Acquisitions of Non-Depositories

2014 Acquire or Be Acquired Conference

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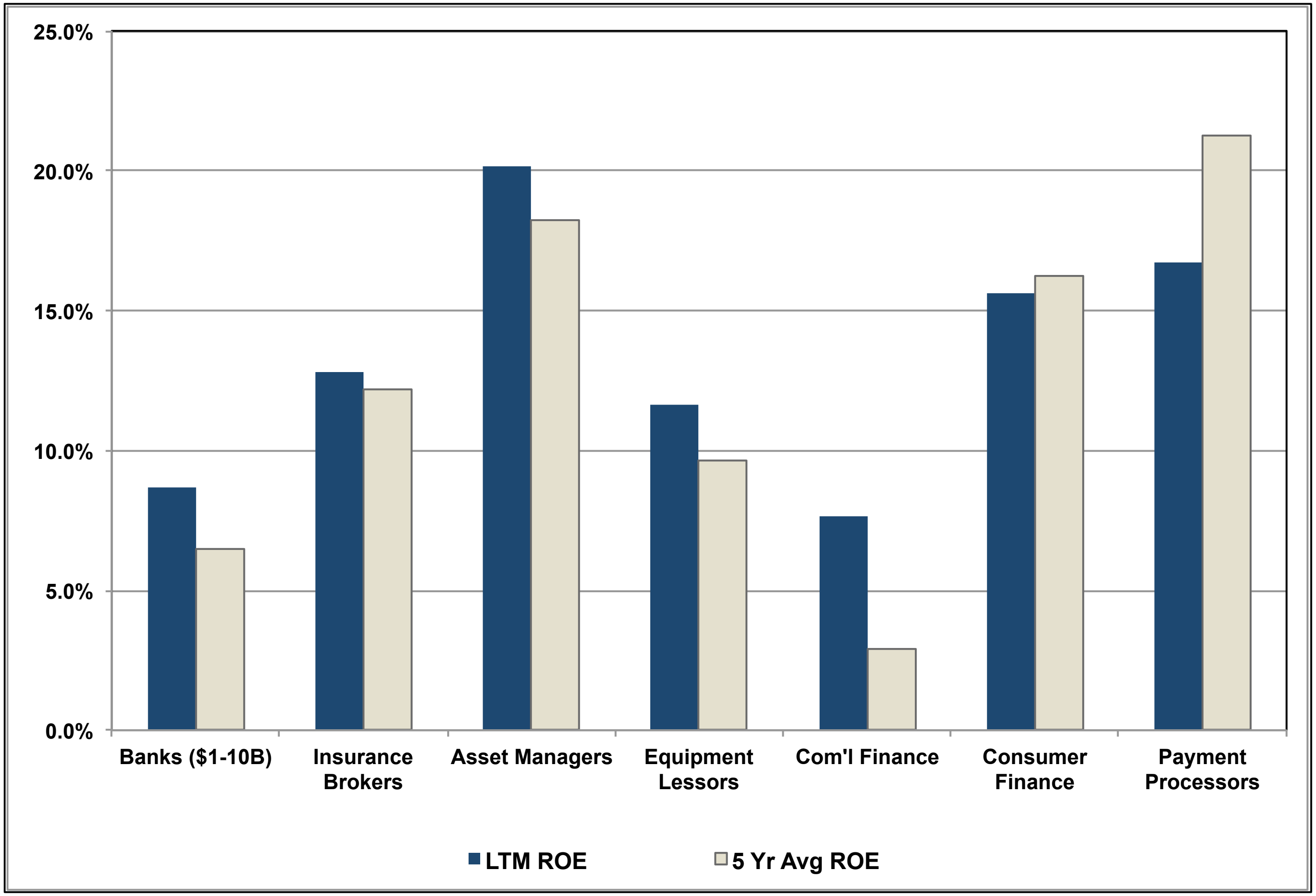
Opportunities

- Deployment of excess capital to drive growth
- Revenue and earnings diversification
- Improve return on capital
- Cross-sell existing customers
- Improve the bank's valuation
- Target as a subsidiary of the bank

