MERCER CAPITAL
BUSINESS VALUATION &
FINANCIAL ADVISORY SERVICES

Bank Watch

August 2017

Emerging Community Bank M&A Trends in 2017

As summer came to an end, the U.S. was treated with a historic event as the first total solar eclipse crossed the country since 1918. The timing of the event had social media and news outlets buzzing in a traditionally sleepy news month. For many, the event exceeded all expectations; for others, it was a dud that didn't live up to the hype. My personal experience was a bit of both. The minutes of darkened skies were definitely memorable, but things returned to normal quickly as the sun shone brightly only minutes after.

Traditional M&A Trends

Community bank M&A trends also seem mixed. Rising regulatory burdens, weak margins from a historically low interest rate environment and heightened competition have crimped ROEs for years. Many pundits have predicted a rapid wave of consolidation and the demise of community banks in the years since the financial crisis. However, the pace of consolidation the last few years is consistent with the past three decades in which roughly 3-4% of the industry's banks are absorbed through M&A yearly. The result is many fewer banks—5,787 at June 30 compared to about 15,000 in the mid-1980s when meaningful industry consolidation got underway.

Somewhat surprisingly, the spike in bank stock prices following the November 2016 national elections did not cause M&A to accelerate. As would be expected, acquisition multiples increased in 2017 because publicly traded acquirers could "pay-up" with appreciated shares. As seen in the table on the next page, the median P/E and P/TBV multiples and the median core deposit premium increased for the latest twelve months (LTM) ended July 31, 2017 compared to the year ago LTM period. The ability of buyers—at least the publicly traded ones—to more easily meet sellers' price expectations seemingly would lead more banks to sell. However, that has not happened as the pace of consolidation declined slightly to 132 transactions in the most recent LTM period compared to 140 in the year ago LTM time frame.

Community Bank M&A Overview

Target Banks Assets < $5 BN and LTM ROE > 5%

	Price / LTM Earnings	Price / Tangible BV	Core Deposit Premium	Total Number of Deals	Non-Bank Acquirers	Median Deal Value ($M)	Target's Median Assets ($000)	Target's Median LTM ROAE
LTM Through July 2016	17.5x	143%	6.3%	140	3	41.58	195,874	8.87%
LTM Through July 2017	20.6x	165%	10.0%	132	8	50.94	259,383	8.44%
% Change (Green = +, Red = -)	**18.1%**	**15.6%**	**58.3%**	**-5.7%**	**166.7%**	**22.5%**	**32.4%**	**-4.9%**

Evidence of multiple expansion, larger bank acquisitions, and more non-"bank" buyers.
Deal activity and profitability were down with the ROE of many targets below their cost of capital.

Source: Mercer Capital Research; S&P Global Market Intelligence

FinTech's Impact on M&A

Another emerging M&A trend is the presence of non-traditional bank acquirers, which include private investor groups, non-bank specialty lenders, and credit unions. While a FinTech company has not yet announced an acquisition of a U.S. bank this year, several FinTechs have announced they are applying for a bank charter (SoFi, VaroMoney), and in the U.K., Tandem has agreed to acquire Harrods Bank.

So far, FinTech acquisitions of banks have been limited to a few acquisitions by online brokers and Green Dot Corporation's acquisition of a bank in 2011. While FinTech companies have yet to emerge as active buyers, there have been **some predictions** that could change if regulatory hurdles can be navigated. Some FinTech companies are well-funded or have access to additional funding that could be tapped for a bank acquisition. In addition, an overlay of enhancing financial inclusion for the under-banked could mean bank transactions may not be as far-fetched as some may think.

Beyond serving as potential acquirers, FinTech continues to emerge as an important piece of the community banking puzzle of how to engage customers through digital channels as the costly branch banking model sees usage decline year-after-year. Many FinTechs are eager to partner with banks to scale their operations for greater profitability, thereby better positioning themselves for a successful exit down the road.

Consistent with this trend, we have also seen some acquirers (and analysts) comment on FinTech as a benefit of a transaction, as opposed to (or at least in addition to) the historical focus on geographic location, credit quality, asset size, and profitability. We will be watching to see if FinTech initiatives, whether internally developed or acquired, become a bigger driving force in bank M&A. If so, acquisitions of FinTech companies by traditional banks may increase (as discussed more fully **in this article**).

As these trends grow in importance, buyers and sellers will have to grapple with unique valuation and transaction issues that require each to fully understand the value of the seller and the buyer, assuming a portion of the consideration consists of the buyer's shares. Whether that buyer includes a traditional bank whose stock is private or a non-bank buyer, such as a specialty lender or FinTech company, we have significant valuation and transaction expertise to help your bank understand the deal landscape and the strategic options available to it.

