) and liquidity (the nature and availability of funding sources, net non-core funding dependence and quality of deposits). In addition, for publicly traded companies' stock price movements were reviewed and the market price of publicly traded debt instruments was examined. The other-than-temporary impairment analysis indicated that the Bancorp's four pooled trust preferred securities had no additional other-than-temporary impairment during the quarter ended June 30, 2014.



The table below shows the credit loss roll forward on a year-to-date basis for the Bancorp's pooled trust preferred securities that have been classified with other-than-temporary impairment:

	(Dollars in thousands)	
	Other-than-temporary impairment	
Ending balance, December 31, 2013	\$	271
Additions not previously recognized		-
Ending balance, June 30, 2014	\$	271

The following table contains information regarding the Bancorp's pooled trust preferred securities as of June 30, 2014:

(Dollars in thousands)

Cusip	74043CAC1	74042TAJ0	01449TAB9	01450NAC6
Deal name	PreTSL XXIV	PreTSL XXVII	Alesco IX	Alesco XVII
Class	B-1	C-1	A-2A	B
Book value	\$ 1,257	\$ 1,296	\$ 1,303	\$ 1,352
Fair value	\$ 533	\$ 522	\$ 832	\$ 557
Unrealized gains/(losses)	\$ (724)	\$ (774)	\$ (471)	\$ (795)
Lowest credit rating assigned	CC	C	BB	CC
Number of performing banks	53	30	55	46
Number of performing insurance companies	13	7	10	n/a
Number of issuers in default	17	9	1	3
Number of issuers in deferral	10	3	10	7
Defaults & deferrals as a % of performing collateral	40.78%	25.75%	17.22%	22.89%
Subordination:				
As a % of performing collateral	6.65%	-2.41%	41.15%	22.09%
As a % of performing collateral - adjusted for projected future defaults	-0.92%	-11.80%	37.39%	17.38%
Other-than-temporary impairment model assumptions:				
Defaults:				
Year 1 - issuer average	2.50%	2.80%	2.00%	1.90%
Year 2 - issuer average	2.50%	2.80%	2.00%	1.90%
Year 3 - issuer average	2.50%	2.80%	2.00%	1.90%
> 3 Years - issuer average	(1)	(1)	(1)	(1)
Discount rate - 3 month Libor, plus implicit yield spread at purchase	1.48%	1.23%	1.27%	1.44%
Recovery assumptions	(2)	(2)	(2)	(2)
Prepayments	0.00%	0.00%	0.00%	0.00%
Other-than-temporary impairment	\$ 41	\$ 132	\$ 36	\$ 62

(1) - Default rates > 3 years are evaluated on a issuer by issuer basis and range from 0.25% to 5.00%.

(2) - Recovery assumptions are evaluated on a issuer by issuer basis and range from 0% to 15% with a five year lag.

In the table above, the Bancorp's subordination for each trust preferred security is calculated by taking the total performing collateral and subtracting the sum of the total collateral within the Bancorp's class and the total collateral within all senior classes, and then stating this result as a percentage of the total performing collateral. This measure is an indicator of the level of collateral that can default before potential cash flow disruptions may occur. In addition, management calculates subordination assuming future collateral defaults by utilizing the default/deferral assumptions in the Bancorp's other-than-temporary-impairment analysis. Subordination assuming future default/deferral assumptions is calculated by deducting future defaults from the current performing collateral. At June 30, 2014, management reviewed the subordination levels for each security in context of the level of current collateral defaults and deferrals within each security; the potential for additional defaults and deferrals within each security; the length of time that the security has been in "payment in kind" status; and the Bancorp's class position within each security.

Management calculated the other-than-temporary impairment model assumptions based on the specific collateral underlying each individual security. The following assumption methodology was applied consistently to each of the four pooled trust preferred securities: For collateral that has already defaulted, no recovery was assumed; no cash flows were assumed from collateral currently in deferral, with the exception of the recovery assumptions. The default and recovery assumptions were calculated based on a detailed collateral review. The discount rate assumption used in the calculation of the present value of cash flows is based on the discount margin (i.e., credit spread) at the time each security was purchased using the original purchase price. The discount margin is then added to the appropriate 3-month LIBOR forward rate obtained from the forward LIBOR curve.

At June 30, 2014, three of the trust preferred securities with a cost basis of \$3.9 million continue to be in “payment in kind” status. The Bancorp’s securities that are classified as “payment in kind” are a result of not receiving the scheduled quarterly interest payments. For the securities in “payment in kind” status, management anticipates to receive the unpaid contractual interest payments from the issuer, because of the self-correcting cash flow waterfall provisions within the structure of the securities. When a tranche senior to the Bancorp’s position fails the coverage test, the Bancorp’s interest cash flows are paid to the senior tranche and recorded as a reduction of principal. The coverage test represents an over collateralization target by stating the balance of the performing collateral as a percentage of the balance of the Bancorp’s tranche, plus the balance of all senior tranches. The principal reduction in the senior tranche continues until the appropriate coverage test is passed. As a result of the principal reduction in the senior tranche, more cash is available for future payments to the Bancorp’s tranche. Consistent with the Investments – Debt and Equity Securities Topic, management considered the failure of the issuer of the security to make scheduled interest payments in determining whether a credit loss existed. Management will not capitalize the “payment in kind” interest payments to the book value of the securities and will keep these securities in non-accrual status until the quarterly interest payments resume.

#### Assets and Liabilities Measured on a Recurring Basis

There were no transfers to or from Levels 1 and 2 during the six months ended June 30, 2014. Assets measured at fair value on a recurring basis are summarized below:

(Dollars in thousands)	Estimated Fair Value	Fair Value Measurements at June 30, 2014 Using		
		Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
Available-for-sale debt securities				
U.S. government sponsored entities	\$ 12,313	\$ -	\$ 12,313	\$ -
Collateralized mortgage obligations and residential mortgage-backed securities	112,834	-	112,834	-
Municipal securities	81,788	-	81,788	-
Collateralized debt obligations	2,444	-	-	2,444
Total securities available-for-sale	<u>\$ 209,379</u>	<u>\$ -</u>	<u>\$ 206,935</u>	<u>\$ 2,444</u>

(Dollars in thousands)	Estimated Fair Value	Fair Value Measurements at December 31, 2013 Using		
		Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
Available-for-sale debt securities				
U.S. government sponsored entities	\$ 18,360	\$ -	\$ 18,360	\$ -
Collateralized mortgage obligations and residential mortgage-backed securities	100,315	-	100,315	-
Municipal securities	73,653	-	73,653	-
Collateralized debt obligations	1,968	-	-	1,968
Total securities available-for-sale	<u>\$ 194,296</u>	<u>\$ -</u>	<u>\$ 192,328</u>	<u>\$ 1,968</u>

A roll forward of available-for-sale securities, which require significant adjustment based on unobservable data, are presented in the following table:

(Dollars in thousands)	Fair Value Measurements Using Significant Unobservable Inputs (Level 3)
	Available-for-sale securities
Beginning balance, December 31, 2013	\$ 1,968
Transfers in and/or (out) of Level 3	-
Total gains or (losses)	
Included in earnings	-
Included in other comprehensive income	476
Purchases, issuances, sales, and settlements	
Purchases	-
Issuances	-
Sales	-
Settlements	-
Ending balance, June 30, 2014	<u>\$ 2,444</u>

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

(Dollars in thousands)	Fair Value Measurements at June 30, 2014 Using			
	Estimated Fair Value	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
Impaired loans	\$ 7,404	\$ -	\$ -	\$ 7,404
Foreclosed real estate	1,402	-	-	1,402

  

(Dollars in thousands)	Fair Value Measurements at December 31, 2013 Using			
	Estimated Fair Value	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
Impaired loans	\$ 8,164	\$ -	\$ -	\$ 8,164
Foreclosed real estate	1,084	-	-	1,084

The fair value of impaired loans with specific allocations of the allowance for loan losses or loans for which charge-offs have been taken is generally based on a present value of cash flows or, for collateral dependent loans, based on recent real estate appraisals. Appraisals may utilize a single valuation approach or a combination of approaches including comparable sales and the income approach. The recorded investment of impaired loans was \$7.8 million and the related specific reserves totaled \$406 thousand, resulting in a fair value of impaired loans totaling \$7.4 million, at June 30, 2014. The recorded investment of impaired loans was \$9.9 million and the related specific reserves totaled \$1.7 million, resulting in a fair value of impaired loans totaling \$8.2 million, at December 31, 2013. Fair value is determined, where possible, using market prices derived from an appraisal or evaluation, which are considered to be Level 2 inputs. However, certain assumptions and unobservable inputs are often used by the appraiser, therefore, qualifying the assets as Level 3 in the fair value hierarchy. The fair value of foreclosed real estate is similarly determined by using the results of recent real estate appraisals. The numerical range of unobservable inputs for these valuation assumptions is not meaningful to this presentation.

The following table shows carrying values and related estimated fair values of financial instruments as of the dates indicated. Estimated fair values are further categorized by the inputs used to measure fair value. Items that are not financial instruments are not included.