Issues

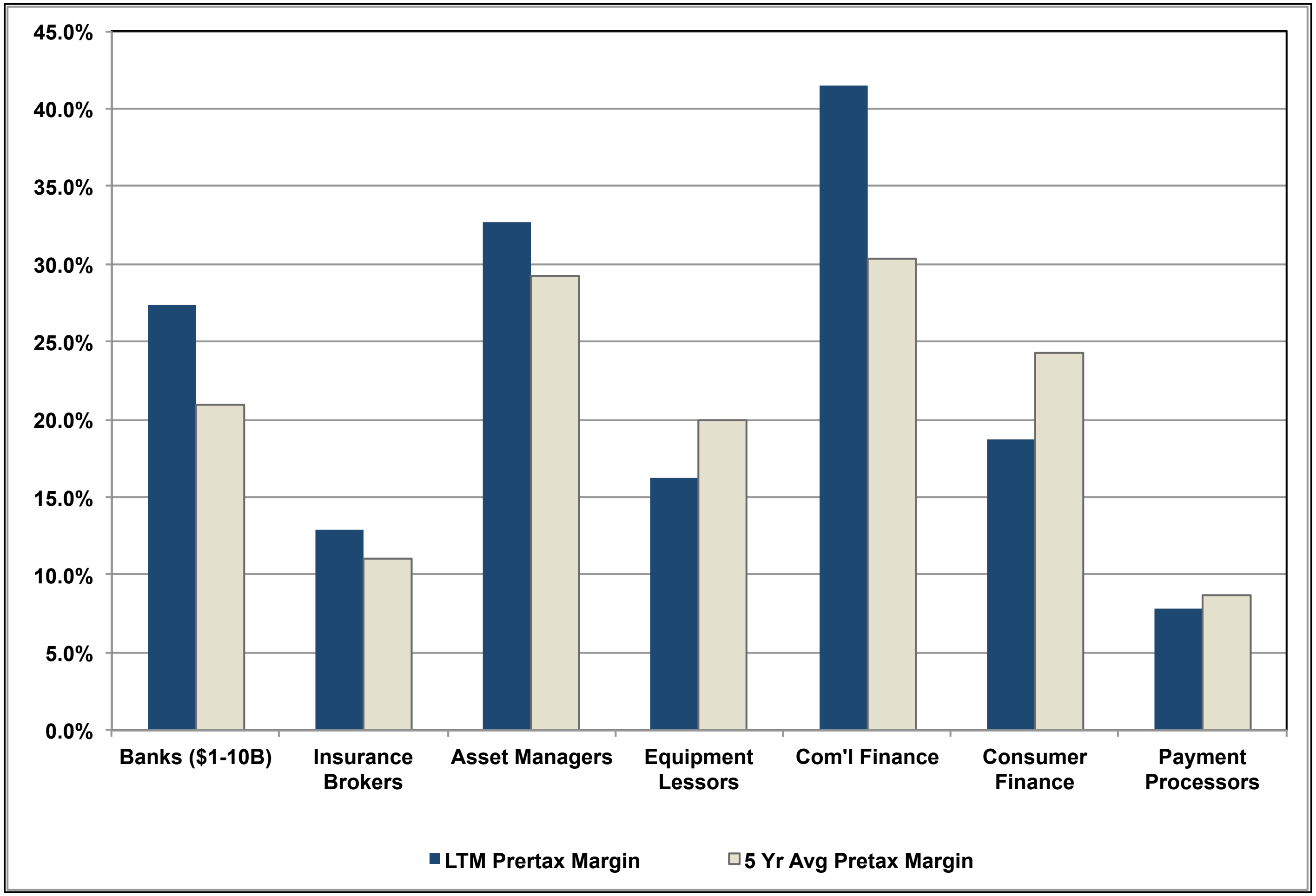
- Execution risks
- Culture
- Dilution (ownership, focus and franchise value)
- Enough scale to matter
- Contingent liabilities
- Will key principals still work hard?
- Limitations on the size of bank subsidiaries relative to the bank
- Regulatory pressure on banks as fiduciaries