To that end, we have an upcoming **webinar** on September 7 that will address the complex issue of how to value early-stage FinTech companies. Whether your bank is considering potential partnerships, investments, or you just desire to gain a better understanding of the FinTech landscape, the webinar should be informative. Additionally, webinar registrants will receive a copy of my latest book on the topic, ***Creating Strategic Value Through Financial Technology***.

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UPCOMING WEBINAR

How to Value an Early-Stage FinTech Company

Date
September 7, 2017

Time
Noon–1:00 pm CST

CPE Offered
1 Hour

Registration
$79.00 (USD)

Whether your bank is considering potential partnerships or investments, this webinar will address the complex issues surrounding early-stage FinTech valuation to help your bank navigate the space.

Special Offer: Free copy of ***Creating Strategic Value Through Financial Technology*** with registration

Register

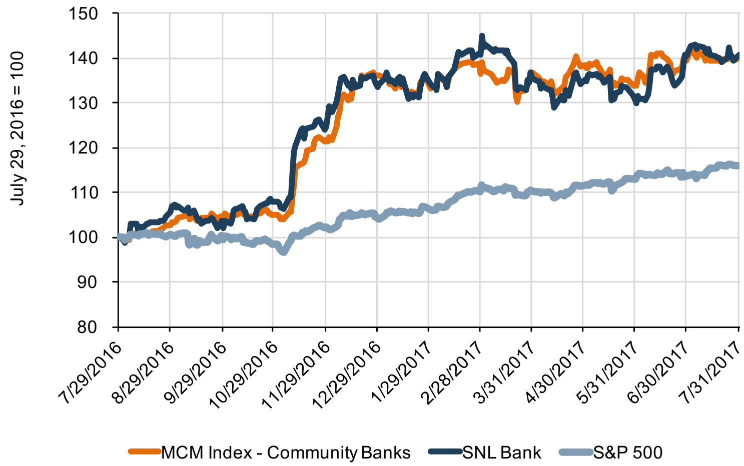
What We're Reading

Bank Issues Primary School Kids with NFC Smartwatches that Let Them Make Payments and Track Pocket Money
NFC World

Many Family-Owned Banks Approach Day of Reckoning
American Banker
(subscription required)

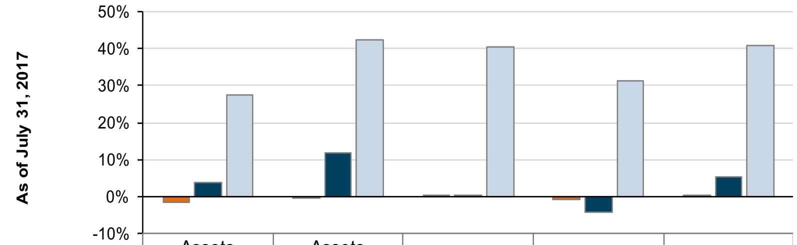
Here Is Why Banks Will Soon Be Acquiring Fintech Startups Instead of Investing in Them
TechBullion

Mercer Capital's Bank Group Index Overview



Return Stratification of U.S. Banks

by Asset Size



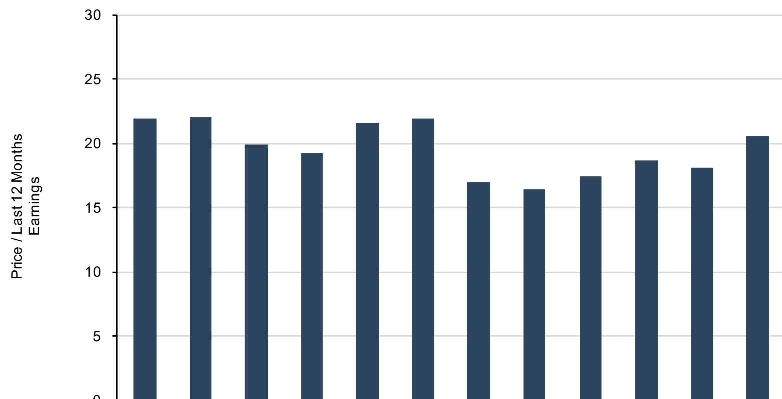
	Assets $250 - $500M	Assets $500M - $1B	Assets $1 - $5B	Assets $5 - $10B	Assets > $10B
Month-to-Date	-1.42%	-0.10%	0.31%	-0.62%	0.23%
Year-to-Date	3.79%	11.87%	0.51%	-4.10%	5.45%
Last 12 Months	27.68%	42.55%	40.65%	31.40%	41.02%

