

Bankwell Financial Group, Inc.  
Form 10-Q  
November 14, 2014

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UNITED STATES  
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 September 30, 2014

- TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

For the transition period from \_\_\_\_\_ to \_\_\_\_\_

Commission File Number: 001-36448

Bankwell Financial Group, Inc.  
(Exact Name of Registrant as specified in its Charter)

Connecticut  
(State or other jurisdiction of  
Incorporation or organization)

20-8251355  
(I.R.S. Employer  
Identification No.)

220 Elm Street  
New Canaan, Connecticut 06840  
(203) 652-0166

(Address, including zip code, and telephone number, including area code, of registrant's principal executive offices)

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 definitions of "large accelerated filer," "accelerated filer" and "smaller reporting company" in Rule 12b-2 of the Exchange Act.

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

Accelerated filer   
Smaller reporting company

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

As of October 31, 2014, there were 7,068,382 shares of the registrant's common stock outstanding.

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## PART 1 – FINANCIAL INFORMATION

## Item 1. Financial Statements

Bankwell Financial Group, Inc.

Consolidated Balance Sheets - (Unaudited)

(Dollars in thousands, except share data)

	September 30, 2014	December 31, 2013
<b>ASSETS</b>		
Cash and due from banks	\$35,566	\$82,013
Held to maturity investment securities, at amortized cost (Note 2)	11,502	13,816
Available for sale investment securities, at fair value (Note 2)	67,537	28,597
Loans held for sale	-	100
Loans receivable (net of allowance for loan losses of \$9,552 at September 30, 2014 and \$8,382 at December 31, 2013) (Note 3)	730,148	621,830
Foreclosed real estate	829	829
Accrued interest receivable	2,670	2,360
Federal Home Loan Bank stock, at cost	4,834	4,834
Premises and equipment, net	7,787	7,060
Bank-owned life insurance	22,837	10,031
Other intangible assets	401	481
Deferred income taxes, net	5,804	5,845
Other assets	5,600	1,822
<b>Total assets</b>	<b>\$895,515</b>	<b>\$779,618</b>
<b>LIABILITIES AND SHAREHOLDERS' EQUITY</b>		
<b>Liabilities</b>		
<b>Deposits</b>		
Noninterest bearing deposits	\$151,146	\$118,618
Interest bearing deposits	544,117	542,927
<b>Total deposits</b>	<b>695,263</b>	<b>661,545</b>
Advances from the Federal Home Loan Bank	77,000	44,000
Accrued expenses and other liabilities	4,755	4,588
<b>Total liabilities</b>	<b>777,018</b>	<b>710,133</b>
<b>Shareholders' equity (Notes 4, 5 and 7)</b>		
Preferred stock, senior noncumulative perpetual, Series C, no par; 10,980 shares issued at September 30, 2014 and December 31, 2013, respectively; liquidation value of \$1,000 per share	10,980	10,980
Common stock, no par value; 10,000,000 shares authorized, 6,559,995 and 3,876,393 shares issued at September 30, 2014 and December 31, 2013, respectively	97,180	52,105
Retained earnings	9,735	5,976
Accumulated other comprehensive income	602	424
<b>Total shareholders' equity</b>	<b>118,497</b>	<b>69,485</b>

Total liabilities and shareholders' equity	\$895,515	\$779,618
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See accompanying notes to consolidated financial statements (unaudited)

Bankwell Financial Group, Inc.  
Consolidated Statements of Income – (Unaudited)  
(Dollars in thousands, except per share amounts)

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2014	2013	2014	2013
<b>Interest and dividend income</b>				
Interest and fees on loans	\$8,054	\$6,748	\$23,040	\$19,619
Interest and dividends on securities	569	355	1,417	1,040
Interest on cash and cash equivalents	45	18	116	39
<b>Total interest income</b>	<b>8,668</b>	<b>7,121</b>	<b>24,573</b>	<b>20,698</b>
<b>Interest expense</b>				
Interest expense on deposits	905	600	2,257	1,553
Interest on Borrowings	168	127	427	417
<b>Total interest expense</b>	<b>1,073</b>	<b>727</b>	<b>2,684</b>	<b>1,970</b>
<b>Net interest income</b>	<b>7,595</b>	<b>6,394</b>	<b>21,889</b>	<b>18,728</b>
<b>Provision for loan losses</b>	<b>566</b>	<b>47</b>	<b>847</b>	<b>489</b>
<b>Net interest income after provision for loan losses</b>	<b>7,029</b>	<b>6,347</b>	<b>21,042</b>	<b>18,239</b>
<b>Noninterest income</b>				
Gains and fees from sales of loans	366	972	1,008	1,737
Service charges and fees	153	100	420	297
Bank owned life insurance	135	-	305	-
Net gain on sale of available for sale securities	-	-	-	648
Gain (loss) on sale of foreclosed real estate, net	-	(16)	-	49
Other	103	27	475	141
<b>Total noninterest income</b>	<b>757</b>	<b>1,083</b>	<b>2,208</b>	<b>2,872</b>
<b>Noninterest expense</b>				
Salaries and employee benefits	2,786	2,894	9,412	8,146
Occupancy and equipment	1,066	836	3,162	2,410
Professional services	394	422	1,035	1,212
Data processing	314	280	949	787
Director fees	177	142	460	426
Merger and acquisition related expenses	145	-	408	64
Marketing	135	378	463	776
FDIC insurance	120	36	345	267
Amortization of intangibles	27	-	80	-
Foreclosed real estate	9	1	21	4
Other	357	342	1,134	950
<b>Total noninterest expense</b>	<b>5,530</b>	<b>5,331</b>	<b>17,469</b>	<b>15,042</b>

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Income before income tax expense	2,256	2,099	5,781	6,069
Income tax expense	765	780	1,940	2,270
Net income	\$1,491	\$1,319	\$3,841	\$3,799
Net income attributable to common shareholders	\$1,441	\$1,271	\$3,677	\$3,660
Earnings per common share - basic	\$0.22	\$0.38	\$0.72	\$1.12
Earnings per common share - diluted	0.22	0.37	0.72	1.10

See accompanying notes to consolidated financial statements (unaudited)

Bankwell Financial Group, Inc.  
 Consolidated Statements of Comprehensive Income – (Unaudited)  
 (In thousands)

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2014	2013	2014	2013
Net income	\$ 1,491	\$ 1,319	\$ 3,841	\$ 3,799
Other comprehensive income (loss):				
Unrealized gains (losses) on securities:				
Unrealized holding gains (losses) on available for sale securities	(253 )	(13 )	180	(920 )
Reclassification adjustment for (gain) loss realized in net income	-	-	-	(648 )
Net change in unrealized gain (loss)	(253 )	(13 )	180	(1,568 )
Tax effect - (expense) benefit	99	5	(70 )	610
Unrealized gains (losses) on securities, net of tax	(154 )	(8 )	110	(958 )
Unrealized gains (losses) on interest rate swap:				
Unrealized gains (losses) on interest rate swaps designated as cash flow hedge	218	-	111	-
Tax effect - (expense) benefit	(85 )	-	(43 )	-
Unrealized gains (losses) on interest rate swap	133	-	68	-
Total other comprehensive income (loss)	(21 )	(8 )	178	(958 )
Comprehensive income	\$ 1,470	\$ 1,311	\$ 4,019	\$ 2,841

See accompanying notes to consolidated financial statements (unaudited)



Bankwell Financial Group, Inc.  
Consolidated Statements of Shareholders' Equity – (Unaudited)  
(In thousands, except share data)

	Preferred Stock	Common Stock	Retained Earnings	Accumulated Other Comprehensive Income (Loss)	Total
Balance at December 31, 2012	\$ 10,980	\$ 38,117	\$ 926	\$ 1,511	\$ 51,534
Net income	-	-	3,799	-	3,799
Other comprehensive loss, net of tax	-	-	-	(958 )	(958 )
Preferred stock dividends	-	-	(84 )	-	(84 )
Stock based compensation expense	-	205	-	-	205
Capital from exercise of stock options	-	471	-	-	471
Capital from private placement	-	13,178	-	-	13,178
Balance at September 30, 2013	\$ 10,980	\$ 51,971	\$ 4,641	\$ 553	\$ 68,145

	Preferred Stock	Common Stock	Retained Earnings	Accumulated Other Comprehensive Income	Total
Balance at December 31, 2013	\$ 10,980	\$ 52,105	\$ 5,976	\$ 424	\$ 69,485
Net income	-	-	3,841	-	3,841
Other comprehensive income, net of tax	-	-	-	178	178
Preferred stock dividends	-	-	(82 )	-	(82 )
Stock based compensation expense	-	164	-	-	164
Capital from exercise of stock options	-	207	-	-	207
Issuance of 2,702,703 shares, net of expenses	-	44,704	-	-	44,704
Balance at September 30, 2014	\$ 10,980	\$ 97,180	\$ 9,735	\$ 602	\$ 118,497

See accompanying notes to consolidated financial statements (unaudited)

Bankwell Financial Group, Inc.  
Consolidated Statements of Cash Flows – (Unaudited)  
(In thousands)

	Nine Months Ended September 30,	
	2014	2013
<b>Cash flows from operating activities</b>		
Net income	\$3,841	\$3,799
Adjustments to reconcile net income to net cash provided by operating activities:		
Net amortization of premiums and discounts on investment securities	82	151
Provision for loan losses	847	489
Benefit for deferred taxes	(213 )	(43 )
Net gain on sales of available for sale securities	-	(648 )
Depreciation and amortization	835	440
Increase in cash surrender value of bank-owned life insurance	(305 )	-
Loans originated for sale	(22,465 )	(59,580 )
Proceeds from sales of loans	23,572	61,316
Net gain on sales of loans	(1,008 )	(1,737 )
Equity-based compensation	164	205
Net accretion of purchase accounting adjustments	(352 )	-
Gain on sale of foreclosed real estate	-	(49 )
Net change in:		
Deferred loan fees	583	297
Accrued interest receivable	(311 )	(55 )
Other assets	(3,524 )	(71 )
Accrued expenses and other liabilities	167	(1,390 )
Net cash provided by operating activities	1,913	3,124
<b>Cash flows from investing activities</b>		
Proceeds from principal repayments on available for sale securities	3,307	638
Proceeds from principal repayments on held to maturity securities	2,308	145
Net proceeds from sales and calls of available for sale securities	1,620	10,194
Purchases of held to maturity securities	-	(7,700 )
Purchase of available for sale securities	(43,763 )	-
Purchase of bank-owned life insurance	(12,500 )	-
Net increase in loans	(109,323 )	(54,334 )
Purchases of premises and equipment	(1,562 )	(450 )
Purchase of Federal Home Loan Bank stock	-	(134 )
Proceeds from sale of foreclosed real estate	-	1,011
Net cash used by investing activities	(159,913 )	(50,630 )

See accompanying notes to consolidated financial statements (unaudited)

Consolidated Statements of Cash Flows- (Continued)  
(In thousands)

	Nine Months Ended September 30,	
	2014	2013
<b>Cash flows from financing activities</b>		
Net change in time certificates of deposit	\$ 38,569	\$ 68,400
Net change in other deposits	(4,845 )	13,643
Net proceeds (repayments) from short term FHLB advances	40,000	(13,000 )
Net proceeds (repayments) from long term FHLB advances	(7,000 )	(13,000 )
Proceeds from issuance of common stock	44,704	13,178
Proceeds from exercise of options	207	471
Dividends paid on preferred stock	(82 )	(84 )
Net cash provided by financing activities	111,553	69,608
Net increase (decrease) in cash and cash equivalents	(46,447 )	22,102
<b>Cash and cash equivalents:</b>		
Beginning of year	82,013	28,927
End of period	\$ 35,566	\$ 51,029
<b>Supplemental disclosures of cash flows information:</b>		
<b>Cash paid for:</b>		
Interest	\$ 2,742	\$ 1,872
Income taxes	450	2,042
Noncash investing and financing activities	-	-

See accompanying notes to consolidated financial statements (unaudited)

Bankwell Financial Group, Inc.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS – (Unaudited)

## 1. Nature of Operations and Summary of Significant Accounting Policies

Bankwell Financial Group, Inc. (the “Company” or “Bankwell”) is a bank holding company headquartered in New Canaan, Connecticut. The Company offers a broad range of financial services through its banking subsidiary, Bankwell Bank, (the “Bank”). The Bank was originally chartered as two separate banks, The Bank of New Canaan (“BNC”) and The Bank of Fairfield (“TBF”). In September 2013, BNC and TBF were merged and rebranded as “Bankwell Bank.” In November 2013, the Bank acquired The Wilton Bank (“Wilton”), which added one branch and approximately \$25.1 million in loans and \$64.2 million in deposits. See Note 12, Mergers and Acquisitions, for further information on the acquisition.

The Bank is a Connecticut state chartered commercial bank, founded in 2002, whose deposits are insured under the Deposit Insurance Fund administered by the Federal Deposit Insurance Corporation (“FDIC”). The Bank provides a full range of banking services to commercial and consumer customers, primarily concentrated in the Fairfield County region of Connecticut, with branch locations in New Canaan, Stamford, Fairfield and Wilton Connecticut. The Company has received approval from its regulators to establish a branch location in Norwalk, Connecticut, which is expected to open in the first quarter of 2015. In addition, The Company acquired Quinnipiac Bank and Trust Company on October 1, 2014. The acquisition expanded the Company’s branch locations to New Haven County, Connecticut, adding a branch in Hamden Connecticut and North Haven, Connecticut. See note 13, *Subsequent Events* for further information about the merger with Quinnipiac Bank and Trust Company.

### Principles of consolidation

The consolidated interim financial statements include the accounts of the Company and the Bank. All significant intercompany accounts and transactions have been eliminated in consolidation.

### Use of estimates

The accounting and reporting policies of the Company conform to accounting principles generally accepted in the United States of America (“GAAP”) and general practices within the banking industry. In preparing the interim consolidated financial statements, management is required to make estimates and assumptions that affect the reported amounts of assets and liabilities, and disclosures of contingent assets and liabilities as of the date of the balance sheet and revenue and expenses for the period. Actual results could differ from those estimates. Material estimates that are particularly susceptible to significant change in the near term relate to deferred taxes, the fair values of financial instruments and the determination of the allowance for loan losses.

### Basis of consolidated financial statement presentation

The unaudited consolidated financial statements presented herein have been prepared pursuant to the rules of the Securities and Exchange Commission (“SEC”) for quarterly reports on Form 10-Q and Rule 10-1 of Regulation S-X and do not include all of the information and note disclosures required by GAAP. In the opinion of management, all adjustments (consisting of normal recurring adjustments) and disclosures considered necessary for the fair presentation of the accompanying unaudited interim consolidated financial statements have been included. Interim results are not necessarily reflective of the results that may be expected for the year ending December 31, 2014. The accompanying unaudited interim consolidated financial statements should be read in conjunction with the audited

consolidated financial statements and notes thereto included in the Registration Statement on Form S-1 for the year ended December 31, 2013.

Significant concentrations of credit risk

Most of the Company's activities are with customers located within Fairfield County and the surrounding region of Connecticut, and declines in property values in these areas could significantly impact the Company. The Company has significant concentrations in commercial real estate loans. Management does not believe they present any special risk. The Company does not have any significant concentrations in any one industry or customer.

Bankwell Financial Group, Inc.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS – (Unaudited)

#### Derivative Instruments

The Company enters into interest rate swap agreements as part of the Company's interest rate risk management strategy. Management applies the hedge accounting provisions of Accounting Standards Codification ("ASC") Topic 815, and formally documents at inception all relationships between hedging instruments and hedged items, as well as its risk management objectives and strategies for undertaking the various hedges. Additionally, the Company uses dollar offset or regression analysis at the hedge's inception and for each reporting period thereafter, to assess whether the derivative used in its hedging transaction is expected to be and has been highly effective in offsetting changes in the fair value or cash flows of the hedged item. The Company discontinues hedge accounting when it is determined that a derivative is not expected to be or has ceased to be highly effective as a hedge, and then reflects changes in fair value of the derivative in earnings after termination of the hedge relationship.

The Company has characterized all of its interest rate swaps that qualify under Topic 815 hedge accounting as cash flow hedges. Cash flow hedges are used to minimize the variability in cash flows of assets or liabilities, or forecasted transactions caused by interest rate fluctuations, and are recorded at fair value in other assets within the consolidated balance sheet. Changes in the fair value of these cash flow hedges are initially recorded in accumulated other comprehensive income and subsequently reclassified into earnings when the forecasted transaction affects earnings. Any hedge ineffectiveness assessed as part of the Company's quarterly analysis is recorded directly to earnings.

#### Reclassification

Certain prior period amounts have been reclassified to conform to the 2014 financial statement presentation. These reclassifications only changed the reporting categories and did not affect the results of operations or consolidated financial position.