Comparative ROEs



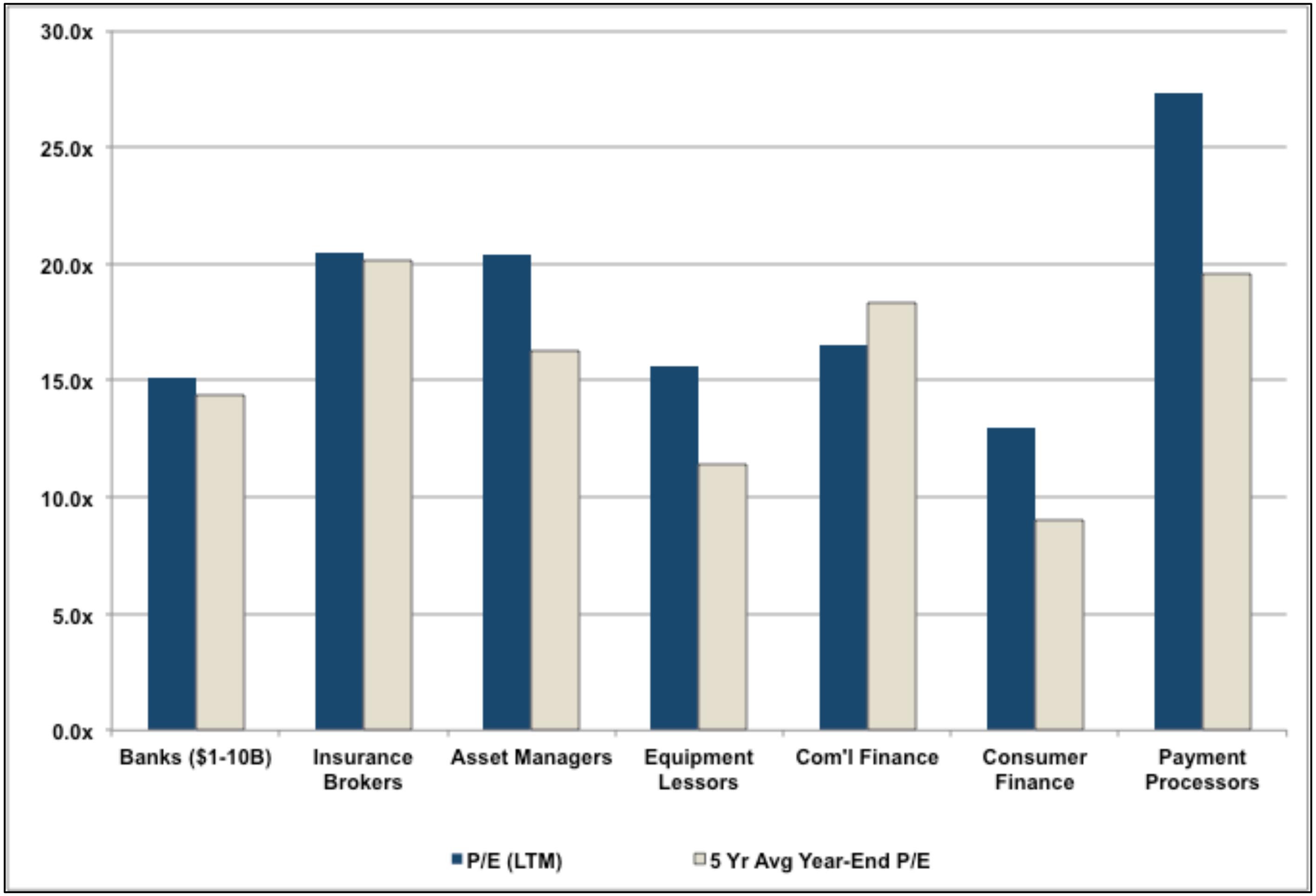
Source: SNL Financial

Comparative Pretax Margins



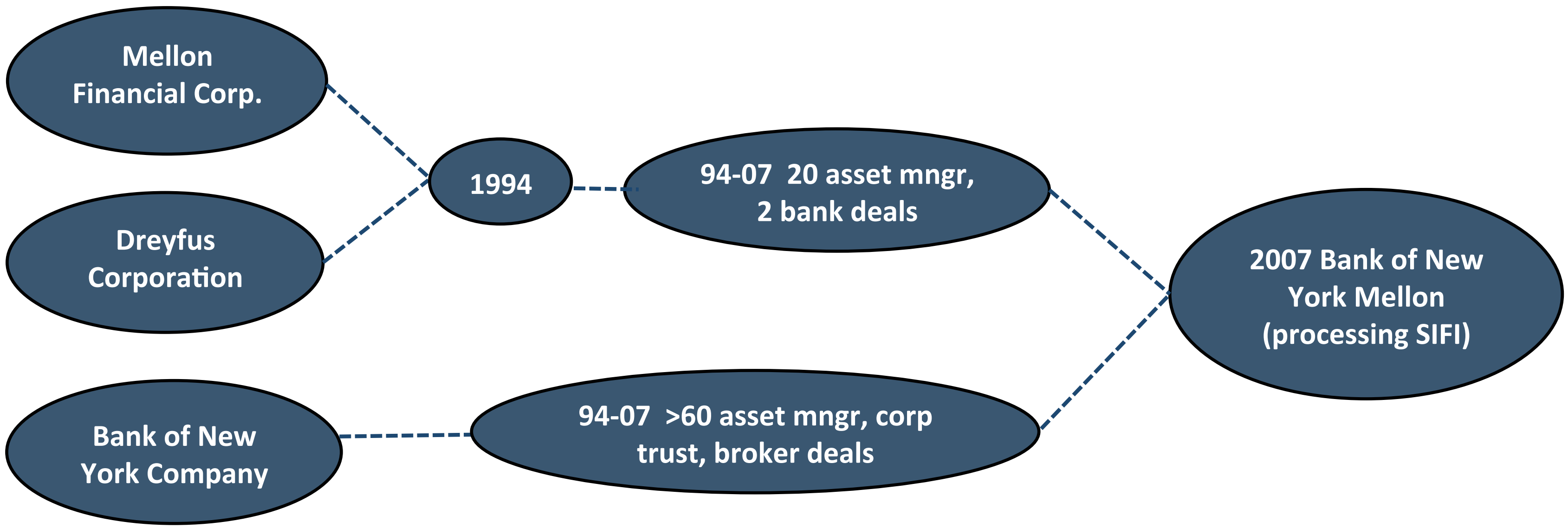
Source: SNL Financial

Comparative P/Es



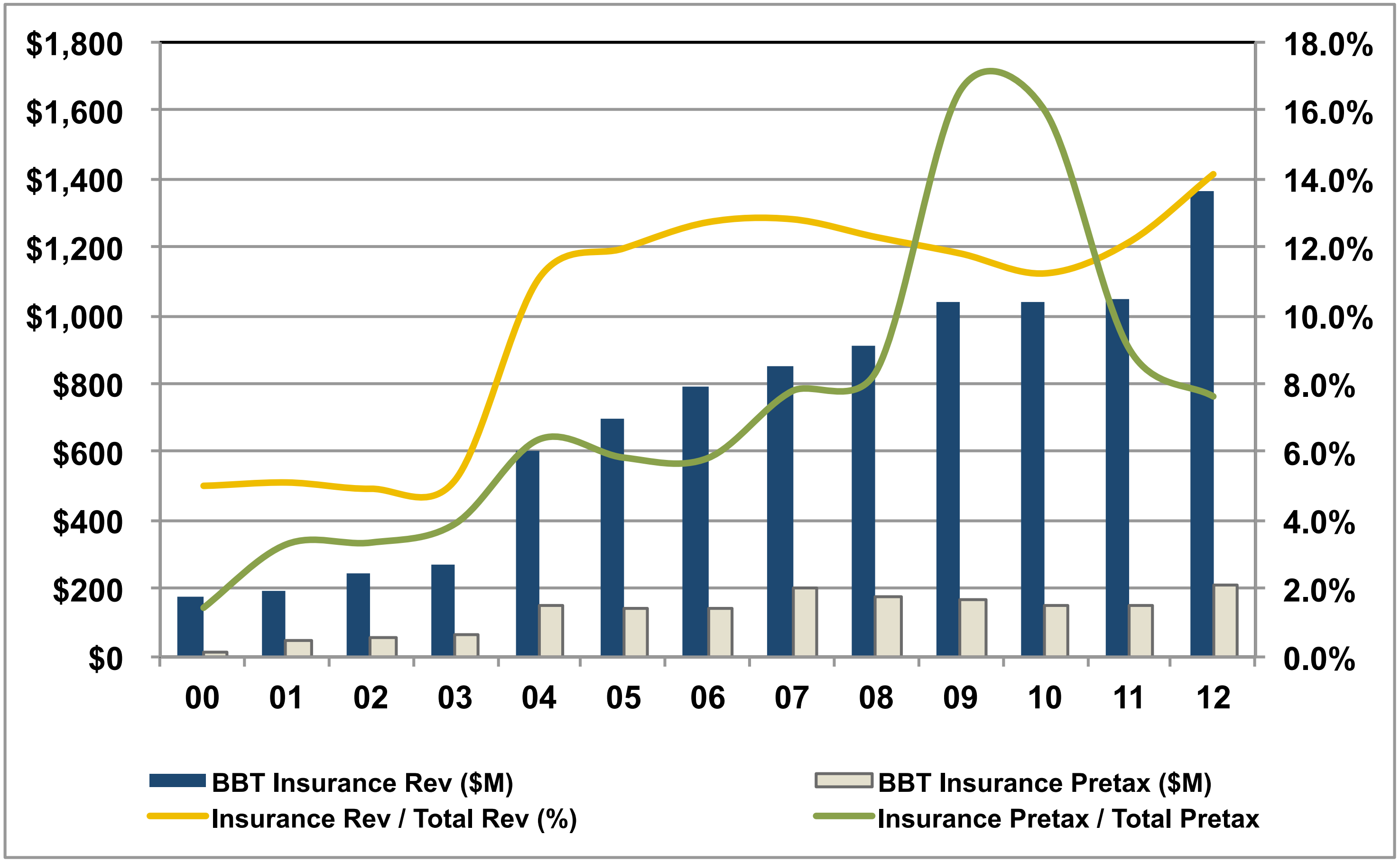
Source: SNL Financial

Bank of New York Mellon Transformation



... Not a transformation for most others

Evolution at the Margin?



… for BBT and some … yes

Key Items to Own

	Budget 2014	2013	2012	2011	2010
Revenue	$16,800	$14,200	$13,200	$12,800	$12,500
Y/Y Growth	18%	8%	3%	2%	14%
EBITDA	**$3,200**	**$2,750**	**$2,340**	**$2,125**	**$1,920**
Y/Y Growth	16%	18%	10%	11%	10%
Margin	19%	19%	18%	17%	15%
Adjustments					
1) Asset sale gain	75	50	-50	15	20
2) Lost Customer	600	400	350	350	300
Adj. Revenue	$16,125	$13,750	$12,900	$12,435	$12,180
Y/Y Growth	17%	7%	4%	2%	14%
Adj. EBITDA	**$2,525**	**$2,300**	**$2,040**	**$1,760**	**$1,600**
Y/Y Growth	10%	13%	16%	10%	12%
Margin	16%	17%	16%	14%	13%

Earning Power

- History vs. forecast
- No hockey sticks
- Concentrations
- Sustainability
- Margin drivers
- Careful w/ synergies
- Where is the business cycle?