(Dollars in thousands)	June 30, 2014		Estimated Fair Value Measurements at June 30, 2014 Using		
	Carrying Value	Estimated Fair Value	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
<b>Financial assets:</b>					
Cash and cash equivalents	\$ 30,965	\$ 30,965	\$ 30,965	\$ -	\$ -
Securities available-for-sale	209,379	209,379	-	206,935	2,444
Loans held-for-sale	1,830	1,852	1,852	-	-
Loans receivable, net	483,784	479,657	-	-	479,657
Federal Home Loan Bank stock	4,392	4,392	-	4,392	-
Accrued interest receivable	2,680	2,680	-	2,680	-
<b>Financial liabilities:</b>					
Non-interest bearing deposits	84,551	84,551	84,551	-	-
Interest bearing deposits	555,079	555,216	395,331	159,885	-
Repurchase agreements	18,437	18,446	12,577	5,869	-
Borrowed funds	38,964	39,049	936	38,113	-
Accrued interest payable	49	49	-	49	-

(Dollars in thousands)	December 31, 2013		Estimated Fair Value Measurements at December 31, 2013 Using		
	Carrying Value	Estimated Fair Value	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
<b>Financial assets:</b>					
Cash and cash equivalents	\$ 21,124	\$ 21,124	\$ 21,124	\$ -	\$ -
Securities available-for-sale	194,296	194,296	-	192,328	1,968
Loans held-for-sale	136	138	138	-	-
Loans receivable, net	430,632	427,719	-	-	427,719
Federal Home Loan Bank stock	3,086	3,086	-	3,086	-
Accrued interest receivable	2,480	2,480	-	2,480	-
<b>Financial liabilities:</b>					
Non-interest bearing deposits	73,430	73,430	73,430	-	-
Interest bearing deposits	499,463	499,470	343,847	155,623	-
Repurchase agreements	14,031	14,043	8,042	6,001	-
Borrowed funds	30,898	30,956	799	30,157	-
Accrued interest payable	47	47	-	47	-

The following methods were used to estimate the fair value of financial instruments presented in the preceding table for the periods ended June 30, 2014 and December 31, 2013:

Cash and cash equivalents carrying amounts approximate fair value. The fair values of securities available-for-sale are obtained from broker pricing (Level 2), with the exception of collateralized debt obligations, which are valued by a third-party specialist (Level 3). Loans held-for-sale comprise residential mortgages and are priced based on values established by the secondary mortgage markets (Level 1). The estimated fair value for net loans receivable is based on estimates of the rate the Bancorp would charge for similar such loans, applied for the time period until estimated repayment, in addition to appraisals which may utilize a single valuation approach or a combination of approaches including comparable sales and the income approach (Level 3). Federal Home Loan Bank stock is estimated at book value due to restrictions that limit the sale or transfer of the security. Fair value of accrued interest receivable and payable approximates book value, as the carrying values are determined using the observable interest rate, balance, and last payment date.

Non-interest and interest bearing deposits, which include checking, savings, and money market deposits, are estimated to have fair values based on the amount payable as of the reporting date (Level 1). The fair value of fixed-maturity certificates of deposit (included in interest bearing deposits) are based on estimates of the rate the Bancorp would pay on similar deposits, applied for the time period until maturity (Level 2). Estimated fair values for short-term repurchase agreements, which represent sweeps from demand deposits to accounts secured by pledged securities, are estimated based on the amount payable as of the reporting date (Level 1). Longer-term repurchase agreements, with contractual maturity dates of three months or more, are based on estimates of the rate the Bancorp would pay on similar deposits, applied for the time period until maturity (Level 2). Short-term borrowings are generally only held overnight, therefore, their carrying amount is a reasonable estimate of fair value (Level 1). The fair value of FHLB Advances (included in borrowed funds) are estimated by discounting the future cash flows using quoted rates from the FHLB for similar advances with similar maturities (Level 2). The estimated fair value of other financial instruments, and off-balance sheet loan commitments, approximate cost and are not considered significant to this presentation.

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

### Summary

NorthWest Indiana Bancorp (the "Bancorp") is a bank holding company registered with the Board of Governors of the Federal Reserve System. Peoples Bank SB ("the Bank"), an Indiana savings bank, is a wholly-owned subsidiary of the Bancorp. The Bancorp has no other business activity other than being the holding company for the Bank.

At June 30, 2014, the Bancorp had total assets of \$776.3 million, total loans of \$483.8 million and total deposits of \$639.6 million. Stockholders' equity totaled \$72.7 million or 9.37% of total assets, with a book value per share of \$25.56. Net income for the quarter ended June 30, 2014, was \$1.9 million, or \$0.69 earnings per common share for both basic and diluted calculations. For the quarter ended June 30, 2014, the return on average assets (ROA) was 1.02%, while the return on average stockholders' equity (ROE) was 10.77%. For the six months ended June 30, 2014, the Bancorp recorded net income of \$3.8 million, or \$1.32 earnings per basic and diluted share. For the six months ended June 30, 2014, the ROA was 1.02%, while the ROE was 10.59%.

### Recent Developments

**The Current Economic and Regulatory Environment.** We continue to operate in an uncertain economic and regulatory environment, which presents risks associated with our business. In this regard, the 2010 Dodd-Frank Wall Street Reform and Consumer Protection Act (the "Dodd-Frank Act") contains comprehensive provisions governing the practices and oversight of large and small financial institutions alike, including several provisions that profoundly affect the regulation of community banks, thrifts, and small bank and thrift holding companies, such as the Bancorp. The Dodd-Frank Act also established a new financial regulator, the Consumer Financial Protection Bureau (the "CFPB"), which has broad authority to regulate consumer financial products and services and entities offering such products and services, including banks. Additional legislative or regulatory action that may impact our business may result from the numerous provisions and multiple studies mandated under the Dodd-Frank Act.

The evolving regulatory environment causes uncertainty with respect to the manner in which we conduct our business and requirements that may be imposed by our regulators. Regulators have implemented and continue to propose new regulations and supervisory guidance and have been increasing their examination and enforcement action activities. We expect that regulators will continue taking formal enforcement actions against financial institutions in addition to addressing supervisory concerns through non-public supervisory actions or criticisms. We are unable to predict the nature, extent or impact of any additional changes to statutes or regulations, including the interpretation, implementation or enforcement thereof, that may occur in the future.

The impact of the evolving regulatory environment on our business and operations depends upon final implementation of regulations and guidance issued by the regulatory agencies, the actions of our competitors and other marketplace participants, and the behavior of consumers. Regulatory actions could require us to limit or change our business practices, limit our ability to pursue business opportunities, limit our product offerings, require continued investment of management time and resources in compliance efforts, limit fees we can charge for services, require us to meet more stringent capital, liquidity, and leverage ratio requirements (including those under Basel III, as discussed below), increase costs, impact the value of our assets, or otherwise adversely affect our business.

Compliance and other regulatory requirements and expenditures have increased for the Bancorp and other financial institutions, and we expect them to continue to increase as regulators adopt new rules and increase their scrutiny of financial institutions, including controls and operational processes. The additional expense, time, and resources needed to comply with ongoing regulatory requirements may impact our business and results of operations.

**Regulatory Capital Rules.** On July 2, 2013, the Federal Reserve approved final rules that substantially amend the regulatory risk-based capital rules applicable to the Bancorp and the Bank. The FDIC and the Office of the Comptroller of the Currency ("OCC") have subsequently approved these rules. The final rules were adopted following the issuance of proposed rules by the Federal Reserve in June 2012, and implement the "Basel III" regulatory capital reforms and changes required by the Dodd-Frank Act. "Basel III" refers to two consultative documents released by the Basel Committee on Banking Supervision in December 2009, the rules text released in December 2010, and loss absorbency rules issued in January 2011, which include significant changes to bank capital, leverage and liquidity requirements.

The rules include new risk-based capital and leverage ratios, which will be phased in from 2015 to 2019, and refine the definition of what constitutes “capital” for purposes of calculating those ratios. The new minimum capital level requirements applicable to the Bancorp and the Bank under the final rules will be: (i) a new common equity Tier 1 capital ratio of 4.5%; (ii) a Tier 1 capital ratio of 6% (increased from 4%); (iii) a total capital ratio of 8% (unchanged from current rules); and (iv) a Tier 1 leverage ratio of 4% for all institutions. The final rules also establish a “capital conservation buffer” above the new regulatory minimum capital requirements, which must consist entirely of common equity Tier 1 capital. The capital conservation buffer will be phased-in over four years beginning on January 1, 2016, as follows: the maximum buffer will be 0.625% of risk-weighted assets for 2016, 1.25% for 2017, 1.875% for 2018, and 2.5% for 2019 and thereafter. This will result in the following minimum ratios beginning in 2019: (i) a common equity Tier 1 capital ratio of 7.0%, (ii) a Tier 1 capital ratio of 8.5%, and (iii) a total capital ratio of 10.5%. Under the final rules, institutions are subject to limitations on paying dividends, engaging in share repurchases, and paying discretionary bonuses if its capital level falls below the buffer amount. These limitations establish a maximum percentage of eligible retained income that could be utilized for such actions.