Median Valuation Multiples

	Median Total Return as of July 31, 2017			Median Valuation Multiples as of July 31, 2017					
Indices	Month-to-Date	Year-to-Date	Last 12 Months	Price/ LTM EPS	Price / 17(E) EPS	Price / 18(E) EPS	Price / Book Value	Price / Tangible Book Value	Dividend Yield
Atlantic Coast Index	0.01%	8.49%	43.17%	19.9x	18.5x	15.7x	139%	160%	1.6%
Midwest Index	1.58%	1.49%	40.05%	16.9x	17.1x	15.4x	146%	164%	1.9%
Northeast Index	0.06%	1.31%	37.45%	16.6x	17.3x	15.5x	147%	162%	2.2%
Southeast Index	-2.36%	-1.22%	31.27%	18.7x	19.9x	16.6x	146%	146%	1.4%
West Index	1.69%	5.25%	46.43%	17.7x	17.8x	15.6x	152%	170%	1.7%
Community Bank Index	0.35%	2.93%	39.98%	18.3x	17.8x	15.6x	146%	161%	1.7%
SNL Bank Index	**0.19%**	**4.89%**	**40.62%**						

Median Price/Earnings Multiples

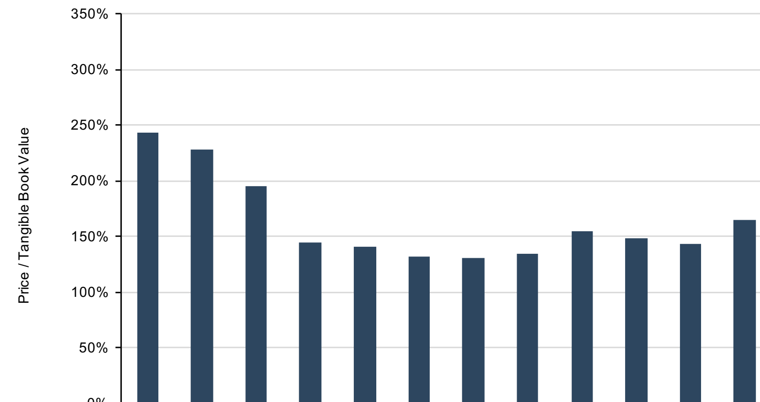
Target Banks' Assets <$5B and LTM ROE >5%



	2006	2007	2008	2009	2010	2011	2012	2013	2014	2015	2016	LTM
U.S.	22.0	22.1	19.9	19.3	21.7	21.9	17.0	16.5	17.5	18.8	18.1	20.6

Median Price/Tangible Book Value Multiples

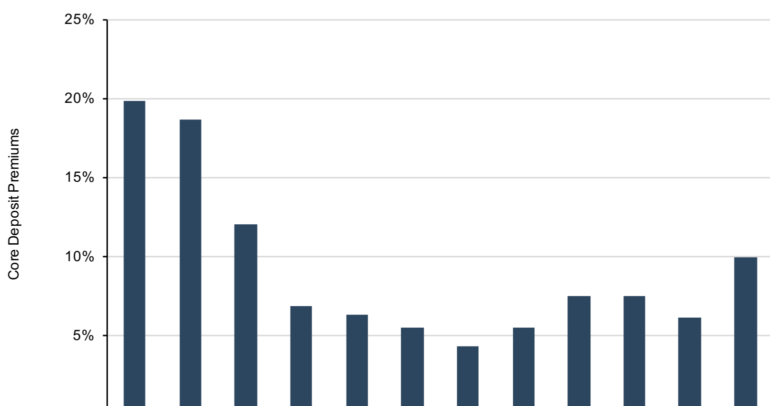
Target Banks' Assets <$5B and LTM ROE >5%



	2006	2007	2008	2009	2010	2011	2012	2013	2014	2015	2016	LTM
U.S.	243%	228%	196%	145%	141%	132%	130%	134%	155%	148%	143%	165%

Median Core Deposit Multiples

Target Banks' Assets <$5B and LTM ROE >5%



	2006	2007	2008	2009	2010	2011	2012	2013	2014	2015	2016	LTM
U.S.	19.9%	18.7%	12.0%	6.9%	6.3%	5.4%	4.3%	5.5%	7.5%	7.5%	6.1%	10.0%

Median Valuation Multiples for M&A Deals

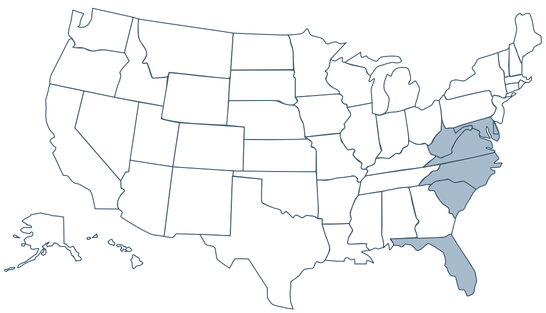
Target Banks' Assets <$5B and LTM ROE >5%, 12 months ended July 2017