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Key Items to Own

Derivation of Equity Discount Rate		
Long-Term Government Bond Yield-to-Maturity		2.75%
Common Stock Premium	5.50%	
x Guideline Beta	1.00	
= Beta Adjusted Common Stock Premium	5.50%	
+ Small Capitalization Stock Premium	2.80%	
= Total Equity Premium	==>	8.30%
+ Target Risk Premium		**5.00%**
= Equity Discount Rate (Required Rate of Return)		16.05%
Derivation of After-Tax Cost of Debt Capital		
Blended Future Avg Effective Interest Rate in Projection		5.00%
- Blended Effective Tax Rate	39%	-1.96%
= After-Tax Rate of Return on Debt Capital		3.04%
Weighted Equity Discount Rate	100%	16.05%
Weighted After-Tax Debt Cost	0%	0.00%
Weighted Average Cost of Capital		**16.05%**
- Perpetual Cash Flow		-2.00%
= Capitalization Rate Applicable to NOPAT		14.05%
= Capitalization Factor (1/Cap Rate)		**7.1x**

Cost of Capital

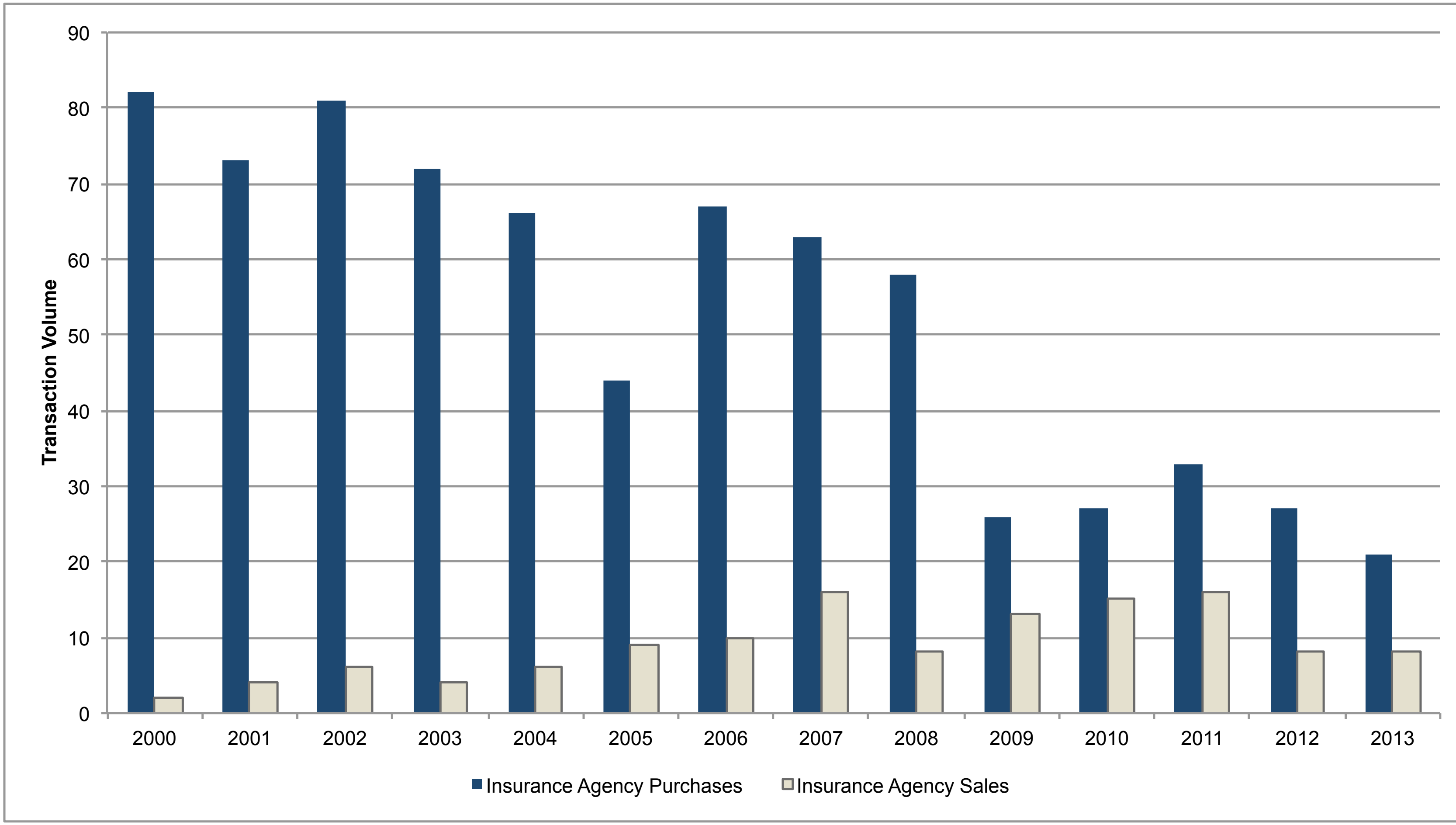
- Price risk
- Make the target clear a high hurdle rate, not the bank's cost of capital
- Remember:
  P/E x ROE = P/B

