Risk Factors Comparison 2024-02-20 to 2023-02-16 Form: 10-K

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An investment in our common stock is subject to risks inherent to our business. The material risks and uncertainties that we believe affect us are described below. See “ Forward Looking Statements ” under Item 7 of this report for a discussion of other important factors that can affect our business. Credit Risks We are subject to credit risks relating to our loan and lease portfolios — ~~We have certain lending policies and procedures in place that are designed to optimize loan and lease income within an acceptable level of risk. Our management reviews and approves these policies and procedures on a regular basis. A reporting system supplements the review process by providing our management with frequent reports related to loan and lease production, loan quality, concentrations of credit, loan and lease delinquencies, and nonperforming and potential problem loans and leases. Diversification in the loan and lease portfolios is a means of managing risk associated with fluctuations in economic conditions. We maintain an independent loan review department that reviews and validates the credit risk program on a periodic basis. Results of these reviews are presented to our management. The loan and lease review process complements and reinforces the risk identification and assessment decisions made by lenders and credit personnel, as well as our policies and procedures.~~ Commercial and commercial real estate loans generally involve higher credit risks than residential real estate and consumer loans. Because payments on loans secured by commercial real estate or equipment are often dependent upon the successful operation and management of the underlying assets, repayment of such loans may be influenced to a great extent by conditions in the market or the economy. We seek to ~~minimize~~ **mitigate** these risks through our underwriting standards ~~. We obtain financial information and perform credit risk analysis on our customers. Credit criteria may include, but are not limited to, assessments of income, cash flows, collateral, and net worth; asset ownership; bank and trade credit references; credit bureau reports; and operational history. Commercial real estate or equipment loans are underwritten after evaluating and understanding the borrower’ s ability to operate profitably and generate positive cash flows. Our management examines current and projected cash flows of the borrower to determine the ability of the borrower to repay their obligations as agreed. Underwriting standards are designed to promote relationship banking rather than transactional banking~~ . Most commercial and industrial loans are secured by the assets being financed or other business assets; however, some loans may be made on an unsecured basis ~~. Our credit policy sets different maximum exposure limits both by business sector and our current and historical relationship and previous experience with each customer~~ . We offer both fixed- rate and adjustable- rate consumer mortgage loans secured by properties, substantially all of which are located in our primary market area. Adjustable- rate mortgage loans help reduce our exposure to changes in interest rates; however, during periods of rising interest rates, the risk of default on adjustable- rate mortgage loans may increase as a result of repricing and the increased payments required from the borrower. Additionally, some residential mortgages are sold into the secondary market and serviced by our principal banking subsidiary, 1st Source Bank. Consumer loans are primarily all other non- real estate loans to individuals in our regional market area. Consumer loans can entail risk, particularly in the case of loans that are unsecured or secured by rapidly depreciating assets. In these cases, any repossessed collateral may not provide an adequate source of repayment of the outstanding loan balance. The remaining deficiency often does not warrant further substantial collection efforts against the borrower beyond obtaining a deficiency judgment. In addition, consumer loan collections are dependent on the borrower’ s continuing financial stability, and thus are more likely to be adversely affected by job loss, divorce, illness, or personal bankruptcy. The 1st Source Specialty Finance Group loan and lease portfolio consists of commercial loans and leases secured by construction and transportation equipment, including aircraft, autos, trucks, and vans. ~~Finance receivables for this Group generally provide for monthly payments and may include prepayment penalty provisions.~~ Our construction and transportation related businesses could be adversely affected by slowdowns in the economy. Clients who rely on the use of assets financed through the Specialty Finance Group to produce income could be negatively affected, and we could experience substantial loan and lease losses. By the nature of the businesses these clients operate in, we could be adversely affected by rapid increases or decreases in fuel costs, terrorist and other potential attacks, and other destabilizing events. These factors could contribute to the deterioration of the quality of our loan and lease portfolio, as they could have a negative impact on the travel and transportation sensitive businesses for which our ~~specialty~~ **Specialty** ~~finance~~ **Finance** ~~businesses~~ **Group** ~~provide~~ **provides** financing. Our aircraft portfolio has foreign exposure, particularly in Mexico and Brazil ~~. We establish exposure limits for each country through a centralized oversight process, and in consideration