Basel III provided discretion for regulators to impose an additional buffer, the “countercyclical buffer,” of up to 2.5% of common equity Tier 1 capital to take into account the macro-financial environment and periods of excessive credit growth. However, the final rules permit the countercyclical buffer to be applied only to “advanced approach banks” (i.e., banks with \$250 billion or more in total assets or \$10 billion or more in total foreign exposures), which currently excludes the Bancorp and the Bank. The final rules also implement revisions and clarifications consistent with Basel III regarding the various components of Tier 1 capital, including common equity, unrealized gains and losses, as well as certain instruments that will no longer qualify as Tier 1 capital, some of which will be phased out over time. However, the final rules provide that small depository institution holding companies with less than \$15 billion in total assets as of December 31, 2009 (which includes the Bancorp) will be able to permanently include non-qualifying instruments that were issued and included in Tier 1 or Tier 2 capital prior to May 19, 2010 in additional Tier 1 or Tier 2 capital until they redeem such instruments or until the instruments mature.

The final rules also contain revisions to the prompt corrective action framework, which is designed to place restrictions on insured depository institutions, including the Bank, if their capital levels begin to show signs of weakness. These revisions take effect January 1, 2015. Under the prompt corrective action requirements, which are designed to complement the capital conservation buffer, insured depository institutions will be required to meet the following increased capital level requirements in order to qualify as “well capitalized:” (i) a new common equity Tier 1 capital ratio of 6.5%; (ii) a Tier 1 capital ratio of 8% (increased from 6%); (iii) a total capital ratio of 10% (unchanged from current rules); and (iv) a Tier 1 leverage ratio of 5% (increased from 4%).

The final rules set forth certain changes for the calculation of risk-weighted assets, which we will be required to utilize beginning January 1, 2015. The standardized approach final rule utilizes an increased number of credit risk exposure categories and risk weights, and also addresses: (i) an alternative standard of creditworthiness consistent with Section 939A of the Dodd-Frank Act; (ii) revisions to recognition of credit risk mitigation; (iii) rules for risk weighting of equity exposures and past due loans; (iv) revised capital treatment for derivatives and repo-style transactions; and (v) disclosure requirements for top-tier banking organizations with \$50 billion or more in total assets that are not subject to the “advance approach rules” that apply to banks with greater than \$250 billion in consolidated assets. Based on our current capital composition and levels, we believe that we would be in compliance with the requirements as set forth in the final rules if they were presently in effect.

**Volcker Rule.** In December 2013, five federal agencies adopted a final regulation implementing the Volcker Rule provision of the Dodd-Frank Act (the “Volcker Rule”). The Volcker Rule places limits on the trading activity of insured depository institutions and entities affiliated with a depository institution, subject to certain exceptions. In this regard, the final Volcker Rule prohibits banking entities from (i) engaging in short-term proprietary trading for their own accounts, and (ii) having certain ownership interests in and relationships with hedge funds or private equity funds. The final rule is intended to provide greater clarity with respect to both the extent of those primary prohibitions and of the related exemptions and exclusions. The Volcker Rule also requires each regulated entity to establish an internal compliance program that is consistent with the extent to which it engages in activities covered by the rule, which must include (for the largest entities) making regular reports about those activities to regulators. Although the final Volcker Rule provides some tiering of compliance and reporting obligations based on size, the fundamental prohibitions of the rule apply to banking entities of any size, including the Bancorp and the Bank. The final rule became effective April 1, 2014, but the conformance period has been extended from its statutory end date of July 21, 2014 until July 21, 2015. The Bancorp continues to evaluate the implications of the final Volcker Rule on its investments and does not expect any material financial implications.

Under the final Volcker Rule, banking entities would have been prohibited from owning certain collateralized debt obligations (“CDOs”) backed by trust preferred securities (“TruPS”) as of July 21, 2015, which could have forced banking entities to recognize unrealized market losses based on the inability to hold any such investments to maturity. However, on January 14, 2014, the federal bank regulatory agencies issued an interim rule, effective April 1, 2014, exempting TruPS CDOs from the Volcker Rule if (i) the CDO was established prior to May 19, 2010, (ii) the banking entity reasonably believes that the offering proceeds of the CDO were used to invest primarily in TruPS issued by banks with less than \$15 billion in assets, and (iii) the banking entity acquired the CDO on or before December 10, 2013. The Bancorp currently does not have any impermissible holdings of TruPS CDOs under the interim rule, and therefore, will not be required to divest any such investments or change their accounting treatment.

**Acquisition Activity.** On April 1, 2014, the Bank successfully complete the acquisition of First Federal Savings and Loan Association of Hammond ("First Federal"), a federal mutual savings association headquartered in Hammond, Indiana. First Federal operated two banking locations in Hammond and Highland, Indiana. The Bank acquired First Federal by merging First Federal with and into the Bank immediately following First Federal's voluntary supervisory conversion to stock form. The Bank was not required to issue or pay any shares, cash, or other consideration in the merger. The First Federal acquisition added assets with a fair value of \$38.0 million, liabilities with a fair value of \$39.6 million, and goodwill of \$1.6 million.

### Financial Condition

During the six months ended June 30, 2014, total assets increased by \$82.9 million (12.0%), with interest-earning assets increasing by \$78.7 million (12.2%). At June 30, 2014, interest-earning assets totaled \$723.4 million compared to \$644.7 million at December 31, 2013. Earning assets represented 93.2% of total assets at June 30, 2014, compared to 93.0% at December 31, 2013. Growth in total assets and interest earning assets for the six months was a combination of strong internal growth, as well the acquisition of First Federal (see Note 3 - Acquisition Activity).

Loans receivable totaled \$483.8 million at June 30, 2014, compared to \$430.6 million at December 31, 2013. The loan portfolio, which is the Bancorp's largest asset, is the primary source of both interest and fee income. The Bancorp's lending strategy emphasizes quality loan growth, product diversification, and competitive and profitable pricing.

The Bancorp's end-of-period loan balances were as follows:

(Dollars in thousands)	June 30, 2014 (unaudited)		December 31, 2013	
	Balance	% Loans	Balance	% Loans
Construction & land development	\$ 24,496	5.0%	\$ 21,462	4.9%
1-4 first liens	162,898	33.2%	141,186	32.2%
Multifamily	31,770	6.5%	30,782	7.0%
Commercial real estate	151,566	30.9%	144,378	33.0%
Commercial business	63,530	13.0%	57,716	13.2%
1-4 Junior Liens	1,331	0.3%	1,186	0.3%
HELOC	23,719	4.8%	16,903	3.9%
Lot loans	2,260	0.5%	2,389	0.5%
Consumer	432	0.1%	232	0.1%
Government and other	27,958	5.7%	21,587	4.9%
<b>Total loans</b>	<b>\$ 489,960</b>	<b>100.0%</b>	<b>\$ 437,821</b>	<b>100.0%</b>
<b>Adjustable rate loans / total loans</b>	<b>\$ 281,343</b>	<b>57.4%</b>	<b>\$ 261,329</b>	<b>59.7%</b>

	June 30, 2014 (unaudited)	December 31, 2013
Total loans to total assets	63.1%	63.1%
Total loans to earning assets	67.7%	67.9%
Total loans to total deposits	76.6%	76.4%

The Bancorp is primarily a portfolio lender. Mortgage banking activities historically have been limited to the sale of fixed rate mortgage loans with contractual maturities greater than 15 years. These loans are identified as held for sale when originated and sold, on a loan-by-loan basis, in the secondary market. The Bancorp will also retain fixed rate mortgage loans with a contractual maturity greater than 15 years on a limited basis. During the six months ended June 30, 2014, the Bancorp sold \$10.1 million in newly originated fixed rate mortgage loans, compared to \$9.5 million during the six months ended June 30, 2013. Net gains realized from the mortgage loan sales totaled \$216 thousand for the six months ended June 30, 2014, compared to \$298 thousand for the six months ended June 30, 2013. At June 30, 2014, the Bancorp had \$1.8 million in loans that were classified as held for sale, compared to \$136 thousand at December 31, 2013.

The allowance for loan losses (ALL) is a valuation allowance for probable incurred credit losses, increased by the provision for loan losses, and decreased by charge-offs net of recoveries. A loan is charged-off against the allowance by management as a loss when deemed uncollectible, although collection efforts continue and future recoveries may occur. The determination of the amounts of the ALL and provisions for loan losses is based on management's current judgments about the credit quality of the loan portfolio with consideration given to all known relevant internal and external factors that affect loan collectability as of the reporting date. The appropriateness of the current period provision and the overall adequacy of the ALL are determined through a disciplined and consistently applied quarterly process that reviews the Bancorp's current credit risk within the loan portfolio and identifies the required allowance for loan losses given the current risk estimates.