Insurance Agency Acquisitions

» The Old Goal: Cross-Selling Opportunity
  - Will being part of the bank create agency growth?
  - Will having the agency lead to more commercial lending opportunities?
  - Should you pay for these things?

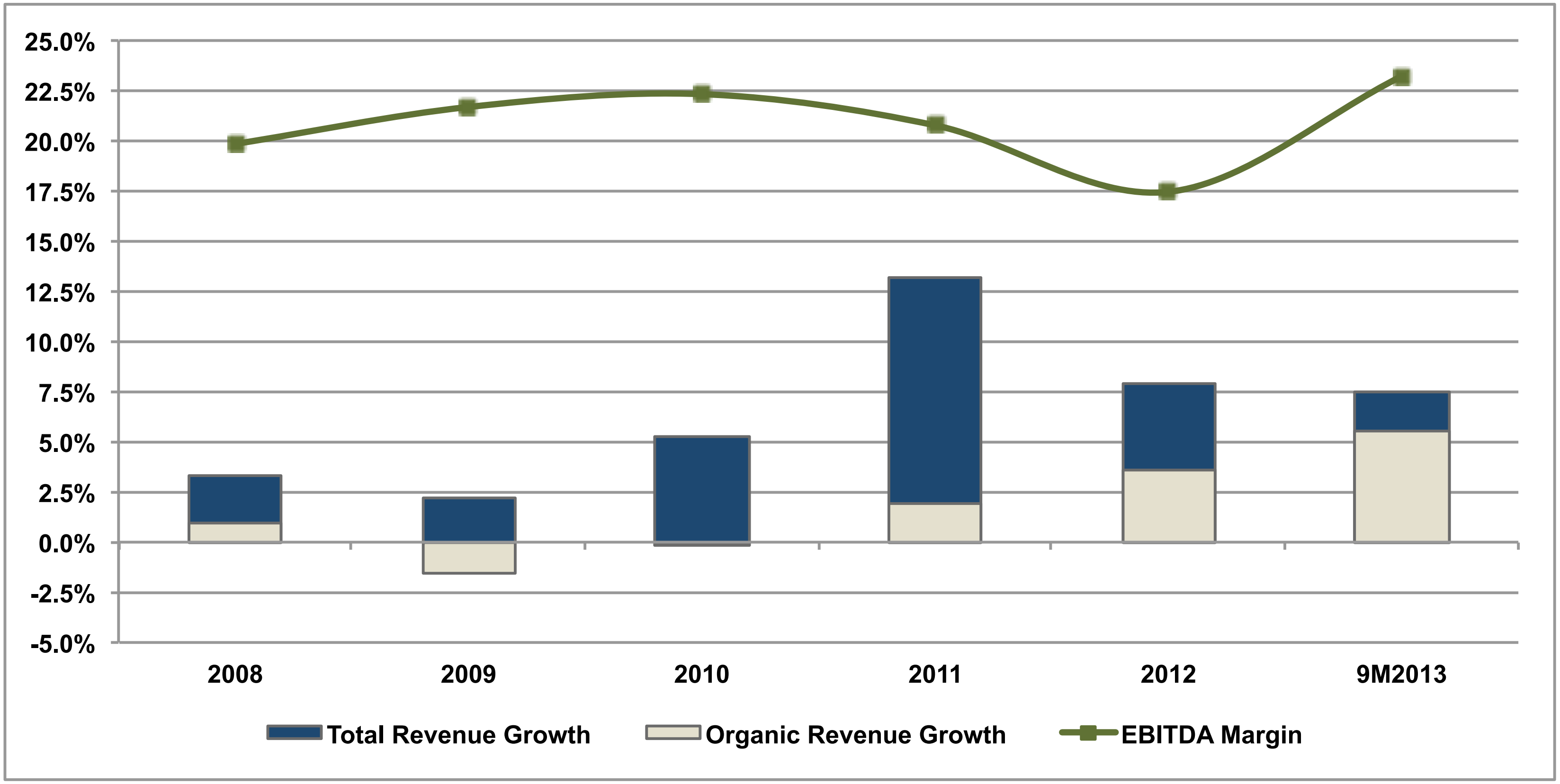
» A Better Goal: Contribution to Non-Interest Income
  - Diversify bank earnings
    » **More meaningful for community banks than larger institutions**
  - Generally stable, renewal-based revenue stream
  - Price based on agency fundamentals, not synergistic growth

Insurance Agency M&A: Bank activity stabilizing?