#### Recent accounting pronouncements

The following section includes changes in accounting principles and potential effects of new accounting guidance and pronouncements.

ASU No. 2013-11-Income Taxes (Topic 740) - Presentation of an Unrecognized Tax Benefit When a Net Operating Loss Carryforward, a Similar Tax Loss, or a Tax Credit Carryforward Exists (a consensus of the FASB Emerging Issues Task Force).

As a result of applying this ASU, an unrecognized tax benefit should be presented as a reduction of a deferred tax asset for a net operating loss ("NOL") or other tax credit carryforward when settlement in this manner is available under the tax law. The assessment of whether settlement is available under the tax law would be based on facts and circumstances as of the balance sheet reporting date and would not consider future events (e.g., upcoming expiration of related NOL carryforwards). This classification should not affect an entity's analysis of the realization of its deferred tax assets. Gross presentation in the roll forward of unrecognized tax positions in the notes to the financial statements will still be required. For the Company, the update was effective prospectively for annual reporting periods beginning on or after January 1, 2014, and interim periods within those annual periods. Retrospective application is permitted. Adoption of this ASU did not have a material impact on the Company's consolidated financial statements.



Bankwell Financial Group, Inc.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS – (Unaudited)

ASU No. 2014-04 - Troubled Debt Restructuring by Creditors (Subtopic 310-40) - Reclassification of Residential Real Estate Collateralized Consumer Mortgage Loans upon Foreclosure (a consensus of the FASB Emerging Issues Task Force).

The amendments in this update apply to all creditors who obtain physical possession (resulting from an in substance repossession or foreclosure) of residential real estate property collateralizing a consumer mortgage loan in satisfaction of a receivable. The objective of the amendments in this update is to reduce diversity by clarifying when an in substance repossession or foreclosure occurs, that is, 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 receivable should be derecognized and the real estate property recognized. Additionally, the amendments require interim and annual disclosure of both (1) the amount of foreclosed residential real estate property held by the creditor and (2) the recorded investment in consumer mortgage loans collateralized by residential real estate property that are in the process of foreclosure according to requirements of the applicable jurisdiction. The amendments in this update are effective for the Company for annual reporting periods beginning on or after January 1, 2015, and interim periods within those annual periods. Adoption of this ASU is not expected to have a material impact on the Company's consolidated financial statements.

ASU No. 2014-09 - Revenue from Contracts with Customers (Topic 660).

This update requires an entity to recognize the amount of revenue to which it expects to be entitled for the transfer of promised goods or services to customers. The ASU will replace most existing revenue recognition guidance in U.S. GAAP when it becomes effective. The new standard is effective for the Company on January 1, 2017. Early application is not permitted. The standard permits the use of either the retrospective or cumulative effect transition method. The Company is evaluating the effect that ASU 2014-09 will have on its consolidated financial statements and related disclosures. The Company has not yet selected a transition method nor has it determined the effect of the standard on its ongoing financial reporting.

ASU No. 2014-12 - Compensation-Stock Compensation (Topic 718) - Accounting for Share-Based Payments When the Terms of an Award Provide That a Performance Target Could Be Achieved after the Requisite Service Period a consensus of the FASB Emerging Issues Task Force.

The amendments in this update require that a performance target that affects vesting and that could be achieved after the requisite service period be treated as a performance condition. As such, the performance target should not be reflected in estimating the grant-date fair value of the award. Compensation cost should be recognized in the period in which it becomes probable that the performance target will be achieved and should represent the compensation cost attributable to the period(s) for which the requisite service has already been rendered. If the performance target becomes probable of being achieved before the end of the requisite service period, the remaining unrecognized compensation cost should be recognized prospectively over the remaining requisite service period. The amendments in this update are effective for the Company for annual periods and interim periods beginning on or after January 1, 2016. Earlier adoption is permitted. Adoption of this ASU is not expected to have a material impact on the Company's consolidated financial statements.



Bankwell Financial Group, Inc.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS – (Unaudited)

ASU No. 2014-14 - Receivables - Troubled Debt Restructurings by Creditors (Subtopic 310-40) - Classification of Certain Government-Guaranteed Mortgage Loans upon Foreclosure a Consensus of the FASB Emerging Issues Task Force.

The objective of this update is to reduce the diversity in classification of government-guaranteed mortgage loans, including FHA or VA guaranteed loans, upon foreclosure. The amendments in this update are effective for the Company for annual periods and interim periods beginning on or after January 1, 2016. Earlier adoption is permitted. Adoption of this ASU is not expected to have a material impact on the Company's consolidated financial statements.

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Bankwell Financial Group, Inc.

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS – (Unaudited)

## 2. Investment Securities

The amortized cost, gross unrealized gains and losses and fair values of available for sale and held to maturity securities at September 30, 2014 were as follows:

	Amortized Cost (In thousands)	September 30, 2014 Gross Unrealized Gains                      Losses		Fair Value
<b>Available for sale securities:</b>				
<b>U.S. Government and agency obligations</b>				
Due from one through five years	\$ 4,994	\$ 5	\$ (59 )	\$ 4,940
Due from five through ten years	20,995	15	(174 )	20,836
Due after ten years	7,961	2	(4 )	7,959
	33,950	22	(237 )	33,735
<b>State agency and municipal obligations</b>				
Due from five through ten years	9,314	248	(63 )	9,499
Due after ten years	7,244	562	(4 )	7,802
	16,558	810	(67 )	17,301
<b>Corporate bonds</b>				
Due in less than one year	1,000	6	-	1,006
Due from one through five years	8,206	338	(9 )	8,535
Due from five through ten years	6,126	-	(70 )	6,056
	15,332	344	(79 )	15,597
<b>Government-sponsored mortgage-backed securities</b>				
	822	82	-	904
<b>Total available for sale securities</b>	<b>\$ 66,662</b>	<b>\$ 1,258</b>	<b>\$ (383 )</b>	<b>\$ 67,537</b>
<b>Held to maturity securities:</b>				
<b>U.S. Government and agency obligations</b>				
Due from one through five years	\$ 1,013	\$ 1	\$ -	\$ 1,014
<b>State agency and municipal obligations</b>				
Due after ten years	9,210	-	-	9,210
<b>Corporate bonds</b>				
Due from five through ten years	1,000	2	-	1,002
<b>Government-sponsored mortgage-backed securities</b>				
	279	34	-	313
<b>Total held to maturity securities</b>	<b>\$ 11,502</b>	<b>\$ 37</b>	<b>\$ -</b>	<b>\$ 11,539</b>

Bankwell Financial Group, Inc.

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS – (Unaudited)

The amortized cost, gross unrealized gains and losses and fair values of available for sale and held to maturity securities at December 31, 2013 were as follows:

	December 31, 2013			
	Amortized Cost	Gross Gains	Unrealized Losses	Fair Value
	(In thousands)			
<b>Available for sale securities:</b>				
U.S. Government and agency obligations				
Due from one through five years	\$1,000	\$-	\$(17 )	\$983
Due from five through ten years	4,997	-	(292 )	4,705
	5,997	-	(309 )	5,688
State agency and municipal obligations				
Due from five through ten years	3,125	152	-	3,277
Due after ten years	8,480	375	-	8,855
	11,605	527	-	12,132
Corporate bonds				
Due from one through five years	9,166	411	(11 )	9,566
Government-sponsored mortgage-backed securities	1,133	78	-	1,211
<b>Total available for sale securities</b>	<b>\$27,901</b>	<b>\$1,016</b>	<b>\$(320 )</b>	<b>\$28,597</b>
<b>Held to maturity securities:</b>				
U.S. Government and agency obligations				
Due from one through five years	\$1,021	\$-	\$(2 )	\$1,019
State agency and municipal obligations				
Due after ten years	11,461	-	-	11,461
Corporate bonds				
Due from five through ten years	1,000	-	(27 )	973
Government-sponsored mortgage-backed securities	334	28	-	362
<b>Total held to maturity securities</b>	<b>\$13,816</b>	<b>\$28</b>	<b>\$(29 )</b>	<b>\$13,815</b>

There were no sales of, or realized gains or losses on investment securities during the three and nine months ended September 30, 2014. The realized gain on the sale of investment securities totaled \$0 and \$648 thousand for the three and nine months ended September 30, 2013, respectively.

At September 30, 2014 and December 31, 2013, securities with approximate fair values of \$6.8 million and \$6.2 million, respectively, were pledged as collateral for public deposits.

Bankwell Financial Group, Inc.

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS – (Unaudited)

The following table provides information regarding investment securities with unrealized losses, aggregated by investment category and length of time that individual securities had been in a continuous unrealized loss position at September 30, 2014 and December 31, 2013:

	Length of Time in Continuous Unrealized Loss Position					
	Less Than 12 Months		12 Months or More		Total	
	Fair Value	Unrealized Loss	Fair Value	Unrealized Loss	Fair Value	Unrealized Loss
(In thousands)						
<b>September 30, 2014</b>						
U.S. Government and agency obligations	\$16,947	\$(54)	\$5,815	\$(183)	\$22,762	\$(237)
State agency & municipal obligations	3,024	(67)	-	-	3,024	(67)
Corporate bonds	7,053	(73)	993	(6)	8,046	(79)
<b>Total investment securities</b>	<b>\$27,024</b>	<b>\$(194)</b>	<b>\$6,808</b>	<b>\$(189)</b>	<b>\$33,832</b>	<b>\$(383)</b>
<b>December 31, 2013</b>						
U.S. Government and agency obligations	\$5,797	\$(222)	\$910	\$(89)	\$6,707	\$(311)
Corporate bonds	-	-	1,961	(38)	1,961	(38)
<b>Total investment securities</b>	<b>\$5,797</b>	<b>\$(222)</b>	<b>\$2,871</b>	<b>\$(127)</b>	<b>\$8,668</b>	<b>\$(349)</b>

There were thirty one and eight individual investment securities as of September 30, 2014 and December 31 2013, respectively, in which the fair value of the security was less than the amortized cost of the security. Management believes the unrealized losses are temporary and are the result of recent market conditions, and determined that there has been no deterioration in credit quality subsequent to purchase.

The U.S. Government and agency obligations owned are either direct obligations of the U.S. Government or are issued by one of the shareholder-owned corporations chartered by the U.S. Government and therefore the contractual cash flows are guaranteed. The Company continually monitors its municipal bond portfolio and at this time this portfolio has minimal default risk because corporate and municipal bonds are all rated above investment grade. The U.S. Government and agency obligations, state agency and municipal bonds, and corporate bonds have experienced declines due to general market conditions. Management determined that there has been no deterioration in credit quality subsequent to purchase and believes that unrealized losses are temporary, resulting from recent market conditions.

Bankwell Financial Group, Inc.

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS – (Unaudited)

## 3. Loans Receivable and Allowance for Loan Losses

Loans acquired in connection with the Wilton acquisition in November 2013 are referred to as “acquired” loans as a result of the manner in which they are accounted for. All other loans are referred to as “originated” loans. Accordingly, selected credit quality disclosures that follow are presented separately for the originated loan portfolio and the acquired loan portfolio.

The following table sets forth a summary of the loan portfolio at September 30, 2014 and December 31, 2013:

(In thousands)	September 30, 2014			December 31, 2013		
	Originated	Acquired	Total	Originated	Acquired	Total
<b>Real estate loans:</b>						
Residential	\$ 167,362	\$ -	\$ 167,362	\$ 155,874	\$ -	\$ 155,874
Commercial	394,004	6,911	400,915	305,823	9,939	315,762
Construction	52,387	893	53,280	44,187	7,308	51,495
Home equity	9,539	3,294	12,833	9,625	3,872	13,497
	623,292	11,098	634,390	515,509	21,119	536,628
Commercial business	105,123	2,038	107,161	92,173	2,374	94,547
Consumer	190	343	533	225	612	837
Total loans	728,605	13,479	742,084	607,907	24,105	632,012
Allowance for loan losses	(9,552 )	-	(9,552 )	(8,382 )	-	(8,382 )
Deferred loan origination fees, net	(2,400 )	-	(2,400 )	(1,785 )	(31 )	(1,816 )
Unamortized loan premiums	16	-	16	16	-	16
Loans receivable, net	\$ 716,669	\$ 13,479	\$ 730,148	\$ 597,756	\$ 24,074	\$ 621,830

Lending activities are conducted principally in the Fairfield County region of Connecticut, and consist of residential and commercial real estate loans, commercial business loans and a variety of consumer loans. Loans may also be granted for the construction of residential homes and commercial properties. All residential and commercial mortgage loans are collateralized by first or second mortgages on real estate.

The following table summarizes activity in the accretable yields for the acquired loan portfolio for the three and nine months ended September 30, 2014:

(In thousands)	Three Months Ended September 30, 2014
Balance at beginning of period	\$ 817
Acquisition	-
Accretion	(81 )

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Other (a)		-
Balance at end of period	\$	736
		Nine Months Ended
(In thousands)		September 30, 2014
Balance at beginning of period	\$	1,418
Acquisition		-
Accretion		(338 )
Other (a)		(344 )
Balance at end of period	\$	736

a) Represents changes in cash flows expected to be collected due to loan sales or payoffs.

Bankwell Financial Group, Inc.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS – (Unaudited)

#### Risk management

The Company has established credit policies applicable to each type of lending activity in which it engages. The Company evaluates the creditworthiness of each customer and, in most cases, extends credit of up to 80% of the market value of the collateral, depending on the borrowers' creditworthiness and the type of collateral. The market value of collateral is monitored on an ongoing basis and additional collateral is obtained when warranted. Real estate is the primary form of collateral. Other important forms of collateral are business assets, time deposits and marketable securities. While collateral provides assurance as a secondary source of repayment, the Company ordinarily requires the primary source of repayment to be based on the borrower's ability to generate continuing cash flows. The Company's policy for residential lending allows that, generally, the amount of the loan may not exceed 80% of the original appraised value of the property. In certain situations, the amount may be up to 90-95% LTV either with private mortgage insurance being required for that portion of the residential loan in excess of 80% of the appraised value of the property or where secondary financing is provided by a housing authority program second mortgage, a community's low/moderate income housing program, or a religious or civic organization. Private mortgage insurance is required for that portion of the residential loan in excess of 80% of the appraised value of the property.

#### Credit quality of loans and the allowance for loan losses

Management segregates the loan portfolio into portfolio segments which is defined as the level at which the Company develops and documents a systematic method for determining its allowance for loan losses. The portfolio segments are segregated based on loan types and the underlying risk factors present in each loan type. Such risk factors are periodically reviewed by management and revised as deemed appropriate.

The Company's loan portfolio is segregated into the following portfolio segments:

**Residential Real Estate:** This portfolio segment consists of the origination of first mortgage loans secured by one-to four-family owner occupied residential properties and residential construction loans to individuals to finance the construction of residential dwellings for personal use located in our market area.

**Commercial Real Estate:** This portfolio segment includes loans secured by commercial real estate, non-owner occupied one-to four-family and multi-family dwellings for property owners and businesses in our market area. Loans secured by commercial real estate generally have larger loan balances and more credit risk than owner occupied one-to four-family mortgage loans.

**Construction:** This portfolio segment includes commercial construction loans for commercial development projects, including condominiums, apartment buildings, and single family subdivisions as well as office buildings, retail and other income producing properties and land loans, which are loans made with land as security. Construction and land development financing generally involves greater credit risk than long-term financing on improved, owner-occupied real estate. Risk of loss on a construction loan depends largely upon the accuracy of the initial estimate of the value of the property at completion of construction compared to the estimated cost (including interest) of construction and other assumptions. If the estimate of construction cost proves to be inaccurate, the Company may be required to advance additional funds beyond the amount originally committed in

order to protect the value of the property. Moreover, if the estimated value of the completed project proves to be inaccurate, the borrower may hold a property with a value that is insufficient to assure full repayment. Construction loans also expose the Company to the risks that improvements will not be completed on time in accordance with specifications and projected costs and that repayment will depend on the successful operation or sale of the properties, which may cause some borrowers to be unable to continue with debt service which exposes the Company to greater risk of non-payment and loss.

Home Equity: This portfolio segment primarily includes home equity loans and home equity lines of credit secured by owner occupied one-to four-family residential properties. Loans of this type are written at a maximum of 80% of the appraised value of the property and the Company requires a second lien position on the property. These loans can be affected by economic conditions and the values of the underlying properties.



Bankwell Financial Group, Inc.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS – (Unaudited)

**Commercial Business:** This portfolio segment includes commercial business loans secured by assignments of corporate assets and personal guarantees of the business owners. Commercial business loans generally have higher interest rates and shorter terms than other loans, but they also may involve higher average balances, increased difficulty of loan monitoring and a higher risk of default since their repayment generally depends on the successful operation of the borrower's business.

**Consumer:** This portfolio segment includes loans secured by savings or certificate accounts, or automobiles, as well as unsecured personal loans and overdraft lines of credit. This type of loan entails greater risk than residential mortgage loans, particularly in the case of loans that are unsecured or secured by assets that depreciate rapidly.