of relevant economic, political, social and legal risks. We monitor exposures closely and adjust our country limits in response to changing conditions~~ . Currency fluctuations could have a negative impact on our client’ s cost of paying dollar denominated debts and, as a result, we could experience higher delinquency in this portfolio. Also, since some of the relationships in this portfolio are large, a slowdown in these markets could have a significant adverse impact on our performance. In addition, our leasing and equipment financing activity is subject to the risk of cyclical downturns, industry concentration and clumping, and other adverse economic developments affecting these industries and markets. This area of lending, with transportation in particular, is dependent upon general economic conditions and the strength of the travel, construction, and transportation industries. Our allowance for credit losses may prove to be insufficient to absorb losses in our loan and lease portfolio — ~~In the financial services industry, there~~ **There** is always a risk that ~~certain~~ borrowers may not repay borrowings. The determination of the appropriate level of the allowance for credit losses inherently involves a high degree of subjectivity and requires us to make significant estimates of current credit risks and future trends, all of which may undergo material changes. Our allowance for credit losses may not be sufficient to cover the loan and lease losses that we may actually incur. If we experience defaults by borrowers in any of our businesses, our earnings could be negatively affected. Changes in local economic conditions could adversely affect credit quality, particularly in our local business loan and lease portfolio. Changes in national or international economic conditions could also adversely affect the quality of our loan and lease portfolio and negate, to some extent, the benefits of national or international diversification through our Specialty Finance Group' s portfolio. In addition, bank regulatory agencies periodically review our allowance for credit losses and may require an increase in the provision for credit losses or the recognition of further loan or lease charge- offs based upon their judgments, which may be different from ours. The soundness of other financial institutions could adversely affect us — Financial services institutions are interrelated as a result of trading, clearing, counterparty, or other relationships. We have exposure to many different industries and counterparties, and we routinely execute transactions with counterparties in the financial services industry, including commercial banks, brokers and dealers, investment banks, and other institutional clients. Many of these transactions expose us to credit risk in the event of a default by our counterparty or client. In addition, our credit risk may be exacerbated when the collateral held by us cannot be realized or is liquidated at prices not sufficient to recover the full amount of the credit or derivative exposure due us. Any such losses could have a material adverse effect on our financial condition and results of operations. We may be adversely affected by climate change and related legislative and regulatory initiatives — ~~Political and social attention to the issue of climate change has increased.~~ Federal and state legislatures and regulatory agencies continue to propose and advance numerous legislative and regulatory initiatives seeking to mitigate the effects of climate change. As a financial institution, it is unclear how future governmental regulations and shifts in business trends resulting from increased concern about climate change will affect our operations ~~;~~, however, natural or man- made disasters and severe weather events may cause operational disruptions and damage to both our properties and properties securing our loans. Losses resulting from these disasters and severe weather events may make it more difficult for borrowers to timely repay their loans. Additionally, our customers who finance vehicles and equipment reliant on fossil fuels could face cost increases, asset value reductions, operating process changes, and the like. If these events occur, we may experience a decrease in the value of our loan and lease portfolio and our revenue, and may incur additional operational expenses, each of which could have a material adverse effect on our financial condition and results of operations. Market Risks Fluctuations in interest rates could reduce our profitability and affect the value of our assets — Like other financial institutions, we are subject to interest rate risk. Our primary source of income is net interest income, which is the difference between interest earned on loans and leases and investments, and interest paid on deposits and borrowings. We expect that we will periodically experience imbalances in the interest rate sensitivities of our assets and liabilities and the relationships of various interest rates to each other. Over any defined period of time, our interest- earning assets may be more sensitive to changes in market interest rates than our interest- bearing liabilities, or vice- versa. In addition, the individual market interest rates underlying our loan and lease and deposit products may not change to the same degree over a given time period. If market interest rates should move contrary to our position, earnings may be negatively affected. In addition, loan and lease volume and quality and deposit volume and mix can be affected by market interest rates as can the businesses of our clients. Changes in levels of market interest rates could have a material