Source: SNL Financial. Includes whole agencies and asset deals

Public Brokers Showing Improved Fundamentals



Source: SNL Financial. Reflects average growth and margins for MMC, AON, WSH, AJG, BRO

Insurance Agency Earnings Model

- Revenue (mostly commission, some fee-based)
  - Driver #1: Rate (hard vs. soft market)
  - Driver #2: Exposure Units (macro/micro economic factors)
- Expenses
  - People (producers, managers, staff)
  - Overhead (marketing, rent, other)
- Growth and Scale
  - Organic – invest in new producers, products, geographies
  - Bolt-on agencies, books of business, renewal rights
  - Potential cross-selling opportunities

Insurance Agency Acquisitions:
Strategic Considerations for Banks

- Type and Amount of Capital Investment
  - Platform agencies (~7x-10x EBITDA)
  - Bolt-on agency (~5x-7x EBITDA)
  - Books of business (~0.5x-1.5x revenue)
- Geographic, demographic, product-line specific rationales
- Due Diligence Issues
  - Customer/producer/carrier concentrations
  - Quality of earnings
  - Technology, compliance issues
  - Culture
- Post-Deal Owner/Producer Compensation
  - Earn-outs, retention agreements, non-competes

Specialty Finance

- Promise – higher yielding loans funded with cheap/excess deposits; venue to diversify heavy CRE exposure

- If acquiring, must understand:
  - Origination model (direct, purchase, hybrid)
  - Seasonality and cyclical issues with originations
  - Pricing model and where the industry is in the pricing cycle
  - Loss model and loss cycle
  - Source of contingent liabilities

- Comfort with a broker origination model?