An unallocated component is maintained, when needed, to cover uncertainties that could affect management's estimate of probable losses. The unallocated component of the allowance reflects the margin of imprecision inherent in the underlying assumptions used in the methodologies for estimating allocated and general reserves in the portfolio. The unallocated allowance is used to provide for an unidentified loss that may exist in emerging problem loans that cannot be fully quantified or may be affected by conditions not fully understood as of the balance sheet date. The unallocated allowance was \$0 at September 30, 2014 and December 31, 2013, respectively.

Allowance for loan losses

The following tables set forth the activity in the Company's allowance for loan losses for the three and nine months ended September 30, 2014 and 2013, by portfolio segment:

	Residential Real Estate	Commercial Real Estate	Construction	Home Equity	Commercial Business	Consumer	Unallocated	Total
	(In thousands)							
<b>Three Months Ended</b>								
<b>September 30, 2014</b>								
<b>Originated</b>								
Beginning balance	\$ 1,392	\$ 4,024	\$ 776	\$ 188	\$ 2,291	\$ 6	\$ 307	\$ 8,984
Charge-offs	-	-	-	-	-	-	-	-
Recoveries	-	-	-	-	-	1	-	1
Provisions	19	637	115	3	100	-	(307 )	567
Ending balance	\$ 1,411	\$ 4,661	\$ 891	\$ 191	\$ 2,391	\$ 7	\$ -	\$ 9,552
<b>Acquired</b>								
Beginning balance	\$ -	\$ -	\$ -	\$ -	\$ 1	\$ -	\$ -	\$ 1
Charge-offs	-	-	-	-	-	-	-	-
Recoveries	-	-	-	-	-	-	-	-

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Provisions	-	-	-	-	(1 )	-	-	(1 )
Ending balance	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -
<b>Total</b>								
Beginning balance	\$ 1,392	\$ 4,024	\$ 776	\$ 188	\$ 2,292	\$ 6	\$ 307	\$ 8,985
Charge-offs	-	-	-	-	-	-	-	-
Recoveries	-	-	-	-	-	1	-	1
Provisions	19	637	115	3	99	-	(307 )	566
Ending balance	\$ 1,411	\$ 4,661	\$ 891	\$ 191	\$ 2,391	\$ 7	\$ -	\$ 9,552

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Bankwell Financial Group, Inc.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS – (Unaudited)

	Residential Real Estate	Commercial Real Estate	Construction	Home Equity	Commercial Business	Consumer	Unallocated	Total
	(In thousands)							
<b>Three Months Ended September 30, 2013</b>								
Beginning balance	\$ 1,326	\$ 3,672	\$ 1,013	\$ 213	\$ 1,766	\$ 91	\$ 143	8,224
Charge-offs	-	-	-	-	-	-	-	-
Recoveries	-	-	-	-	-	6	-	6
Provisions	143	(81 )	(85 )	(1 )	286	(87 )	(128 )	47
Ending balance	\$ 1,469	\$ 3,591	\$ 928	\$ 212	\$ 2,052	\$ 10	\$ 15	\$ 8,277

	Residential Real Estate	Commercial Real Estate	Construction	Home Equity	Commercial Business	Consumer	Unallocated	Total
	(In thousands)							
<b>Nine Months Ended September 30, 2014</b>								
<b>Originated</b>								
Beginning balance	\$ 1,310	\$ 3,616	\$ 1,032	\$ 190	\$ 2,225	\$ 9	\$ -	\$ 8,382
Charge-offs	-	-	-	-	-	(1 )	-	(1 )
Recoveries	-	-	-	-	-	424	-	424
Provisions	101	1,045	(141 )	1	166	(425 )	-	747
Ending balance	\$ 1,411	\$ 4,661	\$ 891	\$ 191	\$ 2,391	\$ 7	\$ -	\$ 9,552

<b>Acquired</b>								
Beginning balance	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -
Charge-offs	-	-	(100 )	-	-	-	-	(100 )
Recoveries	-	-	-	-	-	-	-	-
Provisions	-	-	100	-	-	-	-	100
Ending balance	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -

<b>Total</b>								
Beginning balance	\$ 1,310	\$ 3,616	\$ 1,032	\$ 190	\$ 2,225	\$ 9	\$ -	\$ 8,382
Charge-offs	-	-	(100 )	-	-	(1 )	-	(101 )
Recoveries	-	-	-	-	-	424	-	424
Provisions	101	1,045	(41 )	1	166	(425 )	-	847
Ending balance	\$ 1,411	\$ 4,661	\$ 891	\$ 191	\$ 2,391	\$ 7	\$ -	\$ 9,552

	Residential Real Estate	Commercial Real Estate	Construction	Home Equity	Commercial Business	Consumer	Unallocated	Total
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(In thousands)

Nine Months Ended  
September 30, 2013

Beginning balance	\$ 1,230	\$ 3,842	\$ 929	\$ 220	\$ 1,718	\$ 2	\$ -	\$ 7,941
Charge-offs	-	(166 )	-	-	-	(3 )	-	(169 )
Recoveries	-	-	-	-	-	16	-	16
Provisions	239	(85 )	(1 )	(8 )	334	(5 )	15	489
Ending balance	\$ 1,469	\$ 3,591	\$ 928	\$ 212	\$ 2,052	\$ 10	\$ 15	\$ 8,277

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Bankwell Financial Group, Inc.

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS – (Unaudited)

With respect to the originated portfolio, the allocation to each portfolio segment is not necessarily indicative of future losses in any particular portfolio segment and does not restrict the use of the allowance to absorb losses in other portfolio segments.

The following tables are a summary, by portfolio segment and impairment methodology, of the allowance for loan losses and related portfolio balances at September 30, 2014 and December 31, 2013:

	Originated Loans		Acquired Loans		Total	
	Portfolio	Allowance	Portfolio	Allowance	Portfolio	Allowance
	(In thousands)					
<b>September 30, 2014</b>						
Loans individually evaluated for impairment:						
Residential real estate	\$ 864	\$ -	\$ -	\$ -	\$ 864	\$ -
Commercial real estate	2,895	22	-	-	2,895	22
Construction	-	-	-	-	-	-
Home equity	94	-	-	-	94	-
Commercial business	1,977	17	631	-	2,608	17
Consumer	-	-	-	-	-	-
Subtotal	\$ 5,830	\$ 39	\$ 631	\$ -	\$ 6,461	\$ 39
Loans collectively evaluated for impairment:						
Residential real estate	\$ 166,498	\$ 1,411	\$ -	\$ -	\$ 166,498	\$ 1,411
Commercial real estate	391,109	4,639	6,911	-	398,020	4,639
Construction	52,387	891	893	-	53,280	891
Home equity	9,445	191	3,294	-	12,739	191
Commercial business	103,146	2,374	1,407	-	104,553	2,374
Consumer	190	7	343	-	533	7
Subtotal	\$ 722,775	\$ 9,513	\$ 12,848	\$ -	\$ 735,623	\$ 9,513
Unallocated Allowance	-	-	-	-	-	-
Total	\$ 728,605	\$ 9,552	\$ 13,479	\$ -	\$ 742,084	\$ 9,552

Bankwell Financial Group, Inc.

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS – (Unaudited)

	Originated Loans		Acquired Loans		Total	
	Portfolio	Allowance	Portfolio	Allowance	Portfolio	Allowance
	(In thousands)					
December 31, 2013						
Loans individually evaluated for impairment:						
Residential real estate	\$1,867	\$73	\$-	\$-	\$1,867	\$73
Commercial real estate	1,117	56	-	-	1,117	56
Construction	-	-	-	-	-	-
Home equity	97	4	-	-	97	4
Commercial business	642	12	-	-	642	12
Consumer	-	-	-	-	-	-
Subtotal	\$3,723	\$145	\$-	\$-	\$3,723	\$145
Loans collectively evaluated for impairment:						
Residential real estate	\$154,007	\$1,237	\$-	\$-	\$154,007	\$1,237
Commercial real estate	304,706	3,560	9,939	-	314,645	3,560
Construction	44,187	1,032	7,308	-	51,495	1,032
Home equity	9,528	187	3,872	-	13,400	187
Commercial business	91,531	2,212	2,374	-	93,905	2,212
Consumer	225	9	612	-	837	9
Subtotal	\$604,184	\$8,237	\$24,105	\$-	\$628,289	\$8,237
Total	\$607,907	\$8,382	\$24,105	\$-	\$632,012	\$8,382

Bankwell Financial Group, Inc.

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS – (Unaudited)

## Credit quality indicators

The Company's policies provide for the classification of loans into the following categories: pass, special mention, substandard, doubtful and loss. Consistent with regulatory guidelines, loans that are considered to be of lesser quality are classified as substandard, doubtful, or loss assets. A loan is considered substandard if it is inadequately protected by the current net worth and paying capacity of the obligor or of the collateral pledged, if any. Substandard loans include those loans characterized by the distinct possibility that the Company will sustain some loss if the deficiencies are not corrected. Loans classified as doubtful have all of the weaknesses inherent in those classified substandard with the added characteristic that the weaknesses present make collection or liquidation in full, on the basis of currently existing facts, conditions and values, highly questionable and improbable. Loans classified as loss are those considered uncollectible and of such little value that their continuance as loans is not warranted. Loans that do not expose the Company to risk sufficient to warrant classification in one of the aforementioned categories, but which possess potential weaknesses that deserve close attention, are designated as special mention.

Loans that are considered to be impaired are analyzed to determine whether a loss is possible and if so, a calculation is performed to determine the possible loss amount. If it is determined that the loss amount is \$0, no reserve is held against the asset. If a loss is calculated, then a specific reserve for that asset is determined.

The following tables are a summary of the loan portfolio quality indicators by portfolio segment at September 30, 2014 and December 31, 2013:

	Commercial Credit Quality Indicators					
	At September 30, 2014			At December 31, 2013		
	Commercial Real Estate	Construction	Commercial Business	Commercial Real Estate	Construction	Commercial Business
	(In thousands)					
<b>Originated loans:</b>						
Pass	\$ 387,877	\$ 52,387	\$ 99,354	\$ 304,469	\$ 44,187	\$ 91,093
Special mention	1,571	-	5,191	237	-	438
Substandard	4,556	-	578	1,117	-	642
Doubtful	-	-	-	-	-	-
Loss	-	-	-	-	-	-
<b>Total originated loans</b>	<b>394,004</b>	<b>52,387</b>	<b>105,123</b>	<b>305,823</b>	<b>44,187</b>	<b>92,173</b>
<b>Acquired loans:</b>						
Pass	5,878	-	1,138	9,580	4,639	1,806
Special mention	-	-	53	24	161	252
Substandard	1,033	893	847	335	2,508	316
Doubtful	-	-	-	-	-	-
Loss	-	-	-	-	-	-
<b>Total acquired loans</b>	<b>6,911</b>	<b>893</b>	<b>2,038</b>	<b>9,939</b>	<b>7,308</b>	<b>2,374</b>
<b>Total</b>	<b>\$ 400,915</b>	<b>\$ 53,280</b>	<b>\$ 107,161</b>	<b>\$ 315,762</b>	<b>\$ 51,495</b>	<b>\$ 94,547</b>





Bankwell Financial Group, Inc.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS – (Unaudited)

	Residential and Consumer Credit Quality Indicators					
	At September 30, 2014			At December 31, 2013		
	Residential		Consumer	Residential		Consumer
	Real Estate	Home Equity		Real Estate	Home Equity	
	(In thousands)					
<b>Originated loans:</b>						
Pass	\$ 166,498	\$ 9,372	\$ 190	\$ 153,443	\$ 9,447	\$ 225
Special mention	864	167	-	2,431	178	-
Substandard	-	-	-	-	-	-
Doubtful	-	-	-	-	-	-
Loss	-	-	-	-	-	-
<b>Total originated loans</b>	<b>167,362</b>	<b>9,539</b>	<b>190</b>	<b>155,874</b>	<b>9,625</b>	<b>225</b>
<b>Acquired loans:</b>						
Pass	-	3,294	343	-	3,826	469
Special mention	-	-	-	-	-	143
Substandard	-	-	-	-	46	-
Doubtful	-	-	-	-	-	-
Loss	-	-	-	-	-	-
<b>Total acquired loans</b>	<b>-</b>	<b>3,294</b>	<b>343</b>	<b>-</b>	<b>3,872</b>	<b>612</b>
<b>Total</b>	<b>\$ 167,362</b>	<b>\$ 12,833</b>	<b>\$ 533</b>	<b>\$ 155,874</b>	<b>\$ 13,497</b>	<b>\$ 837</b>

## Loan portfolio aging analysis

When a loan is 15 days past due, the Company sends the borrower a late notice. The Company also contacts the borrower by phone if the delinquency is not corrected promptly after the notice has been sent. When the loan is 30 days past due, the Company mails the borrower a letter reminding the borrower of the delinquency, and attempts to contact the borrower personally to determine the reason for the delinquency and ensure the borrower understands the terms of the loan. If necessary, subsequent delinquency notices are issued and the account will be monitored on a regular basis thereafter. By the 90th day of delinquency, the Company will send the borrower a final demand for payment and may recommend foreclosure. A summary report of all loans 30 days or more past due is provided to the board of directors of the Company each month. Loans greater than 90 days past due are generally put on nonaccrual status. A nonaccrual loan is restored to accrual status when it is no longer delinquent and collectability of interest and principal is no longer in doubt. A loan is considered to be no longer delinquent when timely payments are made for a period of at least six months (one year for loans providing for quarterly or semi-annual payments) by the borrower in accordance with the contractual terms.

Bankwell Financial Group, Inc.

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS – (Unaudited)

The following tables set forth certain information with respect to our loan portfolio delinquencies by portfolio segment and amount as of September 30, 2014 and December 31, 2013:

As of September 30, 2014

	31-60 Days Past Due	61-90 Days Past Due	Greater Than 90 Days (In thousands)	Total Past Due	Current	Carrying Amount > 90 Days and Accruing
<b>Originated Loans</b>						
Real estate loans:						
Residential real estate	\$-	\$-	\$-	\$-	\$167,362	\$-
Commercial real estate	-	-	1,102	1,102	392,902	-
Construction	-	-	-	-	52,387	-
Home equity	-	-	-	-	9,539	-
Commercial business	-	-	-	-	105,123	-
Consumer	-	1	-	1	189	-
<b>Total originated loans</b>	<b>-</b>	<b>1</b>	<b>1,102</b>	<b>1,103</b>	<b>727,502</b>	<b>-</b>
<b>Acquired Loans</b>						
Real estate loans:						
Residential real estate	-	-	-	-	-	-
Commercial real estate	-	-	416	416	6,495	416
Construction	-	-	893	893	-	893
Home equity	-	-	-	-	3,294	-
Commercial business	-	-	-	-	2,038	-
Consumer	1	-	-	1	342	-
<b>Total acquired loans</b>	<b>1</b>	<b>-</b>	<b>1,309</b>	<b>1,310</b>	<b>12,169</b>	<b>1,309</b>
<b>Total loans</b>	<b>\$1</b>	<b>\$1</b>	<b>\$2,411</b>	<b>\$2,413</b>	<b>\$739,671</b>	<b>\$1,309</b>

As of December 31, 2013

	31-60 Days Past Due	61-90 Days Past Due	Greater Than 90 Days	Total Past Due	Current	Carrying Amount > 90 Days and Accruing
<b>Originated Loans</b>						
Real estate loans:						
Residential real estate	\$-	\$-	\$1,003	\$1,003	\$154,871	\$-
Commercial real estate	-	-	-	-	305,823	-
Construction	-	-	-	-	44,187	-

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Home equity	-	-	-	-	9,625	-
Commercial business	-	-	-	-	92,173	-
Consumer	-	-	-	-	225	-
Total originated loans	-	-	1,003	1,003	606,904	-
Acquired Loans						
Real estate loans:						
Residential real estate	-	-	-	-	-	-
Commercial real estate	-	-	797	797	9,142	797
Construction	-	-	2,508	2,508	4,800	2,508
Home equity	-	-	-	-	3,872	-
Commercial business	-	-	315	315	2,059	315
Consumer	-	-	-	-	612	-
Total acquired loans	-	-	3,620	3,620	20,485	3,620
Total loans	\$-	\$-	\$4,623	\$4,623	\$627,389	\$3,620

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Bankwell Financial Group, Inc.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS – (Unaudited)

Loans on nonaccrual status

The following is a summary of nonaccrual loans by portfolio segment as of September 30, 2014 and December 31, 2013:

	September 30, 2014	December 31, 2013
	(In thousands)	
Residential real estate	\$-	\$1,003
Commercial real estate	1,246	-
<b>Total</b>	<b>\$1,246</b>	<b>\$1,003</b>

The amount of income that was contractually due but not recognized on originated nonaccrual loans totaled \$51 thousand, and \$67 thousand, respectively for the nine months ended September 30, 2014, and 2013. The amount of income that was contractually due but not recognized on originated nonaccrual loans totaled \$18 thousand, and \$27 thousand, respectively for the three months ended September 30, 2014 and 2013. There was \$4 thousand and \$8 thousand actual interest income recognized on these loans for the nine months ended September 30, 2014, and 2013.