adverse effect on our net interest spread, asset quality, origination volume, and overall profitability. Additionally, changes in levels of market interest rates could cause our debt securities available- for- sale to move into unrealized loss positions which is a negative component of total shareholders' equity. Market interest rates are beyond our control, and they fluctuate in response to general economic conditions and the policies of various governmental and regulatory agencies, in particular, the Federal Reserve Board. Changes in monetary policy, including changes in interest rates, may negatively affect our ability to originate loans and leases, the value of our assets and our ability to realize gains from the sale of our assets, all of which ultimately could affect our earnings. Adverse changes in economic conditions could impair our financial condition and results of operations — We are impacted by general business and economic conditions in the United States and abroad. These conditions include short- term and long- term interest rates, inflation, money supply, political issues, legislative and regulatory changes, fluctuations in both debt and equity capital markets, broad trends in industry and finance, unemployment, infectious disease epidemics or outbreaks and the strength of the U. S. economy and the local economies in which we operate, all of which are beyond our control. A deterioration in economic conditions could result in an increase in loan delinquencies and non- performing assets, decreases in loan collateral values and a decrease in demand for our products and services. Changes in economic conditions may negatively impact the fees generated by our trust and wealth advisory business — Trust and wealth advisory fees are largely based on the size of client relationships and the market value of assets held under management. Changes in general economic conditions and in the financial and securities markets may negatively impact the value of our clients' wealth management accounts and the market value of assets held under management. Market declines, reductions in the value of our clients' accounts, and the loss of wealth management clients may negatively impact the fees generated by our trust and wealth management business and could have an adverse effect on our business, financial condition and results of operations. ~~We may be adversely impacted by the transition away from LIBOR as a reference interest rate — The London Interbank Offered Rate (" LIBOR ") is a short- term interest rate used as a pricing reference for loans, derivatives and other financial instruments. In July 2017, the United Kingdom Financial Conduct Authority, which regulates the process for establishing LIBOR, announced that it intends to stop persuading or compelling banks to submit rates for the calculation of LIBOR after 2021. In November 2020, the Federal Reserve, FDIC and OCC issued a joint statement confirming that the lesser used one- week and two- month USD LIBOR settings would cease publication at the end of 2021, but the remaining USD LIBOR settings would continue publication until June 30, 2023 to better facilitate an orderly transition. The agencies also stated that the act of entering into new contracts that use USD LIBOR as a reference rate after December 31, 2021 would create safety and soundness risks. The transition is progressing, but the exact impact it will have on financial markets and their individual participants is not currently known. Several substitute benchmarks are developing in the marketplace, with various permutations of the Secured Overnight Financing Rate (SOFR) emerging as primary market alternatives, but at this time it is not feasible to predict exactly which benchmarks will emerge as enduring substitutes for LIBOR. We convened a transition committee in 2019 to monitor market developments and implement a transition plan. Existing loans impacted by the transition~~

~~have been actively tracked, appropriate legal fallback language has been created and incorporated into documentation where appropriate and we are an adhering party to the ISDA IBOR Fallbacks Protocol. In 2021, we began to utilize other interest rate benchmarks and took necessary steps to comply with the regulatory prohibitions of originating LIBOR- denominated loans starting in 2022. We continue with our transition efforts with the expectation of completing all necessary steps prior to the June 30, 2023 deadline. As of December 31, 2022, we have approximately $ 719 million of loans and other financial instruments with attributes that are either directly or indirectly influenced by LIBOR that are scheduled to mature after June 30, 2023. The impact of the transition away from LIBOR may adversely affect revenues, expenses and the value of those financial instruments. Federal legislation governing the transition was adopted in 2022, although the transition could result in litigation with counterparties impacted by the transition as well as increased regulatory scrutiny and other adverse consequences. Any replacement benchmark ultimately adopted as a substitute for LIBOR may behave differently than LIBOR in a manner detrimental to our financial performance. Although we are currently unable to assess what the ultimate impact of the transition from LIBOR will be, failure to adequately manage the transition could have a material adverse effect on our business, financial condition and results of operation.