Non-performing loans include those loans that are 90 days or more past due and those loans that have been placed on non-accrual status. Non-performing loans totaled \$5.2 million at June 30, 2014, compared to \$4.0 million at December 31, 2013, an increase of \$1.2 million or 30.00%. The increase in non-performing loans for the first six months of 2014 is primarily the result of the addition of one commercial real estate loan with a balance of \$1.1 million. The ratio of non-performing loans to total loans was 1.07% at June 30, 2014, compared to 0.90% at December 31, 2013. The ratio of non-performing loans to total assets was 0.67% at June 30, 2014, compared to 0.57% at December 31, 2013. At June 30, 2014, all non-performing loans are also accounted for on a non-accrual basis, except for four loans totaling \$592 thousand that were classified as accruing and more than 90 days past due.

Loans internally classified as substandard totaled \$10.3 million at June 30, 2014, compared to \$12.2 million at December 31, 2013 a decrease of \$1.9 million or 15.6%. The current level of substandard loans is concentrated in one accruing commercial real estate hotel loan in the amount of \$4.7 million, which is the largest loan in this group. Substandard loans include non-performing loans and potential problem loans, where information about possible credit issues or other conditions causes management to question the ability of such borrowers to comply with loan covenants or repayment terms. No loans were internally classified as doubtful or loss at June 30, 2014 or December 31, 2013. In addition to identifying and monitoring non-performing and other classified loans, management maintains a list of watch loans. Watch loans represent loans management is closely monitoring due to one or more factors that may cause the loan to become classified as substandard. Watch loans totaled \$12.4 million at June 30, 2014, compared to \$7.5 million at December 31, 2013, an increase of \$4.9 million or 65.3%. The increase in watch loans is related to the downgrades of residential and commercial real estate.

A loan is considered impaired when, based on current information and events, it is probable that a borrower will be unable to pay all amounts due according to the contractual terms of the loan agreement. At June 30, 2014, impaired loans totaled \$7.8 million, compared to \$9.9 million at December 31, 2013 a decrease of \$2.1 million or 21.2%. The decrease in impaired loans for the first six months of 2014 is primarily the result of the partial charge-off of one commercial real estate loan and the payoff of one development loan. The June 30, 2014, impaired loan balances consist of nine commercial real estate and commercial business loans totaling \$7.0 million that are secured by business assets and real estate, and are personally guaranteed by the owners of the businesses. In addition, twenty-two residential real estate and home equity line of credit loans totaling \$801 thousand, which are troubled debt restructurings or purchased credit impaired, have also been classified as impaired. At June 30, 2014, the ALL contained \$406 thousand of specific reserves for impaired loans, compared to \$1.7 million at December 31, 2013. There were no other loans considered to be impaired loans as of June 30, 2014. Typically, management does not individually classify smaller-balance homogeneous loans, such as residential mortgages or consumer loans, as impaired unless they are troubled debt restructurings.

Purchased loans acquired in a business combination are recorded at estimated fair value on their purchase date. Purchased loans with evidence of credit quality deterioration since origination are considered purchased credit impaired loans. Expected future cash flows at the purchase date in excess of the fair value of loans are recorded as interest income over the life of the loans if the timing and amount of the future cash flows is reasonably estimable ("accretible yield"). The difference between contractually required payments and the cash flows expected to be collected at acquisition is referred to as the non-accretible difference and represents probable losses in the portfolio. In determining the acquisition date fair value of purchased credit impaired loans, and in subsequent accounting, the Bancorp aggregates these purchased loans into pools of loans by common risk characteristics, such as credit risk rating and loan type. Subsequent to the purchase date, increases in cash flows over those expected at the purchase date are recognized as interest income prospectively. Subsequent decreases to the expected cash flows will generally result in a provision for loan losses. At June 30, 2014, purchased credit impaired loans with unpaid principal balances totaled \$1.8 million with a recorded investment of \$647,000.



At June 30, 2014, the Bancorp classified five loans totaling \$6.5 million as troubled debt restructurings, which involves modifying the terms of a loan to forego a portion of interest or principal or reducing the interest rate on the loan to a rate materially less than market rates, or materially extending the maturity date of a loan. The Bancorp's troubled debt restructurings include one commercial real estate hotel loan in the amount of \$4.7 million, for which significant deferrals of principal repayments were granted; one commercial real estate loan in the amount of \$1.1 million for which a significant deferral of principal and interest repayment was granted; one commercial real estate loan in the amount of \$530 thousand for which a significant deferral of principal and interest repayment was granted by the Bank as required by a bankruptcy plan; and two mortgage loans totaling \$168 thousand, for which maturity dates were materially extended. At June 30, 2014, \$5.3 million of the Bancorp's loans classified as troubled debt restructurings are accruing loans. The valuation basis for the Bancorp's troubled debt restructurings is based on the present value of cash flows; unless consistent cash flows are not present, then the fair value of the collateral securing the loan is the basis for valuation.

At June 30, 2014, management is of the opinion that there are no loans, except those discussed above, where known information about possible credit problems of borrowers causes management to have serious doubts as to the ability of such borrowers to comply with the present loan repayment terms and which will imminently result in such loans being classified as past due, non-accrual or a troubled debt restructure. Management does not presently anticipate that any of the non-performing loans or classified loans would materially impact future operations, liquidity or capital resources.

For the six months ended June 30, 2014, \$410 thousand in provisions to the ALL were required, compared to \$230 thousand for the six months ended June 30, 2013, an increase of \$180 thousand or 78.3%. Purchased loans from the First Federal acquisition did add provisions for the quarter, however, the ALL provision increase for the current six month period is primarily a result of increased originations and overall loan portfolio growth. For the six months ended June 30, 2014, charge-offs, net of recoveries, totaled \$1.4 million, compared to charge-offs, net of recoveries of \$887 thousand for the six months ended June 30, 2013. The net loan charge-offs for 2014 were comprised of \$1.4 million in commercial real estate loans, \$11 thousand in residential real estate loans, \$11 thousand in consumer loans, and recoveries of \$2 thousand in commercial business loans. The ALL provisions take into consideration management's current judgments about the credit quality of the loan portfolio, loan portfolio balances, changes in the portfolio mix and local economic conditions. In determining the provision for loan losses for the current period, management has given consideration to historically elevated risks associated with the local economy, changes in loan balances and mix, and asset quality.

The ALL to total loans was 1.26% at June 30, 2014, compared to 1.64% at December 31, 2013. The ALL to non-performing loans (coverage ratio) was 118.12% at June 30, 2014, compared to 181.82% at December 31, 2013. The decrease in both measures is the result of the acquisition of First Federal and the charge-off from one commercial real estate property, which carried a significant specific reserve. The June 30, 2014 balance in the ALL account of \$6.2 million is considered adequate by management after evaluation of the loan portfolio, past experience and current economic and market conditions. While management may periodically allocate portions of the allowance for specific problem loans, the whole allowance is available for any loan charge offs that occur. The allocation of the ALL reflects performance and growth trends within the various loan categories, as well as consideration of the facts and circumstances that affect the repayment of individual loans, and loans which have been pooled as of the evaluation date, with particular attention given to non-performing loans and loans which have been classified as substandard, doubtful or loss. Management has allocated reserves to both performing and non-performing loans based on current information available.

At June 30, 2014, foreclosed real estate totaled \$1.4 million, which was comprised of twenty-three properties, compared to \$1.1 million and nine properties at December 31, 2013. The primary cause of the increase of foreclosed real estate is related to the acquisition of First Federal and is limited to residential real estate properties. Net gains from foreclosed real estate totaled \$5 thousand for the six months ended June 30, 2014, and were the result of proceeds received from a foreclosed property sold. At the end of June 2014 all of the Bancorp's foreclosed real estate is located within its primary market area.

The primary objective of the Bancorp's investment portfolio is to provide for the liquidity needs of the Bancorp and to contribute to profitability by providing a stable flow of dependable earnings. Funds are generally invested in federal funds, interest bearing balances in financial institutions, U.S. government securities, federal agency obligations, obligations of state and local municipalities and corporate securities. The securities portfolio, all of which is designated as available-for-sale, totaled \$209.4 million at June 30, 2014, compared to \$194.3 million at December 31, 2013, an increase of \$15.1 million (7.8%). The increase in the securities portfolio is a result of continued market opportunities. At June 30, 2014, the securities portfolio represented 28.9% of interest-earning assets and 27.0% of total assets compared to 30.1% of interest-earning assets and 28.0% of total assets at December 31, 2013. The Bancorp's end-of-period investment portfolio and other short-term investments and stock balances were as follows:

(Dollars in thousands)	June 30, 2014 (unaudited)		December 31, 2013	
	Balance	% Securities	Balance	% Securities
U.S. government sponsored entities	\$ 12,313	5.9%	\$ 18,360	9.4%
Collateralized mortgage obligations and residential mortgage-backed securities	112,834	53.9%	100,315	51.6%
Municipal securities	81,788	39.1%	73,653	37.9%
Collateralized debt obligations	2,444	1.1%	1,968	1.1%
Total securities available-for-sale	<u>\$ 209,379</u>	<u>100.0%</u>	<u>\$ 194,296</u>	<u>100.0%</u>

(Dollars in thousands)	June 30, 2014 (unaudited)	December 31, 2013	YTD Change	
	Balance	Balance	\$	%
Interest bearing balances in financial institutions	\$ 17,628	\$ 9,256	\$ 8,372	90.4%
Fed funds sold	200	110	90	81.8%
Federal Home Loan Bank stock	4,392	3,086	1,306	42.3%

The increase in interest bearing balances in financial institutions is primarily the result of the Bancorp's deposit gathering efforts and the timing of investing those funds in earning assets. Federal Home Loan Bank stock increased as a result of additional use of the Federal Home Loan Bank's advances during the period ended June 30, 2014 as well as stock assumed by the Bancorp the acquisition of First Federal.