At September 30, 2014 and December 31, 2013, there were no commitments to lend additional funds to any borrower on nonaccrual status.

The preceding table excludes acquired loans that are accounted for as purchased credit impaired loans totaling \$1.9 million and \$6.2 million, respectively at September 30, 2014 and December 31, 2013. Such loans otherwise meet the Company's definition of a nonperforming loan but are excluded because the loans are included in loan pools that are considered performing. The discounts arising from recording these loans at fair value were due, in part, to credit quality. The acquired loans are accounted for on either a pool or individual basis and the accretable yield is being recognized as interest income over the life of the loans based on expected cash flows.

Impaired loans

An impaired loan generally is one for which it is probable, based on current information, the Company will not collect all the amounts due under the contractual terms of the loan. Loans are individually evaluated for impairment. When the Company classifies a problem loan as impaired, it provides a specific valuation allowance for that portion of the asset that is deemed uncollectible.

Bankwell Financial Group, Inc.

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS – (Unaudited)

The following table summarizes impaired loans by portfolio segment as of September 30, 2014 and December 31, 2013:

	Carrying Amount		Unpaid Principal Balance		Associated Allowance	
	September 30, 2014	December 31, 2013	September 30, 2014	December 31, 2013	September 30, 2014	December 31, 2013
(In thousands)						
<b>Originated</b>						
Impaired loans without a valuation allowance:						
Residential real estate	\$864	\$-	\$864	\$-	\$-	\$-
Commercial real estate	2,440	-	2,455	-	-	-
Home equity	94	-	94	-	-	-
Commercial business	1,344	-	1,350	-	-	-
Total impaired loans without a valuation allowance	\$4,742	\$-	\$4,763	\$-	\$-	\$-
Impaired loans with a valuation allowance:						
Residential real estate	\$-	\$1,867	\$-	\$1,880	\$-	\$73
Commercial real estate	455	1,117	455	1,117	22	56
Home equity	-	97	-	97	-	4
Commercial business	633	642	633	642	17	12
Total impaired loans with a valuation allowance	\$1,088	\$3,723	\$1,088	\$3,736	\$39	\$145
Total originated impaired loans	\$5,830	\$3,723	\$5,851	\$3,736	\$39	\$145
<b>Acquired</b>						
Impaired loans without a valuation allowance:						
Commercial business	\$631	\$-	\$631	\$-	\$-	\$-
Total impaired loans without a valuation allowance	\$631	\$-	\$631	\$-	\$-	\$-
Total acquired impaired loans	\$631	\$-	\$631	\$-	\$-	\$-

The following table summarizes the average recorded investment balance of impaired loans and interest income recognized on impaired loans by portfolio segment for the nine months ended September 30, 2014 and 2013:

Nine months ended September 30,	Average Recorded Investment		Interest Income Recognized	
	2014	2013	2014	2013
(In thousands)				
<b>Originated</b>				
Impaired loans without a valuation allowance:				

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Residential real estate	\$864	\$-	\$21	\$-
Commercial real estate	1,714	-	21	-
Home equity	96	-	2	-
Commercial business	1,434	-	48	-
Total impaired loans without a valuation allowance	\$4,108	\$-	\$92	\$-
Impaired loans with a valuation allowance:				
Residential real estate	\$-	\$1,900	\$-	\$29
Commercial real estate	459	1,131	24	38
Home equity	665	246	-	6
Commercial business	-	690	27	28
Total impaired loans with a valuation allowance	\$1,124	\$3,967	\$51	\$101
Total originated impaired loans	\$5,232	\$3,967	\$143	\$101
Acquired				
Impaired loans without a valuation allowance:				
Commercial business	\$599	\$-	\$20	\$-
Total impaired loans without a valuation allowance	\$599	\$-	\$20	\$-
Total acquired impaired loans	\$599	\$-	\$20	\$-

Bankwell Financial Group, Inc.

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS – (Unaudited)

## Troubled debt restructurings (TDRs)

Modifications to a loan are considered to be a troubled debt restructuring when one or both of the following conditions is met: 1) the borrower is experiencing financial difficulties and/or 2) the modification constitutes a concession that is not in line with market rates and/or terms. Modified terms are dependent upon the financial position and needs of the individual borrower. Trouble debt restructurings are classified as impaired loans. If a performing loan is restructured into a TDR it remains in performing status.

If a nonperforming loan is restructured into a TDR, it continues to be carried in nonaccrual status. Nonaccrual classification may be removed if the borrower demonstrates compliance with the modified terms for a minimum of six months. Troubled debt restructured loans are reported as such for at least one year from the date of restructuring. In years after the restructuring, troubled debt restructured loans are removed from this classification if the restructuring agreement specifies a market rate of interest equal to that which would be provided to a borrower with similar credit at the time of restructuring and the loan is not deemed to be impaired based on the modified terms.

The recorded investment in TDRs was \$2.1 million at September 30, 2014 and \$1.6 million at December 31, 2013.

The following table presents loans whose terms were modified as TDRs during the periods presented:

(Dollars in thousands)	Number of Loans		Outstanding Recorded Investment			
	2014	2013	Pre-Modification		Post-Modification	
	2014	2013	2014	2013	2014	2013
Three months ended September 30,						
Commercial business	1	-	\$241	\$-	\$241	\$-
Total	1	-	\$241	\$-	\$241	\$-

(Dollars in thousands)	Number of Loans		Outstanding Recorded Investment			
	2014	2013	Pre-Modification		Post-Modification	
	2014	2013	2014	2013	2014	2013
Nine months ended September 30,						
Commercial real estate	2	-	\$ 1,324	\$-	\$1,324	\$-
Home equity	-	1	-	94	-	94
Commercial business	4	-	796	-	796	-
Total	6	1	\$ 2,120	\$94	\$2,120	\$94

All TDRs at September 30, 2014 and December 31, 2013 were performing in compliance under their modified terms.

Bankwell Financial Group, Inc.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS – (Unaudited)

The following table provides information on how loans were modified as a TDR during the three and nine months ended September 30, 2014 and 2013.

Periods ended September 30,	Three months		Nine months	
	2014	2013	2014	2013
	(In thousands)			
Maturity/amortization concession	\$241	\$-	\$962	\$94
Payment concession	\$-	\$-	\$1,158	\$-
Total	\$241	\$-	\$2,120	\$94

There was \$1.1 million and no loans modified in a troubled debt restructuring, for which there was a payment default during the three or nine months ended September 30, 2014 and 2013, respectively.



Bankwell Financial Group, Inc.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS – (Unaudited)

#### 4. Shareholders' Equity

##### Common stock

On May 15, 2014, the Company priced 2,702,703 common shares in its initial public offering ("IPO") at \$18.00 per share, and on May 15, 2014, Bankwell common shares began trading on the Nasdaq Stock Market. The Company issued a total of 2,702,703 common shares in its IPO, which closed on May 20, 2014. The net proceeds from the IPO were approximately \$44.7 million, after deducting the underwriting discount of approximately \$2.5 million and approximately \$1.3 million of expenses.

Between 2007 and 2013, four private placements for the sale of common stock were completed for the purpose of capitalizing the Company and allowing for continued growth. The private placement offerings were in addition to the initial and secondary offerings completed in 2002 and 2007, respectively. A total of 3,429,623 shares were issued and net proceeds of \$47.8 million were received in connection with these offerings.

##### Preferred stock

In 2011, the Company elected to participate in the U.S. Treasury's Small Business Lending Fund Program ("SBLF"). The SBLF is a \$30 billion fund established under the Small Business Jobs Act of 2010 to encourage lending to small businesses by providing Tier 1 capital to qualified community banks with assets of less than \$10 billion. The SBLF is intended to expand the ability to lend to small businesses, in order to help stimulate the economy and promote job growth. The transaction resulted in net capital proceeds to the Company of \$5.9 million, of which at least 90% was invested in the Banks as Tier 1 Capital.

The Series C Preferred stock pays noncumulative dividends. The dividend rate on the Series C Preferred Stock for the initial ten quarterly dividend periods, commencing with the period ended September 30, 2011 and ending with the period ended December 31, 2013, was determined each quarter based on the increase in the Banks' Qualified Small Business Lending over a baseline amount. The Company has paid dividends at a rate of 1.0% since issuance. For the eleventh quarterly dividend payment through four and one-half years after its issuance, the dividend rate on the Series C Preferred Stock will be fixed at the rate in effect at the end of the ninth quarterly dividend period, which is 1.0%. In the second quarter of 2016, four and one-half years from its issuance, the dividend rate will be fixed at 9.0% per annum.

The Series C Preferred Stock has no maturity date and ranks senior to the Company's common stock with respect to the payment of dividends and distributions and amounts payable upon liquidation, dissolution and winding up of the Company. The Series C Preferred Stock is non-voting, other than voting rights on matters that could adversely affect the Series C Preferred Stock, and is redeemable at any time by the Company, subject to the approval of its federal banking regulator. The redemption price is the aggregate liquidation preference of the SBLF Preferred Stock plus accrued but unpaid dividends and pro rata portion of any lending incentive fee. All redemptions must be in an amount at least equal to 25% of the number of originally issued shares of SBLF Preferred Stock, or 100% of the then-outstanding shares if less than 25% of the number of shares originally issued. In connection with the IPO, the U.S. Treasury exercised its piggyback registration rights under the SBLF and the Series C Preferred Stock held by the U.S. Treasury was registered under the Securities Act of 1933, as amended.

Warrants

The initial and secondary offerings completed in 2002 and 2007 each call for the issuance of Units. Each Unit issued pursuant to these two offerings represented one share of common stock and one non-transferable Warrant. The Warrants were exercisable at any time from and including October 1, 2009 and prior to or on November 30, 2009, unless extended or accelerated by the board of directors in their discretion. The board of directors has extended the exercise period to October 1, 2015 through December 1, 2015. Each Warrant allows a holder to purchase 3221 shares of common stock at an exercise price of \$14.00 per share. None of the Warrants have been exercised as of September 30, 2014. Assuming that all of the Warrants issued are exercised in full during the exercise period, the Company would receive \$4.3 million in gross capital and issue 304,640 shares of common stock.

Bankwell Financial Group, Inc.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS – (Unaudited)

Dividends

The Company's shareholders are entitled to dividends when and if declared by the board of directors, out of funds legally available. The ability of the Company to pay dividends depends, in part, on the ability of the Bank to pay dividends to the Company. In accordance with Connecticut statutes, regulatory approval is required to pay dividends in excess of the Bank's profits retained in the current year plus retained profits from the previous two years. The bank is also prohibited from paying dividends that would reduce its capital ratios below minimum regulatory requirements.

The payment of dividends is subject to additional restrictions in connection with the SBLF preferred stock.

For the nine months ended September 30, 2014 and 2013, the Company declared and paid cash dividends on preferred stock of \$82 thousand and \$84 thousand, respectively. To date, the Company has not declared or paid dividends on its common stock, nor has it repurchased any of its common stock.

5. Comprehensive Income

Comprehensive income represents the sum of net income and items of other comprehensive income or loss, including net unrealized gains or losses on securities available for sale and net gains or losses on derivatives accounted for as cash flow hedges. The Company's total comprehensive income or loss for the three and nine months ended September 30, 2014 and 2013 is reported in the Consolidated Statements of Comprehensive Income.

The following table presents the changes in accumulated other comprehensive income (loss) by component, net of tax for the three and nine months ended September 30, 2014 and 2013:

	Net Unrealized Gain (Loss) on Available for Sale Securities (In thousands)	Net Unrealized Gain (Loss) on Interest Rate Swap	Total
Balance at June 30, 2014	\$ 689	\$ (66 )	\$ 623
Other comprehensive income (loss) before reclassifications	(154 )	133	(21 )
Amounts reclassified from accumulated other comprehensive income	-	-	-
Net other comprehensive income (loss)	(154 )	133	(21 )
Balance at September 30, 2014	\$ 535	\$ 67	\$ 602

	Net Unrealized Gain (Loss) on Available	Net Unrealized Gain (Loss) on Interest Rate Swap	Total
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	for Sale Securities (In thousands)		
Balance at December 31, 2013	\$ 424	\$ -	\$ 424
Other comprehensive income (loss) before reclassifications	110	68	178
Amounts reclassified from accumulated other comprehensive income	-	-	-
Net other comprehensive income (loss)	110	68	178
Balance at September 30, 2014	\$ 534	\$ 68	\$ 602

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Bankwell Financial Group, Inc.

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS – (Unaudited)

	Net Unrealized Gain (Loss) on Available for Sale Securities (In thousands)
Balance at June 30, 2013	\$ 561
Other comprehensive loss before reclassifications	(8 )
Amounts reclassified from accumulated other comprehensive income	-
Net other comprehensive loss	(8 )
Balance at September 30, 2013	\$ 553

	Net Unrealized Gain (Loss) on Available for Sale Securities (In thousands)
Balance at December 31, 2012	\$ 1,511
Other comprehensive loss before reclassifications	(958 )
Amounts reclassified from accumulated other comprehensive income	-
Net other comprehensive loss	(958 )
Balance at September 30, 2013	\$ 553

## 6. Earnings per share

Basic earnings per share (“EPS”) is computed by dividing income available to common shareholders by the weighted-average number of shares of common stock outstanding for the period. Diluted EPS reflects the potential dilution that could occur if securities or other contracts to issue common stock (such as stock options) were exercised or converted into common stock or resulted in the issuance of common stock that then shared in earnings. Unvested share-based payment awards, which include the right to receive non-forfeitable dividends, are considered to participate with common stock in undistributed earnings for purposes of computing EPS.

The Company’s unvested restricted stock awards are participating securities, and therefore, are included in the computation of both basic and diluted earnings per common share. EPS is calculated using the two-class method, under which calculations (1) exclude from the numerator any dividends paid or owed on participating securities and any undistributed earnings considered to be attributable to participating securities and (2) exclude from the denominator the dilutive impact of the participating securities.

Bankwell Financial Group, Inc.

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS – (Unaudited)

The following is a reconciliation of earnings available to common shareholders and basic weighted-average common shares outstanding to diluted weighted average common shares outstanding, reflecting the application of the two-class method:

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2014	2013	2014	2013
	(In thousands, except per share data)			
Net income	\$1,491	\$1,319	\$3,841	\$3,799
Preferred stock dividends	(27)	(29)	(82)	(84)
Dividends and undistributed earnings allocated to participating securities	(23)	(19)	(82)	(55)
Net income available to common shareholders	\$1,441	\$1,271	\$3,677	\$3,660
Weighted average shares outstanding, basic	6,483	3,355	5,099	3,278
Effect of dilutive equity-based awards	19	58	25	60
Weighted average shares outstanding, diluted	6,502	3,413	5,124	3,338
Net earnings per common share:				
Basic earnings per common share	\$0.22	\$0.38	\$0.72	\$1.12
Diluted earnings per common share	0.22	0.37	0.72	1.10

## 7. Regulatory Matters

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

Quantitative measures established by regulation to ensure capital adequacy require the Bank and Company to maintain minimum amounts and ratios of total and Tier I capital to risk-weighted assets and of Tier I capital to average assets, as defined by regulation. Management believes, as of September 30, 2014, the Bank and Company meet all capital adequacy requirements to which they are subject. As of September 30, 2014, the Bank was well capitalized under the regulatory framework for prompt corrective action, as shown in the following schedules. There are no conditions or events since then that management believes have changed this category.