~~ Continued elevated levels of inflation could adversely impact our business and results of operations — The U. S. has recently experienced elevated levels of inflation, with the consumer price index climbing approximately 7 % in 2022 **and increased at a more moderate rate in 2023**. Continued elevated levels of inflation could have complex effects on our business and results of operations, some of which could be materially adverse. The Federal Reserve ~~has~~ increased interest rates dramatically during 2022 **and 2023** in an effort to halt and reverse continued elevated inflation, which has negatively impacted the value of our available- for- sale investment securities portfolio. In addition, inflation- related increases in our interest expense is due to increased rates paid on deposits. Elevated levels of inflation has also caused increased volatility and uncertainty in the business environment, which could adversely affect loan demand and our clients' ability to repay indebtedness. Governmental responses to the current inflationary environment ~~could adversely affect our business~~, such as severe changes to monetary and fiscal policy, or the imposition or threatened imposition of price controls **, could adversely affect our business**. The duration and severity of the current inflationary period and the resulting impact on us cannot be predicted with precision. Liquidity Risks We could experience an unexpected inability to obtain needed liquidity **which could adversely affect our business, profitability, and viability as a going concern** — ~~Liquidity measures the ability to meet current and future cash flow needs as they become due.~~ The liquidity of a financial institution reflects its ability to meet loan requests, to accommodate possible outflows in deposits, and to take advantage of interest rate market opportunities and is essential to a financial institution' s business. The ability of a financial institution to meet its current financial obligations is a function of its balance sheet structure, its ability to liquidate assets, and its access to alternative sources of funds **. The bank failures in the Spring of 2023 exemplify the potential serious results of the unexpected inability of insured depository institutions to obtain needed liquidity to satisfy deposit withdrawal requests, including how quickly such requests can accelerate once uninsured depositors lose confidence in an institution' s ability to satisfy its obligations to depositors**. We seek to ensure our funding needs are met by maintaining a level of liquidity through asset and liability management. If we become unable to obtain funds when needed, it could have a material adverse effect on our business, financial condition, and results of operations. Additionally, under Indiana law governing the collateralization of public fund deposits, the Indiana Board for Depositories determines which financial institutions are required to pledge collateral based on the strength of their financial ratings. We have been informed that no collateral is required for our public fund deposits. However, the Board of Depositories could alter this requirement in the future, which could adversely affect our liquidity depending on the amount of collateral we may be required to pledge. We rely on dividends from our subsidiaries — We receive substantially all of our revenue from dividends from our subsidiaries, including, primarily, the Bank. These dividends are the principal source of funds we use to pay dividends on our common stock and interest and principal on our debt. Various federal and state laws and regulations limit the amount of dividends our subsidiaries may pay to us. In the event our subsidiaries are unable to pay dividends to us, we may not be able to service debt, pay other obligations, or pay dividends on our common stock. Our inability to receive dividends from our subsidiaries could have a material adverse effect on our business, financial condition and results of operations. Operational Risks Our risk management framework could prove ineffective which could have a material adverse effect on our ability to mitigate risks and / or losses — We have established a risk management framework to identify and manage our risk exposure. This framework is comprised of various processes, systems and strategies, and is designed to manage the types of risk to which we are subject, including, credit, market, liquidity, operational, legal / compliance, and reputational risks. Our framework also includes financial, analytical and forecasting modeling methodologies which involve significant management assumptions and judgment that may not be accurate, particularly in times of market stress or other unforeseen circumstances. Additionally, our Board of Directors has adopted a risk appetite statement in consultation with management which sets forth certain thresholds and limits to govern our overall risk profile. There can be no assurance that our risk management framework will be effective under all circumstances or that it will adequately identify, manage or limit any risk of loss to us. Any such failure in our risk management framework could have a material adverse effect on our business, financial condition, and results of operations. We are dependent upon the services of our management team — Our future success and profitability is substantially dependent upon our management and the banking acumen of our senior executives. We believe that our future results will also depend in part upon our ability to attract and retain highly skilled and qualified management. We are especially dependent on a limited number of key management personnel, many of whom do not have employment agreements with us. The loss of the chief executive officer and other senior management and key personnel could have a material adverse impact on our operations because other