Regions	Price / LTM Earnings	Price/ Tang. BV	Price / Core Dep Premium	No. of Deals	Median Deal Value ($M)	Target's Median Assets ($000)	Target's Median LTM ROAE
Atlantic Coast	22.1x	170%	11.8%	25	109.89	583,892	7.60%
Midwest	19.6x	164%	11.3%	51	44.20	181,409	8.83%
Northeast	15.0x	155%	4.3%	8	89.75	656,592	7.93%
Southeast	19.8x	160%	6.9%	26	41.90	170,925	7.57%
West	23.1x	182%	8.2%	22	50.69	287,957	9.06%
National Community Banks	**20.6x**	**165%**	**10.0%**	**132**	**50.94**	**259,383**	**8.44%**

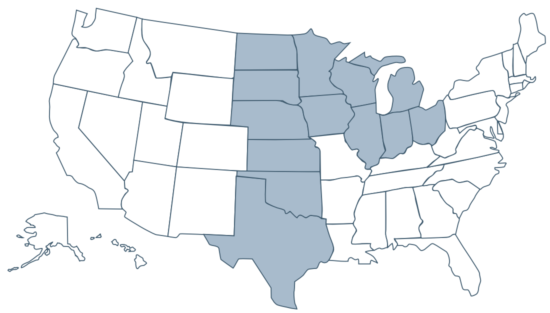
Source: S&P Global Market Intelligence

Mercer Capital's Regional Public Bank Peer Reports

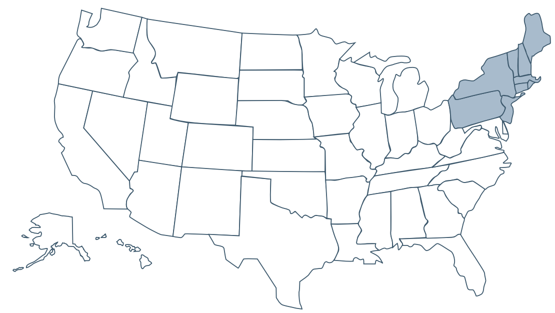
Updated weekly, Mercer Capital's Regional Public Bank Peer Reports offer a closer look at the market pricing and performance of publicly traded banks in the states of five U.S. regions. Click on the map to view the reports from the representative region.



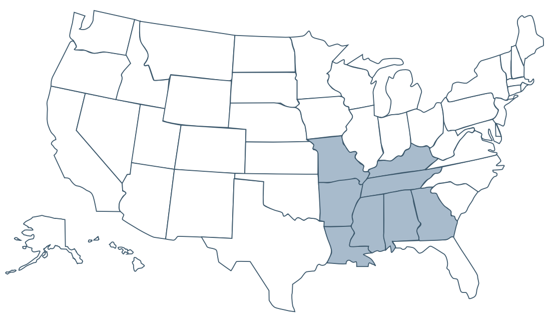
Atlantic Coast



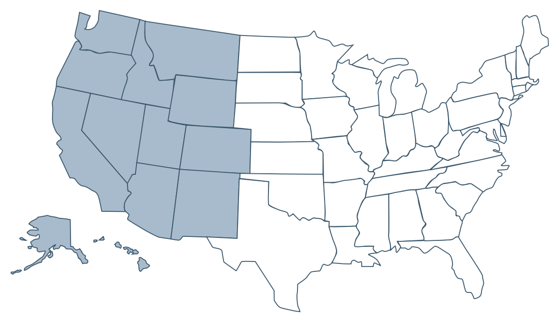
Midwest



Northeast



Southeast



West

Mercer Capital

Financial Institutions Services

Mercer Capital assists banks, thrifts, and credit unions with significant corporate valuation requirements, transactional advisory services, and other strategic decisions.

Mercer Capital pairs analytical rigor with industry knowledge to deliver unique insight into issues facing banks. These insights underpin the valuation analyses that are at the heart of Mercer Capital's services to depository institutions.

- Bank valuation
- Financial reporting for banks
- Goodwill impairment
- Litigation support
- Stress Testing
- Loan portfolio valuation
- Tax compliance
- Transaction advisory
- Strategic planning

Mercer Capital is a thought-leader among valuation firms in the banking industry. In addition to scores of articles and books, *The ESOP Handbook for Banks*, *Acquiring a Failed Bank*, *The Bank Director's Valuation Handbook*, and *Valuing Financial Institutions*, Mercer Capital professionals speak at industry and educational conferences.

For more information about Mercer Capital, visit **www.mercercapital.com**.

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