Bankwell Financial Group, Inc.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS – (Unaudited)

The capital amounts and ratios for the Bank and Company at September 30, 2014 and December 31, 2013, were as follows:

(Dollars in thousands)	Actual Capital		For Capital Adequacy Purposes		To be Well Capitalized Under Prompt Corrective Action Provisions	
	Amount	Ratio	Amount	Ratio	Amount	Ratio
<b>Bankwell Bank</b>						
<b>September 30, 2014</b>						
Total Capital to Risk-Weighted Assets	\$ 112,989	15.27 %	\$ 59,199	8.00 %	\$ 73,999	10.00 %
Tier I Capital to Risk-Weighted Assets	103,735	14.02 %	29,599	4.00 %	44,399	6.00 %
Tier I Capital to Average Assets	103,735	11.93 %	34,793	4.00 %	43,491	5.00 %
<b>Bankwell Financial Group, Inc.</b>						
<b>September 30, 2014</b>						
Total Capital to Risk-Weighted Assets	\$ 126,846	16.96 %	\$ 59,829	8.00 %	N/A	N/A
Tier I Capital to Risk-Weighted Assets	117,495	15.71 %	29,914	4.00 %	N/A	N/A
Tier I Capital to Average Assets	117,495	13.38 %	35,131	4.00 %	N/A	N/A
<b>Bankwell Bank</b>						
<b>December 31, 2013</b>						
Total Capital to Risk-Weighted Assets	\$ 66,674	10.74 %	\$ 49,682	8.00 %	\$ 62,103	10.00 %
Tier I Capital to Risk-Weighted Assets	58,908	9.49 %	24,841	4.00 %	37,262	6.00 %
Tier I Capital to Average Assets	58,908	7.91 %	29,772	4.00 %	37,215	5.00 %
<b>Bankwell Financial Group, Inc.</b>						
<b>December 31, 2013</b>						
Total Capital to Risk-Weighted Assets	\$ 76,537	12.32 %	\$ 49,683	8.00 %	N/A	N/A
Tier I Capital to Risk-Weighted Assets	68,766	11.07 %	24,841	4.00 %	N/A	N/A
Tier I Capital to Average Assets	68,766	9.15 %	30,068	4.00 %	N/A	N/A

Tier I Capital to Average  
Assets

Restrictions on dividends

The ability of the Company to pay dividends depends, in part, on the ability of the Bank to pay dividends to the Company. In accordance with Connecticut statutes, regulatory approval is required to pay dividends in excess of the Bank's profits retained in the current year plus retained profits from the previous two years. The Bank is also prohibited from paying dividends that would reduce its capital ratios below minimum regulatory requirements.

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Bankwell Financial Group, Inc.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS – (Unaudited)

## 8. Stock-Based Compensation

## Equity award plans

The Company has five equity award plans, which are collectively referred to as the “Plan.” The current plan under which any future issuances of equity awards will be made is the 2012 BNC Financial Group, Inc. Stock Plan, or the “2012 Plan,” amended on June 26, 2013. All equity awards made under the 2012 Plan are made by means of an award agreement, which contains the specific terms and conditions of the grant. To date, all equity awards have been in the form of share options or restricted stock. At September 30, 2014, there were 448,885 shares reserved for future issuance under the 2012 Plan.

**Share Options:** The Company accounts for stock options based on the fair value at the date of grant over the vesting period of such awards on a straight line basis. For the nine months ended September 30, 2014 and 2013, the Company recorded expense related to options granted under the various plans of approximately \$24 thousand and \$62 thousand, respectively.

There were no options granted during the nine months ended September 30, 2014.

A summary of the status of outstanding stock options as of and for the nine months ended September 30, 2014 is presented below:

	Nine Months Ended September 30, 2014	
	Number of Shares	Weighted Average Exercise Price
Options outstanding at beginning of period	208,568	\$ 16.67
Granted	-	-
Forfeited	(4,270 )	18.32
Exercised	(20,305 )	10.17
Expired	(480 )	10.00
Options outstanding at end of period	183,513	17.37
Options exercisable at end of period	172,152	17.51
Weighted-average fair value of options granted during the period		N/A

Intrinsic value is the amount by which the fair value of the underlying stock exceeds the exercise price of an option on the exercise date. The total intrinsic value of share options exercised during the nine months ended September 30, 2014 was \$214 thousand.

**Restricted Stock:** Restricted stock provides grantees with rights to shares of common stock upon completion of a service period and certain performance goals. Shares of unvested restricted stock are considered participating securities. Restricted stock awards generally vest over one to five years.



Bankwell Financial Group, Inc.

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS – (Unaudited)

The following table presents the activity for restricted stock for the nine months ended September 30, 2014:

	Nine Months Ended September 30, 2014	
	Number of Shares	Weighted Average Grant Date Fair Value
Unvested at beginning of period	122,140	\$ 15.98
Granted	10,510	17.12
Vested	(6,456 )	14.66
Forfeited	(49,916 )	15.89
Unvested at end of period	76,278	16.31

The Company's restricted stock expense for the nine months ended September 30, 2014 and 2013 was \$141 thousand and \$143 thousand, respectively.

#### 9. Derivative Instruments

The Company entered into a derivative transaction in February, 2014. Information about derivative instruments at September 30, 2014 is as follows:

(Dollars in thousands)	Notional Amount	Maturity	Received	Paid	Fair Value
<b>Cash flow hedge:</b>					
Interest rate swap on FHLB advance	\$25,000	4.7 years	0.23%	1.62%	\$111

The effective portion of unrealized changes in the fair value of derivatives accounted for as cash flow hedges is reported in other comprehensive income and subsequently reclassified to earnings in the same period or periods during which the hedged forecasted transaction affects earnings. The Bank assesses the effectiveness of each hedging relationship by comparing the changes in cash flows of the derivative hedging instrument with the changes in cash flows of the designated hedged item or transaction. The ineffective portion of changes in the fair value of the derivatives is recognized directly in earnings.

The Bank's cash flow hedge positions are all forward starting interest rate swap transactions. As of February 6, 2014 the Bank entered into the following forward starting interest rate swap transactions:

(Dollars in thousands)	Notional Amount	Effective Date of Hedged Borrowing	Duration of Borrowing	Counterparty
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Type of borrowing:

FHLB 90-day advance	\$25,000	April 1, 2014	4.7 years	Bank of Montreal
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This hedge strategy converts the LIBOR based rate of interest on certain FHLB advances to fixed interest rates, thereby protecting the Bank from floating interest rate variability.

Bankwell Financial Group, Inc.

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS – (Unaudited)

Changes in the consolidated statements of comprehensive income related to interest rate derivatives designated as hedges of cash flows were as follows for the three and nine months ended September 30, 2014:

(In thousands)	Three Months Ended September 30, 2014	Nine Months Ended September 30, 2014
<b>Interest rate swap on FHLB advance:</b>		
Unrealized loss recognized in accumulated other comprehensive income	\$ 218	\$ 111
Income tax benefit on items recognized in accumulated other comprehensive income	(85 )	(43 )
Other comprehensive income	\$ 133	\$ 68
Interest expense recognized on hedged FHLB advance	\$ 88	\$ 176

## 10. Fair Value of Financial Instruments

GAAP requires disclosure of fair value information about financial instruments, whether or not recognized in the statements of condition, for which it is practicable to estimate that value. In cases where quoted market prices are not available, fair values are based on estimates using present value or other valuation techniques. Those techniques are significantly affected by the assumptions used, including the discount rates and estimates of future cash flows. In that regard, the derived fair value estimates cannot be substantiated by comparisons to independent markets and, in many cases, could not be realized in immediate settlement of the instrument.

Management uses its best judgment in estimating the fair value of the Company's financial instruments; however, there are inherent weaknesses in any estimation technique. Therefore, for substantially all financial instruments, the fair value estimates presented herein are not necessarily indicative of the amounts the Company could have realized in a sales transaction at either September 30, 2014 or December 31, 2013. The estimated fair value amounts have been measured as of the respective period-ends, and have not been reevaluated or updated for purposes of these consolidated financial statements subsequent to those respective dates. As such, the estimated fair values of these financial instruments subsequent to the respective reporting dates may be different than the amounts reported at each period-end.

Bankwell Financial Group, Inc.

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS – (Unaudited)

The carrying values, fair values and placement in the fair value hierarchy of the Company's financial instruments at September 30, 2014 and December 31, 2013 were as follows:

	September 30, 2014				
	Carrying Value	Fair Value	Level 1	Level 2	Level 3
	(In thousands)				
<b>Financial Assets:</b>					
Cash and due from banks	\$35,566	\$35,566	\$35,566	\$-	\$-
Available for sale securities	67,537	67,537	-	67,537	-
Held to maturity securities	11,502	11,539	-	11,539	-
Loans held for sale	-	-	-	-	-
Loans receivable, net	730,148	731,394	-	-	731,394
Accrued interest receivable	2,670	2,670	-	-	2,670
FHLB stock	4,834	4,834	-	-	4,834
Derivative Asset	111	111	-	111	-
<b>Financial Liabilities:</b>					
Demand deposits	151,146	151,146	-	-	151,146
NOW and money market	233,994	233,994	-	-	233,994
Savings	74,556	74,556	-	-	74,556
Time deposits	235,567	236,834	-	-	236,834
Advances from the FHLB	77,000	76,780	-	-	76,780
<b>December 31, 2013</b>					
	Carrying Value	Fair Value	Level 1	Level 2	Level 3
	(In thousands)				
<b>Financial Assets:</b>					
Cash and due from banks	\$82,013	\$82,013	\$82,013	\$-	\$-
Available for sale securities	28,597	28,597	-	28,597	-
Held to maturity securities	13,816	13,815	-	13,815	-
Loans held for sale	100	100	-	100	-
Loans receivable, net	621,830	623,876	-	-	623,876
Accrued interest receivable	2,360	2,360	-	-	2,360
FHLB stock	4,834	4,834	-	-	4,834
<b>Financial Liabilities:</b>					
Demand deposits	118,618	118,618	-	-	118,618
NOW and money market	238,231	238,231	-	-	238,231
Savings	107,692	107,692	-	-	107,692
Time deposits	197,004	197,762	-	-	197,762
Advances from the FHLB	44,000	43,902	-	-	43,902

The following methods and assumptions were used by management in estimating the fair value of its financial instruments:

Cash and due from banks and accrued interest receivable: The carrying amount is a reasonable estimate of fair value.

Bankwell Financial Group, Inc.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS – (Unaudited)

Investment securities: Fair values are based on quoted market prices or dealer quotes, if available. If a quoted market price is not available, fair value is estimated using quoted market prices for similar securities.

FHLB stock: The carrying value of FHLB stock approximates fair value based on the most recent redemption provisions of the FHLB.

Loans held for sale: The fair value is based upon prevailing market prices.

Loans receivable: For variable rate loans which reprice frequently and have no significant change in credit risk, fair values are based on carrying values. The fair value of fixed rate loans are estimated by discounting the future cash flows using the year end rates at which similar loans would be made to borrowers with similar credit ratings and for the same remaining maturities.

Derivative asset (liability): The valuation of the Company's interest rate swap is obtained from a third-party pricing service and is determined using a discounted cash flow analysis on the expected cash flows of each derivative. The pricing analysis is based on observable inputs for the contractual terms of the derivatives, including the period to maturity and interest rate curves.

Deposits: The fair value of demand deposits, regular savings and certain money market deposits is the amount payable on demand at the reporting date. The fair value of certificates of deposit and other time deposits is estimated using a discounted cash flow calculation that applies interest rates currently being offered for deposits of similar remaining maturities to a schedule of aggregated expected maturities on such deposits.

Advances from the FHLB: The fair value of the advances is estimated using a discounted cash flow calculation that applies current FHLB interest rates for advances of similar maturity to a schedule of maturities of such advances.

## 11. Fair Value Measurements

The Company is required to account for certain assets and liabilities at fair value on a recurring or non-recurring basis. As discussed in Note 1, the Company determines fair value in accordance with GAAP, which defines fair value and establishes a framework for measuring fair value. Fair value is defined as the exchange price that would be received for an asset or paid to transfer a liability (exit price) in the principal or most advantageous market for the asset or liability in an orderly transaction between market participants on the measurement date. GAAP establishes a fair value hierarchy which requires an entity to maximize the use of observable inputs and minimize the use of unobservable inputs when measuring fair value. The standard describes three levels of inputs that may be used to measure fair values:

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

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



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

Valuation techniques based on unobservable inputs are highly subjective and require judgments regarding significant matters such as the amount and timing of future cash flows and the selection of discount rates that may appropriately reflect market and credit risks. Changes in these judgments often have a material impact on the fair value estimates. In addition, since these estimates are as of a specific point in time they are susceptible to material near-term changes.

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Bankwell Financial Group, Inc.

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS – (Unaudited)

## Financial instruments measured at fair value on a recurring basis

The following tables detail the financial instruments carried at fair value on a recurring basis at September 30, 2014 and December 31, 2013, and indicates the fair value hierarchy of the valuation techniques utilized by the Company to determine the fair value. The Company had no transfers into or out of Levels 1, 2 or 3 during the nine months ended September 30, 2014 and the year ended December 31, 2013.

	Fair Value		
	Level 1	Level 2	Level 3
		(In thousands)	
<b>September 30, 2014:</b>			
Available-for-sale investment securities:			
U.S. Government and agency obligations	\$-	\$33,735	\$-
State agency and municipal obligations	-	17,301	-
Corporate bonds	-	15,597	-
Mortgage backed securities	-	904	-
Derivative asset	-	111	-
<b>December 31, 2013:</b>			
Available-for-sale investment securities:			
U.S. Government and agency obligations	\$-	\$5,688	\$-
State agency and municipal obligations	-	12,132	-
Corporate bonds	-	9,566	-
Mortgage backed securities	-	1,211	-

Available for sale investment securities: The fair value of the Company's investment securities are estimated by using pricing models or quoted prices of securities with similar characteristics (i.e. matrix pricing) and are classified within Level 2 of the valuation hierarchy.

*Derivative asset:* The Company's derivative asset is an interest rate swap, initiated in February 2014 as part of management's strategy to manage interest rate risk. The valuation of the Company's interest rate swap is obtained from a third-party pricing service and is determined using a discounted cash flow analysis on the expected cash flows of each derivative. The pricing analysis is based on observable inputs for the contractual terms of the derivatives, including the period to maturity and interest rate curves. The Company has determined that the majority of the inputs used to value its interest rate derivatives fall within Level 2 of the fair value hierarchy.

## Financial instruments measured at fair value on a nonrecurring basis

Certain assets are measured at fair value on a non-recurring basis in accordance with GAAP. These include assets that are measured at the-lower-of-cost-or-market that were recognized at fair value below cost at the end of the period as well as assets that are not measured at fair value on an ongoing basis but are subject to fair value adjustments in certain circumstances, such as when there is evidence of impairment.



Bankwell Financial Group, Inc.

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS – (Unaudited)

The following table details the financial instruments carried at fair value on a nonrecurring basis at September 30, 2014 and December 31, 2013, and indicates the fair value hierarchy of the valuation techniques utilized by the Company to determine the fair value:

	Level 1	Fair Value Level 2 (In thousands)	Level 3
<b>September 30, 2014:</b>			
Impaired loans	\$-	\$-	\$6,461
Foreclosed real estate	-	-	829
<b>December 31, 2013:</b>			
Impaired loans	\$-	\$-	\$3,723
Foreclosed real estate	-	-	829

The following table presents information about quantitative inputs and assumptions for Level 3 financial instruments carried at fair value on a nonrecurring basis at September 30, 2014 and December 31, 2013:

(Dollars in thousands)	Fair Value	Valuation Methodology	Unobservable Input	Range (Weighted Average)
<b>September 30, 2014:</b>				
Impaired loans	\$6,461	Appraisals	Discount for dated appraisals	0%
		Discounted cash flows	Discount rate	3.25% to 7.0%
Foreclosed real estate	\$829	Appraisals	Discount for dated appraisals	34.8% to 66.6%
<b>December 31, 2013:</b>				
Impaired loans	\$3,723	Appraisals	Discount for dated appraisals	0% to 20.0%
		Discounted cash flows	Discount rate	6.0%
Foreclosed real estate	\$829	Appraisals	Discount for dated appraisals	34.8% to 66.6%

Impaired loans: Loans are generally not recorded at fair value on a recurring basis. Periodically, the Company records nonrecurring adjustments to the carrying value of loans based on fair value measurements for partial charge-offs of the uncollectible portions of those loans. Nonrecurring adjustments also include certain impairment amounts for collateral-dependent loans calculated in accordance with ASC 310-10 when establishing the allowance for credit losses. Such amounts are generally based on the fair value of the underlying collateral supporting the loan. Collateral is typically valued using appraisals or other indications of value based on recent comparable sales of similar properties

or other assumptions. Estimates of fair value based on collateral are generally based on assumptions not observable in the marketplace and therefore such valuations have been classified as Level 3. For those loans where the primary source of repayment is cash flow from operations, adjustments include impairment amounts calculated based on the perceived collectability of interest payments on the basis of a discounted cash flow analysis utilizing a discount rate equivalent to the original note rate.

Foreclosed real estate: The Company classifies property acquired through foreclosure or acceptance of deed-in-lieu of foreclosure as foreclosed real estate and repossessed assets in its financial statements. Upon foreclosure, the property securing the loan is written down to fair value less selling costs. The write-down is based upon differences between the appraised value and the book value. Appraisals are based on observable market data such as comparable sales, however assumptions made in determining comparability are unobservable and therefore these assets are classified as Level 3 within the valuation hierarchy

Bankwell Financial Group, Inc.

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS – (Unaudited)

## 12. Mergers and Acquisitions

On November 5, 2013, the Company acquired all of the outstanding common shares of Wilton. This business combination expanded the Bank's presence in Fairfield County and enhanced opportunities for businesses, customer relationships, employees and the communities served by the Bank.