officers may not have the experience and expertise to readily replace these individuals. Many of these senior officers have primary contact with our clients and are important in maintaining ~~personalized~~ ---- **personal** relationships with our client base. The unexpected loss of services of one or more of these key employees could have a material adverse effect on our operations and possibly result in reduced revenues if we were unable to find suitable replacements promptly. Competition for senior personnel is intense, and we may not be successful in attracting and retaining such personnel. Changes in key personnel and their responsibilities may be disruptive to our businesses and could have a material adverse effect on our businesses, financial condition, and results of operations. Technology security breaches — Information security risks have increased due to the sophistication and activities of organized crime, hackers, terrorists and other external parties and the use of online, telephone, and mobile banking channels by clients. Any compromise of our security could **impair our reputation and** deter our clients from using our banking services **. Information security breaches can also disrupt the operation of information systems on which we depend, adversely affecting our business operations. Such events can result in costly remediation measures and litigation or governmental investigation and responding to security breaches can place unanticipated demands on the time and attention of management** . We rely on security systems to provide the protection and authentication necessary to secure transmission of data against damage by theft, fire, power loss, telecommunications failure or **a** similar catastrophic event, as well as from security breaches, ransomware, denial of service attacks, viruses, worms, **use of artificial intelligence** and other disruptive problems caused by hackers. Computer break- ins, phishing and other disruptions of customer or vendor systems could also jeopardize the security of information stored in and transmitted through our computer systems and network infrastructure. We maintain a cyber insurance policy that is designed to cover a majority of loss resulting from cyber security breaches, but there is no assurance such coverage **or other protective measures we employ** will be adequate to address all potential material adverse impacts. We also confront the risk of being compromised by emails sent by perpetrators posing as company executives or vendors in order to dupe company personnel into sending large sums of money to accounts controlled by the perpetrators. We require all our employees to complete annual information security awareness training to increase their awareness of these risks and to engage them in our mitigation efforts. If these precautions are not sufficient to protect our systems from data breaches or compromises, our reputation and business could be adversely affected. We depend on the services of a variety of third- party vendors to meet data processing and communication needs and we have contracted with third parties to run their proprietary software on our behalf. While we perform reviews of security controls instituted by the vendor in accordance with industry standards and institute our own internal security controls, we rely on continued maintenance of the controls by the outside party to safeguard our customer data. Additionally, we issue debit cards which are susceptible to compromise at the point of sale via the physical terminal through which transactions are processed and by other means of hacking. The security and integrity of these transactions are dependent upon the retailers' vigilance and willingness to invest in technology and upgrades. Issuing debit cards to our clients exposes us to potential losses which, in the event of a data breach at one or more major retailers may adversely affect our business, financial condition, and results of operations. We continually encounter technological change — The financial services industry is constantly undergoing rapid technological change with frequent introductions of new technology- driven products and services. ~~The effective use of technology increases efficiency and enables financial institutions to better service clients and reduce costs.~~ Our future success depends, in part, upon our ability to address the needs of our clients **competitively** by using technology to provide products and services that will satisfy client demands, as well as create additional efficiencies within our operations. Many of our large competitors have substantially greater resources to invest in technological improvements. We may not be able to effectively implement new technology- driven products and services quickly or be successful in marketing these products and services to our clients **. In addition, our implementation of certain new technologies, such as those related to artificial intelligence, automation and algorithms, in our business processes may have unintended consequences due to their limitations or our failure to use them effectively** . Failure to successfully keep pace with technological change affecting the financial services industry could have a material adverse impact on our business and, in turn, our financial condition and results of operations. Our accounting estimates rely on analytical and forecasting models — The processes we use to estimate our allowance for credit losses and to measure the fair value of financial instruments, as well as the processes used to estimate the effects of changing interest rates and other market measures on our financial condition and