Deposits are a fundamental and cost-effective source of funds for lending and other investment purposes. The Bancorp offers a variety of products designed to attract and retain customers, with the primary focus on building and expanding relationships. The Bancorp's end-of-period deposit portfolio balances were as follows:

(Dollars in thousands)	June 30, 2014 (unaudited)	December 31, 2013	YTD Change	
	Balance	Balance	\$	%
Checking	\$ 211,670	\$ 196,729	\$ 14,941	7.6%
Savings	89,606	84,460	5,146	6.1%
Money market	150,154	136,088	14,066	10.3%
Certificates of deposit	188,200	155,616	32,584	20.9%
Total deposits	<u>\$ 639,630</u>	<u>\$ 572,893</u>	<u>\$ 66,737</u>	<u>11.6%</u>

The Bancorp's core deposits include checking, savings, and money market accounts. The overall increase in core deposits is a result of management's sales efforts along with current customer preferences for short-term, liquid investment alternatives.

The Bancorp's borrowed funds are primarily used to fund asset growth not supported by deposit generation. The Bancorp's end-of-period borrowing balances were as follows:

(Dollars in thousands)	June 30, 2014 (unaudited)	December 31, 2013	YTD Change	
	Balance	Balance	\$	%
Repurchase agreements	\$ 18,437	\$ 14,031	\$ 4,406	31.4%
Borrowed funds	38,964	30,898	8,066	26.1%
Total borrowed funds	<u>\$ 57,401</u>	<u>\$ 44,929</u>	<u>\$ 12,472</u>	<u>27.8%</u>

Repurchase agreements increased as a result of growth in the Bancorp's business sweep accounts. Borrowed funds increased as projected opportunities to grow lending relationships continue.

## Liquidity and Capital Resources

For the Bancorp, liquidity management refers to the ability to generate sufficient cash to fund current loan demand, meet deposit withdrawals, and pay dividends and operating expenses. Because profit and liquidity are often conflicting objectives, management attempts to maximize the Bank's net interest margin by making adequate, but not excessive, liquidity provisions. Furthermore, funds are managed so that future profits will not be significantly impacted as funding costs increase.

Changes in the liquidity position result from operating, investing and financing activities. Cash flows from operating activities are generally the cash effects of transactions and other events that enter into the determination of net income. The primary investing activities include loan originations, loan repayments, investments in interest bearing balances in financial institutions, and the purchase, sale, and maturity of investment securities. Financing activities focus almost entirely on the generation of customer deposits. In addition, the Bancorp utilizes borrowings (i.e., repurchase agreements, FHLB advances and federal funds purchased) as a source of funds.

During the six months ended June 30, 2014, cash and cash equivalents increased by \$9.8 million compared to a \$9.0 million increase for the six months ended June 30, 2013. The primary sources of cash and cash equivalents were increased deposits, proceeds from FHLB advances, and proceeds from maturities, pay downs, calls, and sales of available-for-sale securities. The primary uses of cash and cash equivalents were loan originations, the purchase of securities, repayment of FHLB advances, and the payment of common stock dividends. Cash used by operating activities totaled \$488 thousand for the six months ended June 30, 2014, compared to cash provided of \$2.8 million for the six month period ended June 30, 2013. The decrease in cash from operating activities was primarily a result of increased origination of loans held for sale. Cash outflows from investing activities totaled \$28.6 million for the current period, compared to cash outflows of \$2.3 million for the six months ended June 30, 2013. The increased cash outflows for the current six months were primarily related to increased loan originations, increased securities purchases, and fewer pay downs and maturities from securities. Net cash inflows from financing activities totaled \$39.0 million during the current period compared to net cash inflows of \$8.5 million for the six months ended June 30, 2013. The increase in net cash inflows from financing activities was a result of net deposit and borrowing inflows. On a cash basis, the Bancorp paid dividends on common stock of \$1.3 million for the six months ended June 30, 2014 and \$1.1 million for the six months ended June 30, 2013.

At June 30, 2014, outstanding commitments to fund loans totaled \$92.5 million. Approximately 48.3% of the commitments were at variable rates. Standby letters of credit, which are conditional commitments issued by the Bancorp to guarantee the performance of a customer to a third party, totaled \$8.6 million at June 30, 2014. Management believes that the Bancorp has sufficient cash flow and borrowing capacity to fund all outstanding commitments and letters of credit, while maintaining proper levels of liquidity.

Management strongly believes that maintaining a high level of capital enhances safety and soundness. During the six months ended June 30, 2014, stockholders' equity increased by \$6.0 million (8.9%). During the six months ended June 30, 2014, stockholders' equity was primarily increased by net income of \$3.8 million and change in the valuation of available-for-sale securities of \$3.5 million. Decreasing stockholders' equity was the declaration of \$1.3 million in cash dividends. On April 24, 2014 the Bancorp's Board of Directors authorized a stock repurchase program to repurchase up to 50,000 shares of the Bancorp's outstanding common stock, from time to time and subject to market conditions, on the open market or in privately negotiated transactions. This stock repurchase program replaced the previous stock repurchase program that was authorized on April 18, 2000. The new stock repurchase program does not expire and is only limited by the number of shares that can be purchased. The stock repurchase program will be reviewed annually by the Board of Directors. During the second quarter, 1,172 shares were repurchased as part of the new stock repurchase program at an average price per share of \$26.50.

The Bancorp is subject to risk-based capital guidelines adopted by the Board of Governors of the Federal Reserve System (the FRB), and the Bank is subject to risk-based capital guidelines adopted by the FDIC. As applied to the Bancorp and the Bank, the FRB and FDIC capital requirements are substantially the same. These regulations divide capital into two tiers. The first tier (Tier 1) includes common equity, certain non-cumulative perpetual preferred stock and minority interests in equity accounts of consolidated subsidiaries, less goodwill and certain other intangible assets. Supplementary (Tier 2) capital includes, among other things, cumulative perpetual and long-term limited-life preferred stock, mandatory convertible securities, certain hybrid capital instruments, term subordinated debt and the allowance for loan losses, subject to certain limitations, less required deductions. The Bancorp and the Bank are required to maintain a total risk-based capital ratio of 8%, of which 4% must be Tier 1 capital. In addition, the FRB and FDIC regulations provide for a minimum Tier 1 leverage ratio (Tier 1 capital to adjusted average assets) of 3% for financial institutions that meet certain specified criteria, including that they have the highest regulatory rating and are not experiencing or anticipating significant growth. All other financial institutions are required to maintain a Tier 1 leverage ratio of 3% plus an additional cushion of at least one to two percent. See "Recent Developments - Regulatory Capital Rules" for a description of the new capital ratios that will be phased-in beginning in 2015.

The following table shows that, at June 30, 2014, and December 31, 2013, the Bancorp's and Bank's capital exceeded all regulatory capital requirements. During the six months ended June 30, 2014, the Bancorp's and Bank's regulatory capital ratios continued to be negatively impacted by regulatory requirements regarding collateralized debt obligations. The decrease in capital ratios during the six months is the result of the acquisition of First Federal as well as asset growth from loan originations and continued investments in the securities portfolio. The regulatory requirements state that for collateralized debt obligations that have been downgraded below investment grade by the rating agencies, increased risk based asset weightings are required. The Bancorp currently holds four pooled trust preferred securities with a cost basis of \$5.2 million. These investments currently have ratings that are below investment grade. As a result, approximately \$26.5 million of risk based assets are generated by the trust preferred securities in the Bancorp's and Bank's total risk based capital calculation. The Bancorp's and the Bank's regulatory capital ratios were substantially the same at both June 30, 2014 and December 31, 2013. The dollar amounts are in millions.