On the acquisition date, Wilton had 372,985 outstanding common shares, net of 108,260 shares of treasury stock, and shareholders' equity of \$6.3 million. Wilton shareholders received \$13.50 per share in cash resulting in a consideration value of \$5.0 million.

The assets and liabilities in the Wilton acquisition were recorded at their fair value based on management's best estimate using information available at the date of acquisition. Consideration paid and fair values of Wilton's assets acquired and liabilities assumed are summarized in the following tables:

Consideration paid: (In thousands)			Amount
Cash consideration paid to Wilton shareholders			\$ 5,035
Recognized amounts of identifiable assets acquired and (liabilities) assumed: (In thousands)	As Acquired	Fair Value Adjustments	As Recorded at Acquisition
Cash	\$ 35,919	\$ -	\$ 35,919
Held to maturity investments securities	1,022	-	1,022
Loans	27,097	(2,008 )a	25,089
Premises and equipment	4,303	-	4,303
Other real estate owned	1,895	(450 )b	1,445
Core deposit intangibles	-	499 c	499
Deferred tax assets, net	-	1,997 d	1,997
Other assets	587	-	587
Deposits	(64,145 )	(12 )e	(64,157 )
Other liabilities	(336 )	-	(336 )
Total identifiable net assets	\$ 6,342	\$ 26	\$ 6,368
Gain on purchase			\$ (1,333 )

## Explanation of fair value adjustments:

- The adjustment represents the write down of the book value of loans to their estimated fair value based on current interest rates and expected cash flows, which includes an estimate of expected loan loss inherent in the portfolio.
- The adjustment represents the write down of the book value of foreclosed real estate to their estimated fair value based on current appraisals.
- Represents the economic value of the acquired core deposit base (total deposits less jumbo time deposits). The core deposit intangible will be amortized over an estimated life of 9.3 years based on the

double declining balance method of amortization.

- d) Represents net deferred tax assets resulting from the fair value adjustments related to the acquired assets and liabilities, identifiable intangibles and other purchase accounting adjustments.
- e) The adjustment represents the fair value of time deposits, which were valued at a premium of 0.11% as they bore slightly higher rates than the prevailing market.

Bankwell Financial Group, Inc.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS – (Unaudited)

Except for collateral dependent loans with deteriorated credit quality, the fair values for loans acquired from Wilton were estimated using cash flow projections based on the remaining maturity and repricing terms. Cash flows were adjusted by estimating future credit losses and the rate of prepayments. Projected monthly cash flows were then discounted to present value using a risk-adjusted market rate for similar loans. For collateral dependent loans with deteriorated credit quality, to estimate the fair value, the Company analyzed the value of the underlying collateral of the loans, assuming the fair values of the loans were derived from the eventual sale of the collateral. Those values were discounted using market derived rates of return, with consideration given to the period of time and costs associated with the foreclosure and disposition of the collateral. There was no carryover of Wilton's allowance for credit losses associated with the loans that were acquired as the loans were initially recorded at fair value.

Information about the acquired loan portfolio subject to purchased credit impaired accounting guidance (ASC 310-30) as of November 5, 2013 was as follows:

(In thousands)	November 5, 2013
Contractually required principal and interest at acquisition	\$ 14,528
Contractual cash flows not expected to be collected (nonaccretable discount)	(1,412 )
Expected cash flows at acquisition	13,116
Interest component of expected cash flows (accretable discount)	(1,513 )
Fair value of acquired loans	\$ 11,603

13. Subsequent events

On October 1, 2014, the Company acquired all of the outstanding common shares of Quinnipiac Bank & Trust Company ("Quinnipiac"). Quinnipiac had two banking offices primarily serving south-central Connecticut and has merged with and into Bankwell Bank.

Quinnipiac shareholders received 510,122 shares of the Company common stock and \$3.6 million in cash. As of September 30, 2014, Quinnipiac had assets with a carrying value of approximately \$117.8 million, including loans outstanding with a carrying value of approximately \$97.1 million, as well as deposits with a carrying value of approximately \$100.4 million and a book value of \$10.1 million. The results of Quinnipiac's operations will be included in the Company's Consolidated Statement of Income from the date of acquisition. The Company incurred \$343 thousand of merger and acquisition expenses related to the Quinnipiac merger for the nine months ended September 30, 2014. The Company anticipates that it will incur approximately an additional \$1.1 million of merger and acquisition expenses in the quarter ended December 31, 2014.

As a result of the proximity of the closing of the merger with Quinnipiac to the date these consolidated financial statements are available to be issued, the Company is still evaluating the estimated fair values of the assets acquired and the liabilities assumed. Accordingly, the amount of any goodwill and other intangible assets to be recognized in connection with this transaction is also yet to be determined.

The effect of the merger will be reflected in the Company's results beginning with the fourth quarter of 2014.





## Item 2. Management's Discussion And Analysis Of Financial Condition And Results Of Operations.

This section presents management's perspective on our financial condition and results of operations. The following discussion and analysis should be read in conjunction with the unaudited interim consolidated financial statements and related notes contained elsewhere in this report on Form 10-Q. To the extent that this discussion describes prior performance, the descriptions relate only to the periods listed, which may not be indicative of future financial outcomes. In addition to historical information, this discussion contains forward-looking statements that involve risks, uncertainties and assumptions that could cause results to differ materially from management's expectations. Factors that could cause such differences are discussed in Company's Registration Statement on Form S-1 filed for the year ended December 31, 2013 in the sections titled "Cautionary Note Regarding Forward-Looking Statements" and "Risk Factors" We assume no obligation to update any of these forward-looking statements.

### General

Bankwell Financial Group, Inc. is a bank holding company headquartered in New Canaan, Connecticut. Through our wholly owned subsidiary, Bankwell Bank, or the Bank, we serve small and medium-sized businesses and retail customers in greater Fairfield County, Connecticut and New Haven County, Connecticut as of October 1, 2014 as a result of the merger with Quinnipiac Bank and Trust Company. We have a history of building long-term customer relationships and attracting new customers through what we believe is our strong customer service and our ability to deliver a diverse product offering.

The following discussion and analysis presents our results of operations and financial condition on a consolidated basis. However, because we conduct all of our material business operations through the Bank, the discussion and analysis relates to activities primarily conducted at the Bank.

As a bank holding company, we generate most of our revenue from interest on loans and investments and fee-based revenues. Our primary source of funding for our loans is deposits. Our largest expenses are interest on these deposits and salaries and related employee benefits. We measure our performance primarily through our net interest margin, efficiency ratio, ratio of allowance for loan losses to total loans, return on average assets and return on average equity, among other metrics, while maintaining appropriate regulatory leverage and risk-based capital ratios.

### Critical Accounting Policies and Estimates

The discussion and analysis of our results of operations and financial condition are based on our consolidated financial statements, which have been prepared in accordance with GAAP. The preparation of financial statements in conformity with GAAP requires us to make significant estimates and assumptions that affect the reported amounts of assets, liabilities, revenues and expenses. Actual results could differ from our current estimates, as a result of changing conditions and future events. The current economic environment has increased the degree of uncertainty inherent in these significant estimates.

We believe that accounting estimates for the allowance for loan losses, fair values of securities and deferred taxes are particularly critical and susceptible to significant near-term change. These accounting estimates are discussed further in the Company's Registration Statement on Form S-1 filed for the year ended December 31, 2013 in the section "Critical Accounting Policies and Estimates" under Management's Discussion and Analysis of Financial Condition and Results of Operations.



## Executive Overview

We are focused on becoming the “Hometown” bank and the banking provider of choice in our highly attractive market area, and to serve as a locally based alternative to our larger competitors. We aim to do this through:

- Responsive, customer-centric products and services and a community focus;
- Strategic acquisitions;
- Utilization of efficient and scalable infrastructure;
- Disciplined focus on risk management; and
- Organic growth.

On November 5, 2013 we completed the merger of Wilton into Bankwell Bank. The results discussed below for the three and nine months ended September 30, 2013 do not reflect any results from Wilton.

On March 31, 2014, we entered into a merger agreement with Quinnipiac Bank & Trust Company, or Quinnipiac, located in New Haven County, Connecticut. Quinnipiac had one branch located in Hamden, Connecticut and a second branch located in the neighboring town of North Haven, Connecticut. On October 1, 2014 we completed the merger and Quinnipiac merged with and into Bankwell Bank. The results discussed below for the three and nine months ended September 30, 2014 do not reflect any results from Quinnipiac.

On May 15, 2014, Bankwell Financial Group, Inc. priced 2,702,703 common shares in its IPO at \$18.00 per share, and on May 15, 2014, Bankwell common shares began trading on the Nasdaq Stock Market. The net proceeds from the IPO were approximately \$44.7 million, after deducting the underwriting discount of approximately \$2.5 million and approximately \$1.3 million of expenses. We intend to use the net proceeds for general corporate purposes, which may include maintaining liquidity at the holding company, providing equity capital to the Bank to fund balance sheet growth or working capital needs, our working capital needs, and funding acquisitions of branches, whole financial institutions and related lines of businesses in or around our existing market that further our objectives.

## Earnings Overview

Net income available to common shareholders was \$1.4 million, or \$0.22 per diluted share, and \$1.3 million, or \$0.37 per diluted share, respectively, for the three months ended September 30, 2014 and 2013. Returns on average equity and average assets for the three months ended September 30, 2014 were 5.02% and 0.67%, respectively, compared to 8.23% and 0.75%, respectively, for the same period in 2013.

Net income available to common shareholders was \$3.7 million, or \$0.72 per diluted share, and \$3.7 million, or \$1.10 per diluted share, respectively, for the nine months ended September 30, 2014 and 2013. Returns on average equity and average assets for the nine months ended September 30, 2014 were 5.84% and 0.62%, respectively, compared to 8.30% and 0.78%, respectively, for the same period in 2013.

For the three months ended September 30, 2014, we had net interest income of \$7.6 million, an increase of \$1.2 million, or 18.8%, over the three months ended September 30, 2013. Our net interest margin (fully taxable equivalent basis) for the three months ended September 30, 2014 and 2013 was 3.69% and 4.00%, respectively. We experienced a decline in our non-interest income, which totaled \$757 thousand for the three months ended September 30, 2014 representing 8.03% of our total revenue, down from \$1.1 million, or 13.2% of total revenue, for the three months ended September 30, 2013. The decline in our non-interest income was driven by a reduction in gains and fees from sales of loans of \$606 thousand.

For the nine months ended September 30, 2014, we had net interest income of \$21.9 million, an increase of \$3.2 million, or 16.9%, over the nine months ended September 30, 2013. Our net interest margin (fully taxable equivalent basis) for the nine months ended September 30, 2014 and 2013 was 3.78% and 4.04%, respectively. We experienced decline in our non-interest income, which totaled \$2.2 million for the nine months ended September 30, 2014 representing 8.24% of our total revenue, down from \$2.9 million, or 12.2% of total revenue, for the nine months ended September 30, 2013. The decline in our non-interest income was driven by a reduction of gains and fees from sales of loans of \$729 thousand and a net gain on sale of available for sale securities recognized in 2013 of \$648 thousand.

## Results of Operations

### Net Interest Income

Net interest income is the difference between interest earned on loans and securities and interest paid on deposits and other borrowings, and is the primary source of our operating income. Net interest income is affected by the level of interest rates, changes in interest rates and changes in the amount and composition of interest-earning assets and interest-bearing liabilities. Included in interest income are certain loan fees, such as deferred origination fees and late charges. The following tables and discussion present net interest income on a fully taxable equivalent, or FTE basis, by adjusting income and yields on tax-exempt loans and securities to be comparable to taxable loans and securities. We convert tax-exempt income to a FTE basis using the statutory federal income tax rate adjusted for applicable state income taxes net of the related federal tax benefit. The average balances are principally daily averages. Interest income on loans includes the effect of deferred loan fees and costs accounted for as yield adjustments. Premium amortization and discount accretion are included in the respective interest income and interest expense amounts.

FTE net interest income for the three months ended September 30, 2014 and 2013 was \$7.7 million and \$6.5 million, respectively. FTE net interest income for the nine months ended September 30, 2014 and 2013 was \$22.2 million and \$19.0 million, respectively. Our net interest margin declined 31 basis points to 3.69% for the three months ended September 30, 2014, compared to the same period in 2013 due primarily to the effects of the low interest rate environment and an increase in cash and fed funds sold as a result of the capital raised from the IPO. Our net interest margin declined 26 basis points to 3.78% for the nine months ended September 30, 2014, compared to the same period in 2013 due primarily to the effects of the low interest rate environment and an increase in cash and fed funds sold as a result of the capital raised from the IPO. While we have experienced significant growth in average loan balances, in the current low interest rate environment, market yields on new loan originations are below the average yield of our existing loan portfolio. Due to the combined effect of new loan growth and the runoff of higher yielding loan balances, we anticipate that interest rates on total earning assets will continue to decline. The impact of this trend is likely to exceed the benefit to be realized in reduced funding costs, resulting in modestly lower net interest margin results in the near term.

FTE basis interest income for the three months ended September 30, 2014 increased by \$1.5 million, or 22%, to \$8.8 million, compared to FTE basis interest income for the three months ended September 30, 2013 due primarily to loan growth in our commercial real estate and commercial business portfolios and growth in our securities portfolio, offset by lower yields on earning assets. Average interest-earning assets were \$835.5 million for the three months ended September 30, 2014, up by \$185.3 million from the same period in 2013. The average balance of total loans increased \$120.3 million, or 21%, contributing \$1.3 million to the increase in interest income. Commercial real estate and commercial business loan average balances grew by \$67.0 million and \$30.3 million, respectively. The average yield on interest earning assets declined from 4.35% for the three months ended September 30, 2013 to 4.11% for the three months ended September 30, 2014.

FTE basis interest income for the nine months ended September 30, 2014 increased by \$3.9 million, or 19%, to \$24.9 million, compared to FTE basis interest income for the nine months ended September 30, 2013 due primarily to loan growth in our commercial real estate and commercial business portfolios and growth in our securities portfolio, offset by lower yields on earning assets. Average interest-earning assets were \$782.0 million for the nine months ended September 30, 2014, up by \$154.9 million from the same period in 2013. The average balance of total loans increased \$106.4 million, or 19%, contributing \$3.4 million to the increase in interest income. Commercial real estate and commercial business loan average balances grew by \$45.7 million and \$34.5 million, respectively. The average yield on interest earning assets declined from 4.41% for the nine months ended September 30, 2013 to 4.20% for the nine months ended September 30, 2014.

Interest expense for the three months ended September 30, 2014, increased by \$346 thousand, or 48%, compared to interest expense for the three months ended September 30, 2013 due to a \$117 million increase in the average balances of interest-bearing liabilities due to higher average balances in money market and time accounts, increased rates on time deposits and the impact of higher rates paid on deposit accounts.

Interest expense for the nine months ended September 30, 2014, increased by \$713 thousand, or 36%, compared to interest expense for the nine months ended September 30, 2013 due to a \$107 million increase in the average balances of interest-bearing liabilities due to higher average balances in money market and time accounts, increased rates on time deposits and borrowings.

## Average Balance Sheet, FTE basis Interest and Average Yields/Rates

The following tables present the average balances and yields earned on interest-earning assets and the average balances and weighted average rates paid on our funding liabilities for the three and nine months ended September 30, 2014 and 2013.

(Dollars in thousands)	Three Months Ended September 30,					
	2014			2013		
	Average Balance	Interest	Yield/Rate	Average Balance	Interest	Yield/Rate
<b>Assets:</b>						
Cash and Fed funds sold	\$64,752	\$45	0.28 %	\$31,569	\$18	0.22 %
Securities (1)	71,536	666	3.73	39,993	451	4.51
<b>Loans:</b>						
Commercial real estate	365,042	4,473	4.79	298,085	3,789	4.97
Residential real estate	166,123	1,499	3.61	156,580	1,429	3.65
Construction (2)	47,261	570	4.72	38,018	461	4.74
Commercial business	101,184	1,296	5.01	70,843	968	5.35
Home equity	12,786	121	3.75	10,511	100	3.80
Consumer	698	15	8.75	39	2	17.98
Acquired Loan Portfolio Non accrual loans (net of mark)	1,327	81	24.15	-	-	-
Total loans	694,421	8,055	4.54	574,076	6,749	4.60
Federal Home Loan Bank stock	4,834	18	1.49	4,587	4	0.37
Total earning assets	835,543	\$8,784	4.11 %	650,225	\$7,222	4.35 %
Other assets	47,383			49,160		
Total assets	\$882,926			\$699,385		
<b>Liabilities and shareholders' equity:</b>						
<b>Interest -bearing liabilities:</b>						
NOW	\$52,298	\$15	0.11 %	\$31,933	\$9	0.12 %
Money market	175,111	218	0.49	118,705	138	0.46
Savings	79,505	65	0.33	110,510	128	0.46
Time	257,616	607	0.93	170,246	325	0.76
Total interest-bearing deposits	564,530	905	0.64	431,394	600	0.55
Borrowed Money	47,333	168	1.41	63,903	127	0.79
Total interest bearing liabilities	611,863	\$1,073	0.70 %	495,297	\$727	0.58 %
Noninterest-bearing deposits	138,272			97,574		
Other liabilities	14,918			42,915		
Total Liabilities	765,053			635,786		
Shareholders' equity	117,873			63,599		
Total liabilities and shareholders' equity	\$882,926			\$699,385		
Net interest income (3)		\$7,711			\$6,495	
Interest rate spread			3.41 %			3.77 %
Net interest margin (4)			3.69 %			4.00 %

(1) Average balances and yields for securities are based on amortized cost.