results of operations, depend upon the use of analytical and forecasting models. These models reflect assumptions that may not be accurate, particularly in times of market stress or other unforeseen circumstances. Even if these assumptions are adequate, the models may prove to be inadequate or inaccurate because of other flaws in their design or their implementation. Any such failure in our analytical or forecasting models could have a material adverse effect on our business, financial condition and results of operations. Legal / Compliance Risks We are subject to extensive government regulation and supervision — Our operations are subject to extensive federal and state regulation and supervision. Banking regulations are primarily intended to protect depositors' funds, federal deposit insurance funds and the banking system as a whole, not security holders. These regulations affect our lending practices, capital structure, investment practices, dividend policy and growth, among other things. Congress and federal regulatory agencies continually review banking laws, regulations and policies for possible change. Changes to statutes, regulations or regulatory policies, including changes in interpretation or implementation of statutes, regulation or policies, could affect us in substantial and unpredictable ways. Such changes could subject us to additional costs and limit the types of financial services and products we may offer. Failure to comply with laws, regulations or policies could result in sanctions by regulatory agencies, civil money penalties and / or reputation damage, which could have a material adverse effect on our business, financial condition and results of operations ~~. While we have policies and procedures designed to prevent any such violations, there can be no assurance that such violations will not occur~~ . Our investments and / or financings in certain tax- advantaged projects may not generate returns as anticipated and may have an adverse impact on our financial results — We invest and / or finance certain tax- advantaged projects promoting affordable housing, community redevelopment and renewable energy sources. Our investments in these projects are designed to generate a return primarily through the realization of federal and state income tax credits, and other tax benefits, over specified time periods. We are subject to the risk that previously recorded tax credits will not be able to be fully realized. Such credits are subject to recapture by taxing authorities based on compliance features required to be met at the project level which may not be met. The possible inability to realize these tax credits and other tax benefits can have a negative impact on our financial results.

The risk of not being able to realize the tax credits and other tax benefits depends on many factors outside of our control, including changes in the applicable tax code and the ability of the projects to be completed and properly managed. Substantial ownership concentration — Our directors, executive officers and 1st Source Bank, as trustee, collectively hold a significant ownership concentration of our common shares. Due to this significant level of ownership among our affiliates, our directors, executive officers, and 1st Source Bank, as trustee, may be able to influence the outcome of director elections or impact significant transactions, such as mergers or acquisitions, or any other matter that might otherwise be favored by other shareholders. Reputational Risks Competition from other financial services providers could adversely impact our results of operations — The banking and financial services business is highly competitive. We face competition in making loans and leases, attracting deposits and providing insurance, investment, trust and wealth advisory, and other financial services. Increased competition in the banking and financial services businesses may reduce our market share, impair our growth or cause the prices we charge for our services to decline. Our results of operations may be adversely impacted in future periods depending upon the level and nature of competition we encounter in our various market areas. Managing reputational risk is important to attracting and maintaining customers, investors, and employees — Threats to our reputation can come from many sources, including adverse sentiment about financial institutions generally, unethical practices, employee misconduct, failure to deliver minimum standards of service or quality, **data security failures,** compliance deficiencies, and questionable or fraudulent activities of our customers. We have policies and procedures in place that seek to protect our reputation and promote ethical conduct. Nonetheless, negative publicity may arise regarding our business, employees, or customers, with or without merit, and could result in the loss of customers, investors, or employees, costly litigation, a decline in revenues, and increased government regulation. In addition, focus among investors, customers, and regulators on environmental, social and governance (" ESG ") issues has continued to increase in recent years. Customers, prospective customers, investors or third parties evaluate us based on their assessment of our achievement of ESG objectives and may assign their ESG ratings to us. Such persons may believe that our practices, including our lending practices, are not sufficiently robust from an ESG perspective and may publish their views. Adverse publicity regarding such assessments of our ESG performance could damage our reputation or prospects. **Adverse market perception can adversely affect the trading price of our shares.**