(Dollars in millions)

At June 30, 2014	Actual		Minimum Required For Capital Adequacy Purposes		Minimum Required To Be Well Capitalized Under Prompt Corrective Action Regulations	
	Amount	Ratio	Amount	Ratio	Amount	Ratio
Total capital to risk-weighted assets	\$ 75.9	14.3%	\$ 42.6	8.0%	\$ 53.2	10.0%
Tier 1 capital to risk-weighted assets	\$ 69.7	13.1%	\$ 21.3	4.0%	\$ 31.9	6.0%
Tier 1 capital to adjusted average assets	\$ 69.7	9.1%	\$ 23.0	3.0%	\$ 38.3	5.0%

(Dollars in millions)

At December 31, 2013	Actual		Minimum Required For Capital Adequacy Purposes		Minimum Required To Be Well Capitalized Under Prompt Corrective Action Regulations	
	Amount	Ratio	Amount	Ratio	Amount	Ratio
Total capital to risk-weighted assets	\$ 75.0	15.6%	\$ 38.5	8.0%	\$ 48.2	10.0%
Tier 1 capital to risk-weighted assets	\$ 69.0	14.3%	\$ 19.3	4.0%	\$ 28.9	6.0%
Tier 1 capital to adjusted average assets	\$ 69.0	10.0%	\$ 20.8	3.0%	\$ 34.6	5.0%

The Bancorp's ability to pay dividends to its shareholders is entirely dependent upon the Bank's ability to pay dividends to the Bancorp. Under Indiana law, the Bank may pay dividends from its undivided profits (generally, earnings less losses, bad debts, taxes and other operating expenses) as is considered expedient by the Bank's Board of Directors. However, the Bank must obtain the approval of the Indiana Department of Financial Institutions (DFI) if the total of all dividends declared by the Bank during the current year, including the proposed dividend, would exceed the sum of retained net income for the year to date plus its retained net income for the previous two years. For this purpose, "retained net income," means net income as calculated for call report purposes, less all dividends declared for the applicable period. An exemption from DFI approval would require that the Bank have been assigned a composite uniform financial institutions rating of 1 or 2 as a result of the most recent federal or state examination; the proposed dividend would not result in a Tier 1 leverage ratio below 7.5%; and that the Bank not be subject to any corrective action, supervisory order, supervisory agreement, or board approved operating agreement. The aggregate amount of dividends that may be declared by the Bank in 2014, without the need for qualifying for an exemption or prior DFI approval, is \$9.4 million plus 2014 net profits. Moreover, the FDIC and the Federal Reserve Board may prohibit the payment of dividends if it determines that the payment of dividends would constitute an unsafe or unsound practice in light of the financial condition of the Bank. On June 27, 2014 the Board of Directors of the Bancorp declared a second quarter dividend of \$0.25 per share. The Bancorp's second quarter dividend was paid to shareholders on July 3, 2014.

#### Results of Operations - Comparison of the Quarter Ended June 30, 2014 to the Quarter Ended June 30, 2013

For the quarter ended June 30, 2014, the Bancorp reported net income of \$1.9 million, compared to net income of \$1.7 million for the quarter ended June 30, 2013, an increase of \$242 thousand (14.2%). For the current quarter the ROA was 1.02%, compared to 0.99% for the quarter ended June 30, 2013. The ROE was 10.77% for the quarter ended June 30, 2014, compared to 9.65% for the quarter ended June 30, 2013.

Net interest income for the three months ended June 30, 2014 was \$6.5 million, an increase of \$692 thousand (12.0%), compared to \$5.8 million for the quarter ended June 30, 2013. The weighted-average yield on interest-earning assets was 3.88% for the three months ended June 30, 2014, compared to 3.84% for the three months ended June 30, 2013. The weighted-average cost of funds for the quarter ended June 30, 2014, was 0.26%, compared to 0.29% for the quarter ended June 30, 2013. The impact of the 3.88% return on interest earning assets and the 0.26% cost of funds resulted in an interest rate spread of 3.62% for the current quarter, compared to 3.55% for the quarter ended June 30, 2013. Compared to the three months ended June 30, 2013, total interest income increased by \$709 thousand (11.4%) while total interest expense increased by \$17 thousand (3.9%). The net interest margin was 3.62% for the three months ended June 30, 2014, compared to 3.57% for the quarter ended June 30, 2013. On a tax equivalent basis, the Bancorp's net interest margin was 3.89% for the three months ended June 30, 2014, compared to 3.76% for the quarter ended June 30, 2013. Comparing the net interest margin on a tax equivalent basis more accurately compares the returns on tax-exempt loans and securities to those on taxable interest-earning assets.

During the three months ended June 30, 2014, interest income from loans increased by \$457 thousand (9.2%), compared to the three months ended June 30, 2013. The increase was due to higher average balances outstanding. The weighted-average yield on loans outstanding was 4.41% for the current quarter, compared to 4.48% for the three months ended June 30, 2013. Loan balances averaged \$490.6 million for the current quarter, an increase of \$48.5 million (11.0%) from \$442.1 million for the three months ended June 30, 2013. During the three months ended June 30, 2014, interest income on securities and other interest bearing balances increased by \$252 thousand (20.1%), compared to the quarter ended June 30, 2013. The change was due to an increase in the weighted-average yield on securities balances as well as higher average balances outstanding. The weighted-average yield on securities and other interest bearing balances was 2.83%, for the current quarter, compared to 2.60% for the three months ended June 30, 2013. Securities balances averaged \$212.3 million for the current quarter, up \$20.9 million (10.9%) from \$191.4 million for the three months ended June 30, 2013. Other interest bearing balances averaged \$11.0 million for the current period, down \$2.4 million (17.9%) from \$13.4 million for the three months ended June 30, 2013. The decrease in other interest bearing balances is a result of increased loan origination and investments in securities.

Interest expense on deposits increased by \$24 thousand (8.5%) during the current quarter compared to the three months ended June 30, 2013. The change was due to an increase in average balances outstanding. The weighted-average rate paid on deposits for both the three months ended June 30, 2014 and 2013 was 0.20%. Total deposit balances averaged \$628.3 million for the current quarter, an increase of \$72.1 million (13.0%) from \$556.2 million for the quarter ended June 30, 2013. Interest expense on borrowed funds decreased by \$7 thousand (4.5%) during the current quarter due to a decrease in the weighted-average cost of funds compared to the three months ended June 30, 2013. The weighted-average cost of borrowed funds was 1.01% for the current quarter, compared to 1.14% for the three months ended June 30, 2013. Borrowed funds averaged \$57.8 million during the quarter ended June 30, 2014, an increase of \$4.2 million (7.8%) from \$53.6 million for the quarter ended June 30, 2013.

Noninterest income for the quarter ended June 30, 2014 was \$1.6 million, an increase of \$76 thousand (5.1%) from \$1.5 million for the quarter ended June 30, 2013. During the current quarter, fees and service charges totaled \$703 thousand, an increase of \$78 thousand (12.5%) from \$625 thousand for the quarter ended June 30, 2013. The increase in fees and service charges is the result of the Bancorp's growing depository base. Fees from Wealth Management operations totaled \$441 thousand for the quarter ended June 30, 2014, an increase of \$111 thousand (33.6%) from \$330 thousand for the quarter ended June 30, 2013. The increase in Wealth Management income is related to growth in assets under management and market value changes. Gains from the sale of securities totaled \$107 thousand for the current quarter, a decrease of \$209 thousand (66.1%) from \$316 thousand for the quarter ended June 30, 2013. Current market conditions continued to provide opportunities to maintain securities cash flows, while recognizing gains from the sales of securities. Income from an increase in the cash value of bank owned life insurance totaled \$103 thousand for the quarter ended June 30, 2014, an increase of \$15 thousand (17.0%) from \$88 thousand for the quarter ended June 30, 2013. The increase in income from the cash value of bank owned life insurance is the result of added policies taken during 2013. Gains from loan sales totaled \$141 thousand for the current quarter, an increase of \$2 thousand (1.4%), compared to \$139 thousand for the quarter ended June 30, 2013. The increase in gains from the sale of loans is a result of increased mortgage loan origination efforts, including increased originations generated by additional mortgage loan officers. Loss on foreclosed real estate totaled \$7 thousand for the quarter ended June 30, 2014, a decrease of \$11 thousand (61.1%) from losses of \$18 thousand for the quarter ended June 30, 2013. Other noninterest income totaled \$72 thousand for the quarter, an increase of \$68 thousand (1700.0%) compared to \$4 thousand for the quarter ended June 30, 2013. The increase in other non-interest income is primarily related to rent from foreclosed real estate properties and income from other one-time items.

Noninterest expense for the quarter ended June 30, 2014 was \$5.3 million, an increase of \$477 thousand (9.9%) from \$4.8 million for the three months ended June 30, 2013. During the current quarter, compensation and benefits totaled \$2.8 million, an increase of \$165 thousand (6.3%) from \$2.6 million for the quarter ended June 30, 2013. The increase in compensation and benefits is the result of the Bancorp's ordinary course annual adjustments to salaries as well as adding sales staff. Occupancy and equipment totaled \$821 thousand for the current quarter, an increase of \$80 thousand (10.8%), compared to \$741 thousand for the quarter ended June 30, 2013. The increase in occupancy and equipment expense is the result of slightly higher building operating expenses as well as the addition of two new banking centers during the current quarter from the acquisition of First Federal. Data processing expense totaled \$284 thousand for the three months ended June 30, 2014, an increase of \$52 thousand (22.4%) from \$232 thousand for the three months ended June 30, 2013. Data processing expense has increased as a result of increased system utilization. Marketing expense related to banking products totaled \$142 thousand for the current quarter, a decrease of \$17 thousand (10.7%) from \$159 thousand for the three months ended June 30, 2013. The Bancorp proactively markets its products, but varies its timing based on projected benefits and needs. Federal deposit insurance premium expense totaled \$127 thousand for the three months ended June 30, 2014, a decrease of \$4 thousand (3.1%) from \$131 thousand for the quarter ended June 30, 2013. The decrease was the result of lower FDIC assessment rates. Other expenses related to banking operations totaled \$1.1 million for the quarter ended June 30, 2014, an increase of \$201 thousand (21.5%) from \$937 thousand for the quarter ended June 30, 2013. The increase in other operating expenses is primarily related to the acquisition of First Federal. The Bancorp's efficiency ratio was 66.1% for the quarter ended June 30, 2014, compared to 66.6% for the three months ended June 30, 2013. The ratio is determined by dividing total noninterest expense by the sum of net interest income and total noninterest income for the period and the decrease can be attributed to higher net interest income and noninterest income.