- (2) Includes commercial and residential real estate construction.
- (3) The adjustment for securities and loans taxable equivalency amounted to \$116 thousand and \$101 thousand, respectively, for the three months ended September 30, 2014 and 2013.
- (4) Annualized net interest income as a percentage of earning assets.

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(Dollars in thousands)	Nine Months Ended September 30,					
	2014			2013		
	Average Balance	Interest	Yield/Rate	Average Balance	Interest	Yield/Rate
<b>Assets:</b>						
Cash and Fed funds sold	\$58,699	\$116	0.26 %	\$23,547	\$39	0.22 %
Securities (1)	53,723	1,697	4.21	40,654	1,294	4.25
<b>Loans:</b>						
Commercial real estate	341,480	12,523	4.84	295,752	11,206	5.00
Residential real estate	161,049	4,362	3.61	150,957	4,214	3.72
Construction (2)	46,317	1,615	4.60	36,149	1,317	4.80
Commercial business	99,113	3,705	4.93	64,576	2,576	5.26
Home equity	13,373	370	3.70	10,624	298	3.75
Consumer	640	42	8.88	282	13	6.14
Acquired Loan Portfolio Non accrual loans (net of mark)	2,753	425	20.64	-	-	-
Total loans	664,725	23,042	4.57	558,340	19,624	4.63
Federal Home Loan Bank stock	4,834	54	1.48	4,516	13	0.37
Total earning assets	781,981	\$24,909	4.20 %	627,057	\$20,970	4.41 %
Other assets	39,993			20,134		
Total assets	\$821,974			\$647,191		
<b>Liabilities and shareholders' equity:</b>						
<b>Interest-bearing liabilities:</b>						
NOW	\$52,544	\$43	0.11 %	\$34,030	\$33	0.13 %
Money market	173,104	564	0.44	106,279	338	0.43
Savings	93,328	216	0.31	121,088	421	0.47
Time	224,765	1,434	0.85	147,138	761	0.69
Total interest-bearing deposits	543,741	2,257	0.55	408,535	1,553	0.51
Borrowed Money	48,370	427	1.18	76,612	418	0.73
Total interest bearing liabilities	592,111	\$2,684	0.61 %	485,147	\$1,971	0.54 %
Noninterest-bearing deposits	129,074			87,312		
Other liabilities	12,808			13,546		
Total liabilities	733,993			586,005		
Shareholders' equity	87,981			61,186		
Total liabilities and shareholders' equity	\$821,974			\$647,191		
Net interest income (3)		\$22,225			\$18,999	
Interest rate spread			3.59 %			3.87 %
Net interest margin (4)			3.78 %			4.04 %

(1) Average balances and yields for securities are based on amortized cost.

(2) Includes commercial and residential real estate construction.

(3) The adjustment for securities and loans taxable equivalency amounted to \$336 thousand and \$271 thousand, respectively, for the nine months ended September 30, 2014 and 2013.

(4) Annualized net interest income as a percentage of earning assets.



## Effect of changes in interest rates and volume of average earning assets and average interest-bearing liabilities

The following table shows the extent to which changes in interest rates and changes in the volume of average earning assets and average interest-bearing liabilities have affected net interest income. For each category of earning assets and interest-bearing liabilities, information is provided relating to: changes in volume (changes in average balances multiplied by the prior year's average interest rates); changes in rates (changes in average interest rates multiplied by the prior year's average balances); and the total change. Changes attributable to both volume and rate have been allocated proportionately based on the relationship of the absolute dollar amount of change in each.

(In thousands)	Three Months Ended September 30, 2014 vs 2013 Increase (Decrease)			Nine Months Ended September 30, 2014 vs 2013 Increase (Decrease)		
	Volume	Rate	Total	Volume	Rate	Total
<b>Interest and dividend income:</b>						
Cash and Fed funds sold	\$ 22	\$ 5	\$ 27	\$ 68	\$ 9	\$ 77
Securities	304	(89 )	215	413	(10 )	403
<b>Loans:</b>						
Commercial real estate	825	(141 )	684	1,686	(370 )	1,316
Residential real estate	86	(16 )	70	276	(128 )	148
Construction	111	(3 )	108	357	(59 )	298
Commercial business	392	(64 )	328	1,301	(172 )	1,129
Home equity	22	(1 )	21	76	(4 )	72
Consumer	15	(1 )	14	22	8	30
Wilton Non accrual loans (net of mark)	81	-	81	425	-	425
Total loans	1,532	(226 )	1,306	4,143	(725 )	3,418
Federal Home Loan Bank stock	1	13	14	1	40	41
Total change in interest and dividend income	1,859	(297 )	1,562	4,625	(686 )	3,939
<b>Interest expense:</b>						
<b>Deposits:</b>						
NOW	6	-	6	16	(6 )	10
Money market	69	11	80	217	9	226
Savings	(31 )	(32 )	(63 )	(83 )	(122 )	(205 )
Time	194	88	282	466	207	673
Total deposits	238	67	305	616	88	704
Borrowed Money	(39 )	80	41	(190 )	199	9
Total change in interest expense	199	147	346	426	287	713
Change in net interest income	\$ 1,660	\$ (444 )	\$ 1,216	\$ 4,199	\$ (973 )	\$ 3,226

### Provision for Loan Losses

The provision for loan losses is based on management's periodic assessment of the adequacy of the allowance for loan losses which, in turn, is based on such interrelated factors as the composition of the loan portfolio and its inherent risk characteristics, the level of nonperforming loans and net charge-offs, both current and historic, local economic and credit conditions, the direction of real estate values, and regulatory guidelines. The provision for loan losses is charged against earnings in order to maintain our allowance for loan losses and reflects management's best estimate of probable losses inherent in our loan portfolio at the balance sheet date.

Under accounting standards for business combinations, acquired loans are recorded at fair value with no loan loss allowance on the date of acquisition. A provision for loan losses will be recorded for the emergence of new probable and estimable losses on acquired loans which were not impaired as of the acquisition date. As of and for the three and nine months ended September 30, 2014, there was a \$0 provision or allowance for loan losses related to the loan portfolio that we acquired from The Wilton Bank on November 5, 2013.

The provision for loan losses for the three months ended September 30, 2014 was \$566 thousand compared to \$47 thousand provision for loan losses for the three months ended September 30, 2013. The provision for loan losses for the nine months ended September 30, 2014 was \$847 thousand compared to \$489 thousand provision for loan losses for the nine months ended September 30, 2013. For further information, see sections titled Asset Quality and Allowance for Loan Losses.

#### Noninterest Income

The following tables compare noninterest income for the three and nine months ended September 30, 2014 and 2013:

(Dollars in thousands)	Three Months Ended		Change	
	September 30, 2014	September 30, 2013	\$	%
Gains and fees from sales of loans	\$366	\$972	\$(606 )	(62 )%
Service charges and fees	153	100	53	53
Bank owned life insurance	135	-	135	100
Gain (loss) on sale of foreclosed real estate, net	-	(16 )	16	100
Other	103	27	76	281
Total noninterest income	\$757	\$1,083	\$(326 )	(30 )%

Noninterest income decreased \$326 thousand to \$757 thousand for the three months ended September 30, 2014 compared to the same period in 2013, reflecting a decrease in gains recorded on sales of loans. During the three months ended September 30, 2014, the Company recorded \$21 thousand in gains on the sale of \$1.6 million of residential real estate loans and \$345 thousand of gains on the sale of \$2.7 million of SBA loans. During the three months ended September 30, 2013, the Company recorded income of \$866 thousand on the sale of \$32 million of commercial real estate loans, \$71 thousand on the sale of \$1.2 million of SBA loans and \$35 thousand on the sale of \$2.7 million of residential real estate loans. The Company did not have any bank owned life insurance income in the prior year because the Company did not start purchasing bank owned life insurance until the fourth quarter of 2013. In the fourth quarter of 2013, the Company purchased \$10.0 million in bank-owned life insurance coverage and for the quarter ended September 30, 2014, the Company purchased an additional \$12.5 million in bank-owned life insurance coverage and the cash surrender value increased by \$135 thousand. Other income increased \$76 thousand from \$27 thousand for the three months ended September 30, 2013 to \$103 thousand for the three months ended September 30, 2014, primarily driven by increases in rental income and investments services income.

(Dollars in thousands)	Nine Months Ended		Change	
	September 30, 2014	September 30, 2013	\$	%
Gains and fees from sales of loans	\$1,008	\$1,737	\$(729)	(42)%
Service charges and fees	420	297	123	41
Bank owned life insurance	305	-	305	100
Net gain on sale of available for sale securities	-	648	(648)	(100)
Gain (loss) on sale of foreclosed real estate, net	-	49	(49)	(100)
Other	475	141	334	237
Total noninterest income	\$2,208	\$2,872	\$(664)	(23)%

Noninterest income decreased \$664 thousand to \$2.2 million for the nine months ended September 30, 2014 compared to the same period in 2013 reflecting a decrease in gains recorded on sales of loans and net gains recognized on the sale of securities for the nine months ended September 30, 2013 not repeated in 2014. During the nine months ended September 30, 2014, the Company recorded income of \$413 thousand on the sale of \$14.9 million of commercial real estate loans, \$43 thousand on the sale of \$3.2 million of residential real estate loans and \$552 thousand on the sale of \$4.5 million of SBA loans. During the nine months ended September 30, 2013, the Company recorded income of \$1.6 million on the sale of \$54 million commercial real estate loans, \$71 thousand on the sale of \$1.2 million of SBA loans and \$68 thousand on the sale of \$5.5 million of residential real estate loans. The Company did not have any bank owned life insurance income in the prior year because the Company did not start purchasing bank owned life insurance until the fourth quarter of 2013. In the fourth quarter of 2013, the Company purchased \$10.0 million in bank-owned life insurance coverage and for the nine-months ended September 30, 2014, the Company purchased an additional \$12.5 million in bank-owned life insurance coverage and the cash surrender value increased by \$305 thousand. Other income increased \$334 thousand from \$141 thousand as of September 30, 2013 to \$475 thousand as of September 30, 2014, primarily driven by increases in rental income and investments services income.

#### Noninterest Expense

The following tables compare noninterest expense for the three and nine months ended September 30, 2014, and 2013:

(Dollars in thousands)	Three Months Ended		Change	
	September 30, 2014	September 30, 2013	\$	%
Salaries and employee benefits	\$2,786	\$2,894	\$(108)	(4)%
Occupancy and equipment	1,066	836	230	28
Professional services	394	422	(28)	(7)
Data processing	314	280	34	12
Director fees	177	142	35	25
Merger and acquisition related expenses	145	-	145	100
Marketing	135	378	(243)	(64)
FDIC insurance	120	36	84	233
Amortization of intangibles	27	-	27	100
Foreclosed real estate	9	1	8	800
Other	357	342	15	4
Total noninterest expense	\$5,530	\$5,331	\$199	4%





Noninterest expense increased \$199 thousand to \$5.5 million for the three months ended September 30, 2014 compared to the same period in 2013. The increase in occupancy and equipment largely reflects investments related to technology and other equipment as well as costs related to our new Wilton location acquired in November, 2013 and the relocation of two branch locations. Merger and acquisition related expenses reflect costs associated with the merger agreement with Quinnipiac Bank and Trust Company. The decrease in salaries and employee benefits is largely driven by open positions, timing of hiring employees and reductions in incentive accruals. The decrease in marketing expenses is largely driven by rebranding costs incurred during 2013.

(Dollars in thousands)	Nine Months Ended		Change		
	September 30, 2014	September 30, 2013	\$	%	
Salaries and employee benefits	\$9,412	\$8,146	\$1,266	16	%
Occupancy and equipment	3,162	2,410	752	31	
Professional services	1,035	1,212	(177)	(15)	)
Data processing	949	787	162	21	
Director fees	460	426	34	8	
Merger and acquisition related expenses	408	64	344	538	
Marketing	463	776	(313)	(40)	)
FDIC insurance	345	267	78	29	
Amortization of intangibles	80	-	80	100	
Foreclosed real estate	21	4	17	425	
Other	1,134	950	184	19	
Total noninterest expense	\$17,469	\$15,042	\$2,427	16	%

Noninterest expense increased \$2.4 million to \$17.5 million for the nine months ended September 30, 2014 compared to the same period in 2013. The largest component of the total increase was salaries and employee benefits, primarily reflecting higher staffing levels and increases in incentive accruals. The increase in occupancy and equipment expense largely reflects investments related to technology and other equipment as well as costs related to our new Wilton location acquired in November, 2013 and the relocation of two branch locations. Data processing costs have increased reflecting higher transaction volume. Merger and acquisition related expenses during the nine months ended September 2014 primarily reflect costs associated with the merger agreement with Quinnipiac Bank and Trust Company and the Bank of Wilton. Professional services declined \$177 thousand from \$1.2 million as of September 30, 2013 to \$1.0 million as of September 30, 2014, primarily driven by a reduction in the fees paid to consultants. The decrease in marketing expenses is largely driven by rebranding costs incurred during 2013.

#### Income Tax Expense

Income tax expense for the three months ended September 30, 2014 and 2013 totaled \$765 thousand and \$780 thousand, respectively. The effective tax rates for the three months ended September 30, 2014 and 2013 were 33.9%, and 37.2%, respectively. The decrease in the effective tax rate reflects increases in nontaxable income, mainly bank-owned life insurance income.

Income tax expense for the nine months ended September 30, 2014 and 2013 totaled \$1.9 million and \$2.3 million, respectively. The effective tax rates for the nine months ended September 30, 2014 and 2013 were 33.6%, and 37.4%, respectively. The decrease in the effective tax rate reflects increases in nontaxable income, mainly bank-owned life insurance income.



## Financial Condition Summary

At September 30, 2014, total assets were \$895.5 million, a \$115.9 million, or 15%, increase over December 31, 2013. Total loans outstanding and total deposits totaled \$730.1 million and \$695.3 million, respectively at September 30, 2014. Our credit quality remained strong, with nonperforming assets to total assets of 0.23% and the allowance for loan losses to total loans was 1.28%. Total shareholders' equity at September 30, 2014 and December 31, 2013 was \$118.5 million and \$69.5 million, respectively. Tangible book value was \$16.52 per share at September 30, 2014 compared to \$15.46 per share at December 31, 2013.

## Loan Portfolio

We originate commercial and residential real estate loans, including construction loans, commercial business loans, home equity and other consumer loans. Lending activities are primarily conducted within our market of Fairfield County and the surrounding Connecticut region. Our loan portfolio is the largest category of our earning assets. Loans acquired in connection with the Wilton acquisition in November 2013 are referred to as "acquired" loans as a result of the manner in which they are accounted for. All other loans are referred to as "originated" loans. Accordingly, selected disclosures that follow are presented separately for the originated loan portfolio and the acquired loan portfolio.

Total loans before deferred loan fees were \$742.1 million at September 30, 2014, up by \$110.1 million, or 17%, from December 31, 2013. Commercial real estate loans have experienced the most significant growth, up by \$85.2 million.

The following table compares the composition of our loan portfolio for the dates indicated:

(In thousands)	September 30, 2014			December 31, 2013			Change Total
	Originated	Acquired	Total	Originated	Acquired	Total	
<b>Real estate loans:</b>							
Residential	\$167,362	\$-	\$167,362	\$155,874	\$-	\$155,874	\$11,488
Commercial	394,004	6,911	400,915	305,823	9,939	315,762	85,153
Construction	52,387	893	53,280	44,187	7,308	51,495	1,785
Home equity	9,539	3,294	12,833	9,625	3,872	13,497	(664 )
	623,292	11,098	634,390	515,509	21,119	536,628	97,762
<b>Commercial</b>							
business	105,123	2,038	107,161	92,173	2,374	94,547	12,614
Consumer	190	343	533	225	612	837	(304 )
<b>Total loans</b>	<b>\$728,605</b>	<b>\$13,479</b>	<b>\$742,084</b>	<b>\$607,907</b>	<b>\$24,105</b>	<b>\$632,012</b>	<b>\$110,072</b>

## Asset Quality

Asset quality metrics remained strong through the third quarter of 2014. Nonperforming assets totaled \$2.1 million and represented 0.23% of total assets at September 30, 2014, compared to \$1.8 million and 0.23% of total assets at December 31, 2013. Nonaccrual loans totaled \$1.2 million at September 30, 2014, an increase of \$0.2 million from December 31, 2013. The balance of foreclosed real estate remained unchanged and was \$829 thousand at September 30, 2014 and December 31, 2013, consisting of four residential lots that were acquired with Wilton.

The following table presents nonperforming assets and additional asset quality data for the dates indicated:

(In thousands)	At September 30, 2014			At December 31, 2013		
	Originated	Acquired	Total	Originated	Acquired	Total
<b>Nonaccrual loans:</b>						
<b>Real estate loans:</b>						
Residential	\$-	\$-	\$-	\$1,003	\$-	\$1,003
Commercial	1,246	-	1,246	-	-	-
<b>Total non accrual loans</b>	<b>\$1,246</b>	<b>\$-</b>	<b>\$1,246</b>	<b>\$1,003</b>	<b>\$-</b>	<b>\$1,003</b>
Property acquired through foreclosure or repossession, net	-	829	829	-	829	829
<b>Total nonperforming assets</b>	<b>\$1,246</b>	<b>\$829</b>	<b>\$2,075</b>	<b>\$1,003</b>	<b>\$829</b>	<b>\$1,832</b>
<b>Nonperforming assets to total assets</b>	<b>0.14</b>	<b>%</b>	<b>0.09</b>	<b>%</b>	<b>0.23</b>	<b>%</b>
<b>Nonaccrual loans to total loans</b>	<b>0.17</b>	<b>%</b>	<b>0.00</b>	<b>%</b>	<b>0.16</b>	<b>%</b>
<b>Total past due loans to total loans</b>	<b>0.18</b>	<b>%</b>	<b>9.72</b>	<b>%</b>	<b>0.35</b>	<b>%</b>
Accruing loans 90 days or more past due	\$-	\$1,309	\$1,309	\$-	\$3,620	\$3,620

#### Allowance for Loan Losses

Establishing an appropriate level of allowance for loan losses, or the allowance, involves a high degree of judgment. We use a methodology to systematically measure the amount of estimated loan loss exposure inherent in our loan portfolio for purposes of establishing a sufficient allowance for loan losses. We evaluate the adequacy of the allowance at least quarterly. Our allowance for loan losses is our best estimate of the probable loan losses inherent in our loan portfolio as of the balance sheet date. The allowance is increased by provisions charged to earnings and by recoveries of amounts previously charged off, and is reduced by charge-offs on loans.

At September 30, 2014, our allowance for loan losses was \$9.6 million and represented 1.28% of total loans, compared to \$8.4 million, or 1.33% of total loans, at December 31, 2013. The net increase in the allowance primarily reflects a provision of \$847 thousand and net recoveries of \$323 thousand. The carrying amount of total impaired loans at September 30, 2014 and December 31, 2013 was \$6.5 million and \$3.7 million, respectively and the amount of related allowance totaled \$39 thousand and \$145 thousand, respectively. At September 30, 2014 impaired loans consisted of 1 residential real estate loan, 5 commercial real estate loans, 1 home equity loan and 10 commercial business loans and at December 31, 2013 impaired loans consisted of one residential mortgage loan, one substandard commercial mortgage loan and three performing troubled debt restructured loans.

The following tables present the activity in our allowance for loan losses and related ratios for the dates indicated, and include both originated and acquired allowance activity:

(Dollars in thousands)	Three Months Ended		Nine Months Ended	
	September 30,		September 30,	
	2014	2013	2014	2013
Balance at beginning of period	\$8,985	\$8,224	\$8,382	\$7,941
Charge-offs:				
Commercial real estate	-	-	-	(166 )
Construction	-	-	(100 )	-
Consumer	-	-	(1 )	(3 )
Total charge-offs	-	-	(101 )	(169 )
Recoveries:				
Consumer	1	6	424	16
Total recoveries	1	6	424	16
Net recoveries (charge-offs)	1	6	323	(153 )
Provision charged to earnings	566	47	847	489
Balance at end of period	\$9,552	\$8,277	\$9,552	\$8,277
Net recoveries (charge-offs) to average loans	0.00	% 0.00	% 0.05	% -0.03
Allowance for loan losses to total loans	1.28	% 1.42	% 1.28	% 1.42

The following tables present the allocation of the allowance for loan losses and the percentage of these loans to total loans for the dates indicated:

(Dollars in thousands)	At September 30,		At December 31,	
	2014	Percent of	2013	Percent of
	Amount	Loan	Amount	Loan
		Portfolio		Portfolio
Residential real estate	\$1,411	22.55 %	\$1,310	24.66 %
Commercial real estate	4,661	54.03	3,616	50.08
Construction	891	7.18	1,032	8.16
Home equity	191	1.73	190	2.20
Commercial business	2,391	14.44	2,225	14.80
Consumer	7	0.07	9	0.10
Unallocated	-	-	-	-
Total allowance for loan losses	\$9,552	100.00 %	\$8,382	100.00 %

The allocation of the allowance for loan losses at September 30, 2014 reflects our assessment of credit risk and probable loss within each portfolio. We believe that the level of the allowance for loan losses at September 30, 2014 is appropriate to cover probable losses.

#### Investment Securities

At September 30, 2014, the carrying value of our investment securities portfolio totaled \$79.0 million and represented 9% of total assets, compared to \$42.4 million and 5% of total assets at December 31, 2013. The increase of \$36.6 million, or 86%, primarily reflects purchases of U.S. Government agency obligations, corporate and municipal bonds

totaling \$43.8 million. We purchase investment grade securities with a focus on earnings, duration exposure and for use as collateral for public funds. There were no sales of available-for-sale investment securities during the third quarter of 2014.

The net unrealized gain position on our investment portfolio at September 30, 2014 and December 31, 2013 was \$912 thousand and \$695 thousand, respectively and included gross unrealized losses of \$383 thousand and \$349 thousand, respectively. The gross unrealized losses were concentrated in U.S. Government, agency obligations and corporate bonds, reflecting interest rate fluctuation. At September 30, 2014, we determined that there had been no deterioration in credit quality subsequent to purchase and believe that all unrealized losses are temporary. All of our investment securities are investment grade.

#### Sources of Funds

Total deposits were \$695.3 million at September 30, 2014, an increase of \$33.7 million, or 5%, from the balance at December 31, 2013 reflecting growth in noninterest bearing deposits and time deposits.

We utilize advances from the Federal Home Loan Bank of Boston, or FHLBB, as part of our overall funding strategy and to meet short-term liquidity needs. Total FHLBB advances were \$77.0 million at September 30, 2014 compared to \$44.0 million at December 31, 2013. The increase of \$33.0 million, or 75%, reflects normal operating fluctuation in our borrowings.

#### Liquidity

The Company is required to maintain levels of liquid assets sufficient to ensure the Company's safe and sound operation. Liquidity is defined as the ability to generate sufficient cash flows to meet all present and future funding requirements at reasonable costs. Our primary source of liquidity is deposits. Other sources of funding include discretionary use of FHLBB term advances and other borrowings, cash flows from our investment securities portfolios, loan repayments and earnings. Investment securities designated as available-for-sale may also be sold in response to short-term or long-term liquidity needs.

The Company anticipates that it will have sufficient funds available to meet its current loan and other commitments. As of September 30, 2014, the Company had cash and cash equivalents of \$35.6 million and available-for-sale securities of \$67.5 million. At September 30, 2014, outstanding commitments to originate loans totaled \$59.9 million and undisbursed funds from approved lines of credit, home equity lines of credit and secured commercial lines of credit totaled \$105.2 million. Time deposits scheduled to mature in one year or less at September 30, 2014 totaled \$164.4 million. Historically, the Company's deposit flow history has been that a significant portion of such deposits remain with the Company.

#### Capital Resources

Total shareholders' equity was \$118.5 million at September 30, 2014 compared to \$69.5 million at December 31, 2013. The increase of \$49.0 million primarily reflected net capital raised from the IPO of \$44.7 million and net income of \$3.8 million for the nine months ended September 30, 2014. The ratio of total equity to total assets was 13% at September 30, 2014, which compares to 9% at December 31, 2013.

The Bank is subject to various regulatory capital requirements administered by the federal banking agencies. Failure to meet minimum capital requirements can initiate certain mandatory and possibly additional discretionary actions by regulators that, if undertaken, could have a direct material effect on the Company's financial statements. At September 30, 2014, the Bank, met all capital adequacy requirements to which it was subject and exceeded the regulatory minimum capital levels to be considered well-capitalized under the regulatory framework for prompt corrective action. At September 30, 2014, the Bank's ratio of total capital to risk-weighted assets was 15.27%, Tier 1 capital to

risk-weighted assets was 14.02% and Tier 1 capital to average assets was 11.93%.



On May 15, 2014, Bankwell Financial Group, Inc. priced 2,702,703 common shares in its initial public offering at \$18.00 per share, and on May 15, 2014, Bankwell common shares began trading on the Nasdaq Stock Market. The net proceeds from the IPO were approximately \$44.7 million, after deducting the underwriting discount of approximately \$2.5 million and approximately \$1.3 million of expenses.

#### Interest Rate Sensitivity Analysis

We measure interest rate risk using simulation analysis to calculate earnings and equity at risk. These risk measures are quantified using simulation software from one of the leading firms in the field of asset/liability modeling. Key assumptions relate to the behavior of interest rates and spreads, prepayment speeds and the run-off of deposits. From such simulations, interest rate risk, or IRR, is quantified and appropriate strategies are formulated and implemented. We manage IRR by using two primary risk measurement techniques: simulation of net interest income and simulation of economic value of equity. These two measurements are complementary and provide both short-term and long-term risk profiles for the Company. Because income simulations assume that our balance sheet will remain static over the simulation horizon, the results do not reflect adjustments in strategy that the Asset and Liability Committee could implement in response to rate shifts.

We use two sets of standard scenarios to measure net interest income at risk. For the Parallel Ramp scenario, rate changes are ramped over a twelve-month horizon based upon a parallel yield curve shift and then maintained at those levels over the remainder of the simulation horizon. The Parallel shock scenario assumes instantaneous parallel movements in the yield curve compared to a flat yield curve scenario. Simulation analysis involves projecting a future balance sheet structure and interest income and expense under the various rate scenarios. Internal policy regarding internal rate risk simulations currently specifies that for instantaneous parallel shifts of the yield curve, estimated net income at risk for the subsequent one-year period should not decline by more than: 6% for a 100 basis point shift; 12% for a 200 basis point shift and 18% for a 300 basis point shift.

The following tables set forth the estimated percentage change in our net interest income at risk over one-year simulation periods beginning September 30, 2014 and December 31, 2013:

Parallel Ramp	Estimated Percent Change in Net Interest Income	
	September 30,	December 31,
Rate Changes (basis points)	2014	2013
-100	(1.19 )%	(0.73 )%
+200	(3.54 )	(3.63 )

Parallel Shock	Estimated Percent Change in Net Interest Income	
	September 30,	December 31,
Rate Changes (basis points)	2014	2013
-100	(3.52 )%	(1.97 )%
+100	(2.50 )	(3.18 )
+200	(4.46 )	(5.93 )

+300

(7.07 )

(10.20)

We conduct economic value of equity at risk simulation in tandem with net interest income simulations, to ascertain a longer term view of our interest rate risk position by capturing longer-term re-pricing risk and options risk embedded in the balance sheet. It measures the sensitivity of economic value of equity to changes in interest rates. Economic value of equity at risk simulation values only the current balance sheet and does not incorporate the growth assumptions used in income simulation. As with the net interest income simulation, this simulation captures product characteristics such as loan resets, re-pricing terms, maturity dates, rate caps and floors. Key assumptions include loan prepayment speeds, deposit pricing elasticity and non-maturity deposit attrition rates. These assumptions can have significant impacts on valuation results as the assumptions remain in effect for the entire life of each asset and liability. We conduct non-maturity deposit behavior studies on a periodic basis to support deposit assumptions used in the valuation process. All key assumptions are subject to a periodic review.

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Base case economic value of equity at risk is calculated by estimating the net present value of all future cash flows from existing assets and liabilities using current interest rates. The base case scenario assumes that future interest rates remain unchanged.

The following table sets forth the estimated percentage change in our economic value of equity at risk, assuming various shifts in interest rates:

Parallel Shock	Estimated Percent Change in Economic Value of Equity	
	September 30,	December 31,
Rate Changes (basis points)	2014	2013
-100	(0.30 )%	(4.30 )%
+100	(7.60 )	(9.30 )
+200	(16.30 )	(20.10 )
+300	(23.90 )	(29.20 )

The interest rate risk position remains liability sensitive. The sensitivity intensified for the quarter ended September 30, 2014 due to the decreased cash position and the addition of short-term FHLB advances. The Bank remains within all internally established policies for interest rate risk and the economic value of equity calculation.

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

#### Interest Rate Risk Management

Interest rate risk management is our primary market risk. See “Management’s Discussion and Analysis of Financial Condition and Results of Operations — Interest Rate Sensitivity Analysis” herein for a discussion of our management of our interest rate risk.

#### Inflation Risk Management

Inflation has an important impact on the growth of total assets in the banking industry and causes a need to increase equity capital higher than normal levels in order to maintain an appropriate equity-to-assets ratio. We cope with the effects of inflation by managing our interest rate sensitivity position through our asset/liability management program, and by periodically adjusting our pricing of services and banking products to take into consideration current costs.

### Item 4. Controls and Procedures.

#### (a) Evaluation of disclosure controls and procedures:

The Company carried out an evaluation, under the supervision and with the participation of the Company’s management, including the Company’s Executive Chairman and Chief Financial Officer, of the effectiveness of the design and operation of the Company’s disclosure controls and procedures pursuant to Exchange Act Rule 13a-15. Based upon that evaluation, the Executive Chairman and Chief Financial Officer concluded that as of the end of the period reported on in this report, the Company’s disclosure controls and procedures are effective in timely alerting them to material information relating to the Company (including its consolidated subsidiary) required to be

included in the Company's periodic SEC filings.

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(b) Change in internal controls

There has been no change in the Company's internal controls over financial reporting during the quarter that has materially affected, or is reasonably likely to affect, the Company's internal control over financial reporting.

Part ii — Other Information

Item 1. Legal Proceedings.

The Company and the Bank are periodically involved in various legal proceedings as normal incident to their businesses. In the opinion of management, no material loss is expected from any such pending lawsuit.

Item 1A. Risk Factors.

There have been no material changes in risk factors previously disclosed in the Company's Registration Statement dated April 4, 2014, as amended, filed with the SEC except as follows;

Effective August 7, 2014, Peyton R. Patterson resigned as the Chief Executive Officer and President of BWFG and the Chief Executive Officer of Bankwell Bank. Although BWFG is engaged in a comprehensive search for a permanent Chief Executive Officer, it is possible that the disruption caused by the resignation of BWFG's and Bankwell Bank's chief executive could adversely affect BWFG's future results of operations or BWFG's ability to maintain relationships with clients, customers, depositors and employees. Chairman Blake S. Drexler has been appointed executive chairman by the Board of Directors and has assumed Ms. Patterson's responsibilities. Blake S. Drexler does not have any previous experience as an executive officer of a depository institution.

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

None.

Item 3. Defaults Upon Senior Securities.

None.

Item 4. Mine Safety Disclosures.

None.

Item 5. Other Information.

None.

Item 6. Exhibits

The following exhibits are filed herewith:

10.18 Blake S. Drexler, Executive Chairman Compensation Letter and management contract on compensatory plan or arrangement.

- 31.1 Certification of Blake S. Drexler pursuant to Rule 13a-14(a)
- 31.2 Certification of Ernest J. Verrico, Sr. pursuant to Rule 13a-14(a)
- 32 Certification pursuant to Section 906 of the Sarbanes-Oxley Act of 2002
- 101 The following materials from Bankwell Financial Group, Inc.'s Quarterly Report on Form 10-Q for the period ended September 30, 2014, formatted in eXtensible Business Reporting Language (XBRL): (i) Consolidated Statements of Financial Condition; (ii) Consolidated Statement of Income; (iii) Consolidated Statements of Comprehensive Income; (iv) Consolidated Statements of Shareholders' Equity; (v) Consolidated Statements of Cash Flows; and (vi) Notes to Consolidated Financial Statements.

Signatures

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

Bankwell Financial Group, Inc.

Date: November 14, 2014

/s/ Blake S. Drexler  
Blake S. Drexler  
Executive Chairman

Date: November 14, 2014

/s/ Ernest J. Verrico, Sr.  
Ernest J. Verrico, Sr.  
Executive Vice President and Chief  
Financial Officer