Income tax expenses for the three months ended June 30, 2014 totaled \$603 thousand, compared to income tax expense of \$624 thousand for the three months ended June 30, 2013, a decrease of \$21 thousand (3.4%). The combined effective federal and state tax rates for the Bancorp was 23.6% for the three months ended June 30, 2014, compared to 26.8% for the three months ended June 30, 2013. The Bancorp's lower current quarter effective tax rate is a result of higher tax preferred income.

#### **Results of Operations - Comparison of the Six Months Ended June 30, 2014 to the Six Months Ended June 30, 2013**

For the six months ended June 30, 2014, the Bancorp reported net income of \$3.8 million, compared to net income of \$3.4 million for the six months ended June 30, 2013, an increase of \$376 thousand (11.1%). For the current six months the ROA was 1.02%, compared to 0.98% for the six months ended June 30, 2013. The ROE was 10.59% for the six months ended June 30, 2014, compared to 9.58% for the six months ended June 30, 2013.

Net interest income for the six months ended June 30, 2014 was \$12.3 million, an increase of \$763 thousand (6.6%), compared to \$11.6 million for the six months ended June 30, 2013. The weighted-average yield on interest-earning assets was 3.83% for the six months ended June 30, 2014, compared to 3.85% for the six months ended June 30, 2013. The weighted-average cost of funds for the six months ended June 30, 2014, was 0.26%, compared to 0.29% for the six months ended June 30, 2013. The impact of the 3.83% return on interest earning assets and the 0.26% cost of funds resulted in an interest rate spread of 3.57% for the current six months, compared to 3.56% for the six months ended June 30, 2013. Compared to the six months ended June 30, 2013, total interest income increased by \$734 thousand (5.9%) while total interest expense decreased by \$29 thousand (3.2%). The net interest margin was 3.58% for the six months ended June 30, 2014, compared to 3.57% for the six months ended June 30, 2013. On a tax equivalent basis, the Bancorp's net interest margin was 3.85% for the six months ended June 30, 2014, compared to 3.77% for the six months ended June 30, 2013. Comparing the net interest margin on a tax equivalent basis more accurately compares the returns on tax-exempt loans and securities to those on taxable interest-earning assets.

During the six months ended June 30, 2014, interest income from loans increased by \$346 thousand (3.5%), compared to the six months ended June 30, 2013. The change was primarily due to an increase in average balances outstanding. The weighted-average yield on loans outstanding was 4.38% for the current six months, compared to 4.49% for the six months ended June 30, 2013. Loan balances averaged \$470.8 million for the current six months, an increase of \$27.6 million (6.2%) from \$443.2 million for the six months ended June 30, 2013. During the six months ended June 30, 2014, interest income on securities and other interest bearing balances increased by \$388 thousand (15.5%), compared to the six months ended June 30, 2013. The increase was due to an increase in the weighted-average yield and balances outstanding. The weighted-average yield on securities and other interest bearing balances was 2.65%, for the current six months, compared to 2.46% for the six months ended June 30, 2013. Securities balances averaged \$201.4 million for the current six months, up \$10.0 million (5.2%) from \$191.4 million for the six months ended June 30, 2013. The increase in security average balances is a result of ongoing, consistent investment growth. Other interest bearing balances averaged \$17.2 million for the current period, down \$4.3 million (33.3%) from \$12.9 million for the six months ended June 30, 2013.

Interest expense on deposits decreased by \$4 thousand (0.7%) during the current six months compared to the six months ended June 30, 2013. The change was primarily due to a decrease in the weighted-average rate paid on deposits. The weighted-average rate paid on deposits for the six months ended June 30, 2014 was 0.19%, compared to 0.21%, for the six months ended June 30, 2013. Total deposit balances averaged \$603.1 million for the current six months, up \$44.7 million (8.0%) from \$558.4 million for the six months ended June 30, 2013. Interest expense on borrowed funds decreased by \$25 thousand (8.0%) during the current six months due to lower weighted average cost, as compared to the six months ended June 30, 2013. The weighted-average cost of borrowed funds was 1.00% for the current six months, compared to 1.20% for the six months ended June 30, 2013. Borrowed funds averaged \$57.6 million during the six months ended June 30, 2014, a decrease of \$5.5 million (10.6%) from \$52.1 million for the six months ended June 30, 2013.

Noninterest income for the six months ended June 30, 2014 was \$3.1 million, an increase of \$240 thousand (8.4%) from \$2.8 million for the six months ended June 30, 2013. During the current six months, fees and service charges totaled \$1.3 million, an increase of \$81 thousand (6.7%) from \$1.2 million for the six months ended June 30, 2013. The increase in fees and service charges is the result of the Bancorp's growing depository base. Fees from Wealth Management operations totaled \$819 thousand for the six months ended June 30, 2014, an increase of \$122 thousand (17.5%) from \$697 thousand for the six months ended June 30, 2013. The increase in Wealth Management income is related to growth in assets under management and market value changes. Gains from the sale of securities totaled \$457 thousand for the current six months, a decrease of \$13 thousand (2.9%) from \$444 thousand for the six months ended June 30, 2013. Current market conditions provided opportunities to manage securities cash flows, while recognizing gains from the sales of securities. Gains from loan sales totaled \$216 thousand for the current six months, a decrease of \$82 thousand (27.5%), compared to \$298 thousand for the six months ended June 30, 2013. The decrease in gains from the sale of loans is the result of less mortgage refinance activity. Income from an increase in the cash value of bank owned life insurance totaled \$205 thousand for the six months ended June 30, 2014, an increase of \$30 thousand (17.1%), compared to \$175 thousand for the six months ended June 30, 2013. The increase in income from the cash value of bank owned life insurance is the result of added policies taken during 2013. Gains on foreclosed real estate totaled \$5 thousand for the six months ended June 30, 2014, an increase of \$6 thousand (600.0%) from \$1 thousand in losses for the six months ended June 30, 2013. Other noninterest income totaled \$88 thousand for the six months ended June 30, 2014, compared to \$18 thousand for the six months ended June 30, 2013. The increase in other non-interest income is primarily related to rent from foreclosed real estate properties and income from other one-time items.

Noninterest expense for the six months ended June 30, 2014 was \$10.1 million, an increase of \$511 thousand (5.3%) from \$9.6 million for the six months ended June 30, 2013. During the current six months, compensation and benefits totaled \$5.4 million, an increase of \$169 thousand (3.2%) from \$5.3 million for the six months ended June 30, 2013. The increase in compensation and benefits is the result of the Bancorp's ordinary course annual adjustments to salaries as well as adding sales staff. Occupancy and equipment totaled \$1.6 million for the current six months, an increase of \$88 thousand (5.8%), compared to \$1.5 million for the six months ended June 30, 2013. The increase in occupancy and equipment expense is the result of slightly higher building operating expenses as well as the addition of two new banking centers during the current six months from the acquisition of First Federal. Data processing expense totaled \$560 thousand for the six months ended June 30, 2014, an increase of \$88 thousand (18.6%) from \$472 thousand for the six months ended June 30, 2013. Data processing expense has increased as a result of increased system utilization. Marketing expense related to banking products totaled \$260 thousand for the current six months, a decrease of \$7 thousand (2.6%) from \$267 thousand for the six months ended June 30, 2013. The Bancorp continues to proactively market its products, but varies its timing based on projected benefits and needs. Federal deposit insurance premium expense totaled \$218 thousand for the six months ended June 30, 2014, a decrease of \$35 thousand (13.8%) from \$253 thousand for the six months ended June 30, 2013. The decrease was the result of lower FDIC assessment rates. Other expenses related to banking operations totaled \$2.0 million for the six months ended June 30, 2014, an increase of \$208 thousand (11.3%) from \$1.8 million for the six months ended June 30, 2013. The increase in other operating expenses is primarily related to the acquisition of First Federal. The Bancorp's efficiency ratio was 65.7% for the six months ended June 30, 2014, compared to 66.7% for the six months ended June 30, 2013. The ratio is determined by dividing total noninterest expense by the sum of net interest income and total noninterest income for the period and the decrease can be attributed to higher net interest income and noninterest income.

Income tax expenses for the six months ended June 30, 2014 totaled \$1.1 million, compared to income tax expense of \$1.2 million for the six months ended June 30, 2013, a decrease of \$64 thousand (5.4%). The combined effective federal and state tax rates for the Bancorp was 23.0% for the six months ended June 30, 2014, compared to 26.0% for the six months ended June 30, 2013. The Bancorp's lower current period effective tax rate is a result of higher tax preferred income.

#### **Critical Accounting Policies**

Critical accounting policies are those accounting policies that management believes are most important to the portrayal of the Bancorp's financial condition and that require management's most difficult, subjective or complex judgments. The Bancorp's critical accounting policies from December 31, 2013 remain unchanged.

#### **Forward-Looking Statements**

Statements contained in this report that are not historical facts are forward-looking statements within the meaning of the Private Securities Litigation Reform Act of 1995. The words or phrases "would be," "will allow," "intends to," "will likely result," "are expected to," "will continue," "is anticipated," "estimate," "project," or similar expressions are also intended to identify "forward-looking statements" within the meaning of the Private Securities Litigation Reform Act. The Bancorp cautions readers that forward-looking statements, including without limitation those relating to the Bancorp's future business prospects, interest income and expense, net income, liquidity, and capital needs are subject to certain risks and uncertainties that could cause actual results to differ materially from those indicated in the forward-looking statements, due to, among other things, factors identified in this report, including those identified in the Bancorp's 2013 Form 10-K.

**Item 3. Quantitative and Qualitative Disclosures About Market Risk**

Not Applicable.

**Item 4. Controls and Procedures**

(a) Evaluation of Disclosure Controls and Procedures.

The Bancorp maintains disclosure controls and procedures (as defined in Sections 13a – 15(e) and 15d – 15(e)) of regulations promulgated under the Securities Exchange Act of 1934 (the "Exchange Act") that are designed to ensure that information required to be disclosed by the Bancorp in the reports that it files or submits under the "Exchange Act" is recorded, processed, summarized and reported within the time periods specified in the SEC's rules and forms. These disclosure controls and procedures include controls and procedures designed to ensure that information required to be disclosed by the Bancorp in the reports that it files or submits under the Exchange Act is accumulated and communicated to the Bancorp's management, including its principal executive officer and principal financial officer, as appropriate to allow timely decisions regarding required disclosure. The Bancorp's chief executive officer and chief financial officer evaluate the effectiveness of the Bancorp's disclosure controls and procedures as of the end of each quarter. Based on that evaluation as of June 30, 2014, the Bancorp's chief executive officer and chief financial officer have concluded that such disclosure controls and procedures were effective as of that date in ensuring that information required to be disclosed by the Bancorp under the Exchange Act is recorded, processed, summarized and reported within the time periods specified in the SEC's rules and forms.

(b) Changes in Internal Control Over Financial Reporting.

There was no change in the Bancorp's internal control over financial reporting identified in connection with the Bancorp's evaluation of controls that occurred during the six months ended June 30, 2014 that has materially affected, or is reasonably likely to materially affect, the Bancorp's internal control over financial reporting.



## PART II - Other Information

### Item 1. Legal Proceedings

There are no matters reportable under this item.

### Item 1A. Risk Factors

Not Applicable.

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

On April 18, 2000 the Bancorp's Board of Directors authorized a stock repurchase program to repurchase up to 50,000 shares of the Bancorp's outstanding common stock, from time to time and subject to market conditions, on the open market or in privately negotiated transactions. This stock repurchase program did not have an express expiration date and was only limited by the number of shares that could be purchased. This repurchase program was replaced by a new stock repurchase program authorized by the Bancorp's Board of Directors on April 24, 2014, as described below. As a result, the Bancorp will not make any further repurchases under the April 2000 repurchase program. As of June 30, 2014, the Bancorp repurchased 43,812 shares of its outstanding common stock under the program at an average price per share of \$22.64. No shares were repurchased during three months ended June 30, 2014 as shown in the following table:

Period	Total Number of Shares Purchased	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 Program(1)
April 1, 2014 – April 30, 2014	-	N/A	43,812	6,188
May 1, 2014 – May 31, 2014	-	N/A	43,812	6,188
June 1, 2014 – June 30, 2014	-	N/A	43,812	6,188
	-	N/A	43,812	0

- (1) The stock repurchase plan was announced on April 18, 2000, whereby the Bancorp was authorized to repurchase up to 50,000 shares of the Bancorp's common stock outstanding. This plan was replaced by the new plan on April 24, 2014.

On April 24, 2014 the Bancorp's Board of Directors authorized a new stock repurchase program to repurchase up to 50,000 shares of the Bancorp's outstanding common stock, from time to time and subject to market conditions, on the open market or in privately negotiated transactions. This stock repurchase replaced the previous stock repurchase program that was authorized on April 18, 2000. The new stock repurchase program does not expire and is only limited by the number of shares that can be purchased. The stock repurchase program will be reviewed annually by the Board of Directors. During the quarter ended June 30, 2014, 1,172 shares were repurchased as part of the newly authorized stock repurchase program. As of June 30, 2014, the Bancorp has repurchased 1,172 shares of its outstanding common stock under the program at an average price per share of \$26.50. Information on the shares repurchased during the quarter ended June 30, 2014 under the program is as follows:

Period	Total Number of Shares Purchased	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 Program(2)
April 1, 2014 – April 30, 2014	1,160	\$ 26.50	1,160	48,840
May 1, 2014 – May 31, 2014	12	\$ 26.46	1,172	48,828
June 1, 2014 – June 30, 2014	-	N/A	-	48,828
	1,172	\$ 26.50	1,172	48,828

- (2) The stock repurchase program was announced on April 24, 2014, whereby the Bancorp is authorized to repurchase up to 50,000 shares of the Bancorp's common stock outstanding. There is no express expiration date for this program. This program replaced the previous stock repurchase program authorized on April 18, 2000.

### Item 3. Defaults Upon Senior Securities

There are no matters reportable under this item.

### Item 4. Mine Safety Disclosures

Not Applicable.

### Item 5. Other Information

There are no matters reportable under this item.

Item 6. Exhibits

Exhibit Number	Description
31.1	Rule 13a-14(a)/15d-14(a) Certification of Chief Executive Officer
31.2	Rule 13a-14(a)/15d-14(a) Certification of Chief Financial Officer
32.1	Section 1350 Certifications
101	The following materials from the Bancorp's Form 10-Q for the quarterly period ended June 30, 2014, formatted in an XBRL Interactive Data File: (i) Consolidated Balance Sheets; (ii) Consolidated Statements of Income; (iii) Consolidated Statements of Changes in Stockholders' Equity; (iv) Consolidated Statements of Cash Flows; and (v) Notes to Consolidated Financial Statements, with detailed tagging of notes and financial statement schedules.

**SIGNATURES**

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

**NORTHWEST INDIANA BANCORP**

Date: August 4, 2014

/s/ David A. Bochnowski  
David A. Bochnowski  
Chairman of the Board, Chief Executive  
Officer and President

Date: August 4, 2014

/s/ Robert T. Lowry  
Robert T. Lowry  
Executive Vice President, Chief Financial  
Officer and Treasurer

CERTIFICATION PURSUANT TO  
RULE 13a-14(a)/15d-14(a) OF THE SECURITIES EXCHANGE ACT OF 1934,  
AS ADOPTED PURSUANT TO SECTION 302 OF THE SARBANES-OXLEY ACT OF 2002

I, David A. Bochnowski, certify that:

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

Date: August 4, 2014

/s/ David A. Bochnowski

David A. Bochnowski  
Chairman of the Board, Chief Executive  
Officer and President

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CERTIFICATION PURSUANT TO  
RULE 13a-14(a)/15d-14(a) OF THE SECURITIES EXCHANGE ACT OF 1934,  
AS ADOPTED PURSUANT TO SECTION 302 OF THE SARBANES-OXLEY ACT OF 2002

I, Robert T. Lowry, certify that:

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

Date: August 4, 2014

/s/ Robert T. Lowry  
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Robert T. Lowry  
Executive Vice President, Chief Financial  
Officer and Treasurer

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CERTIFICATIONS PURSUANT TO  
18 U.S.C. SECTION 1350,  
AS ADOPTED PURSUANT TO  
SECTION 906 OF THE SARBANES-OXLEY ACT OF 2002

In connection with the Quarterly Report on Form 10-Q of NorthWest Indiana Bancorp (the "Company") for the quarterly period ended June 30, 2014, as filed with the Securities and Exchange Commission (the "Report"), each of David A. Bochnowski, Chairman of the Board, Chief Executive Officer, and President of the Company, and Robert T. Lowry, Executive Vice President, Chief Financial Officer and Treasurer of the Company, hereby certifies, pursuant to 18 U.S.C. § 1350, as adopted pursuant to § 906 of the Sarbanes-Oxley Act of 2002, that:

- (1) The Report fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934; and
- (2) The information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Company.

Dated: August 4, 2014

/s/ David A. Bochnowski

David A. Bochnowski  
Chairman of the Board, Chief Executive  
Officer and President

/s/ Robert T. Lowry

Robert T. Lowry  
Executive Vice President, Chief Financial  
Officer and Treasurer

A signed original of this written statement required by Section 906, or other document authenticating, acknowledging, or otherwise adopting the signature that appears in typed form within the electronic version of this written statement required by Section 906, has been provided to NorthWest Indiana Bancorp and will be retained by NorthWest Indiana Bancorp and furnished to the Securities and Exchange Commission or its staff upon request.

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