- If you have the option, initial deal should be small(ish) to learn

- Potential impact of the Consumer Financial Protection Bureau

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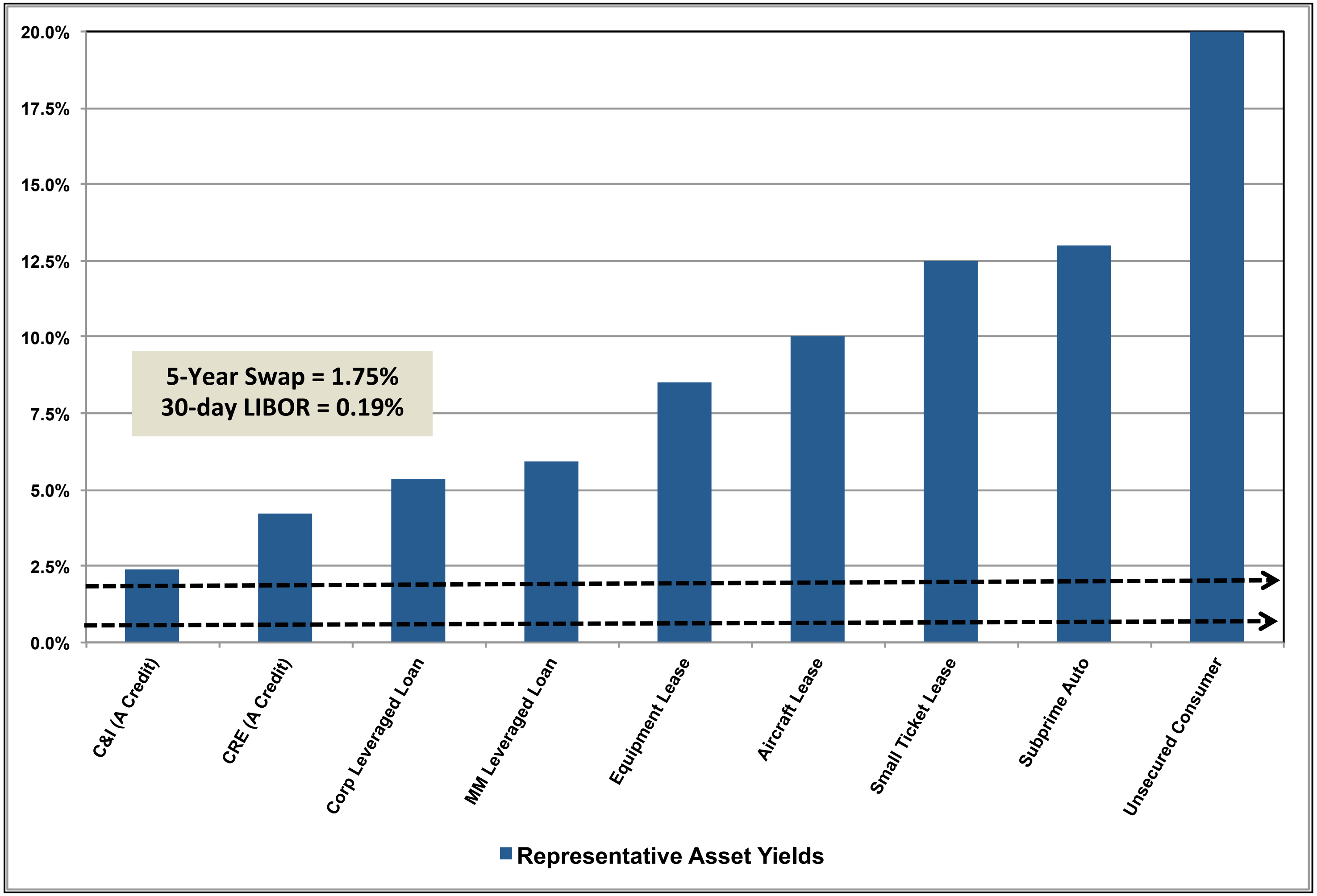
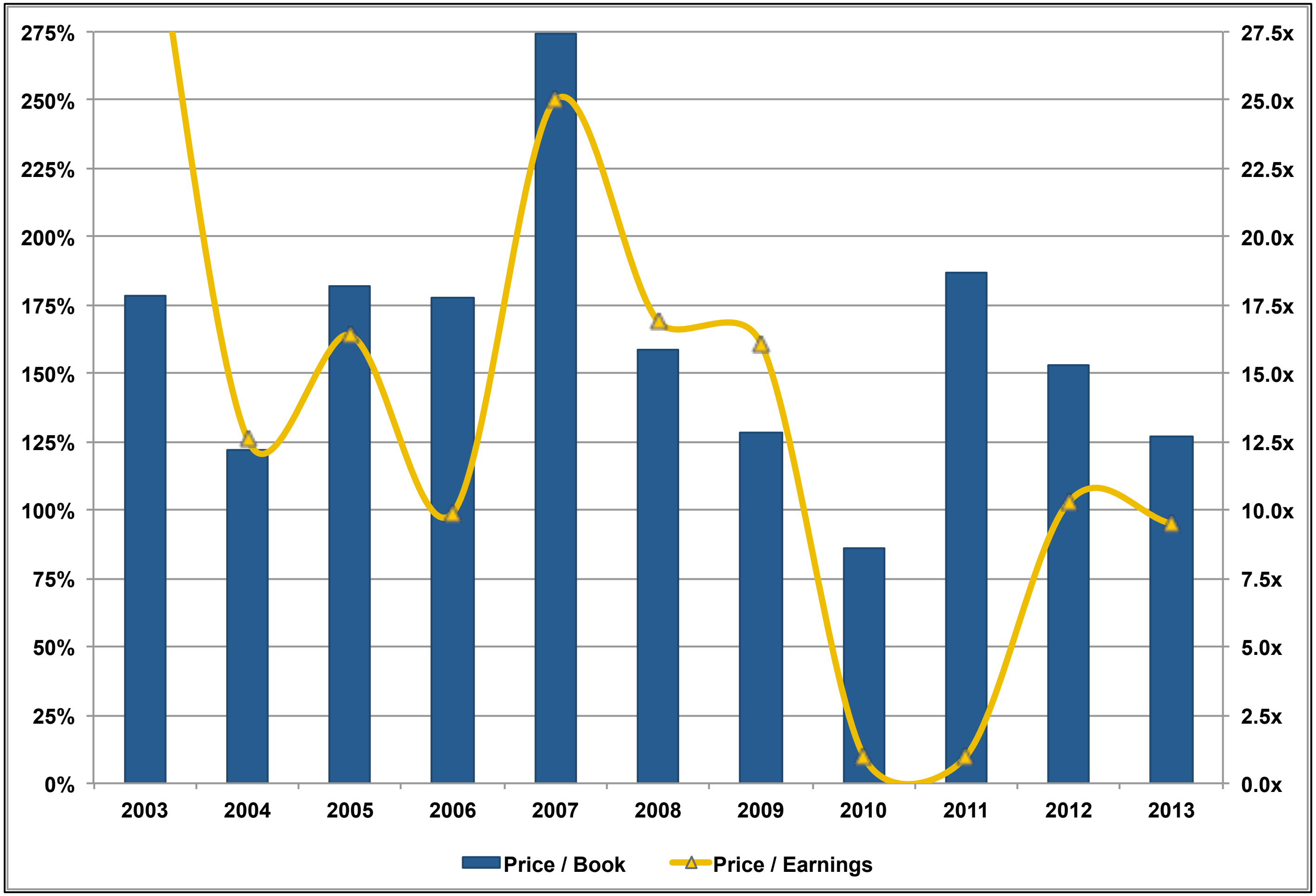
Yield Comparison



Specialty Finance Multiples



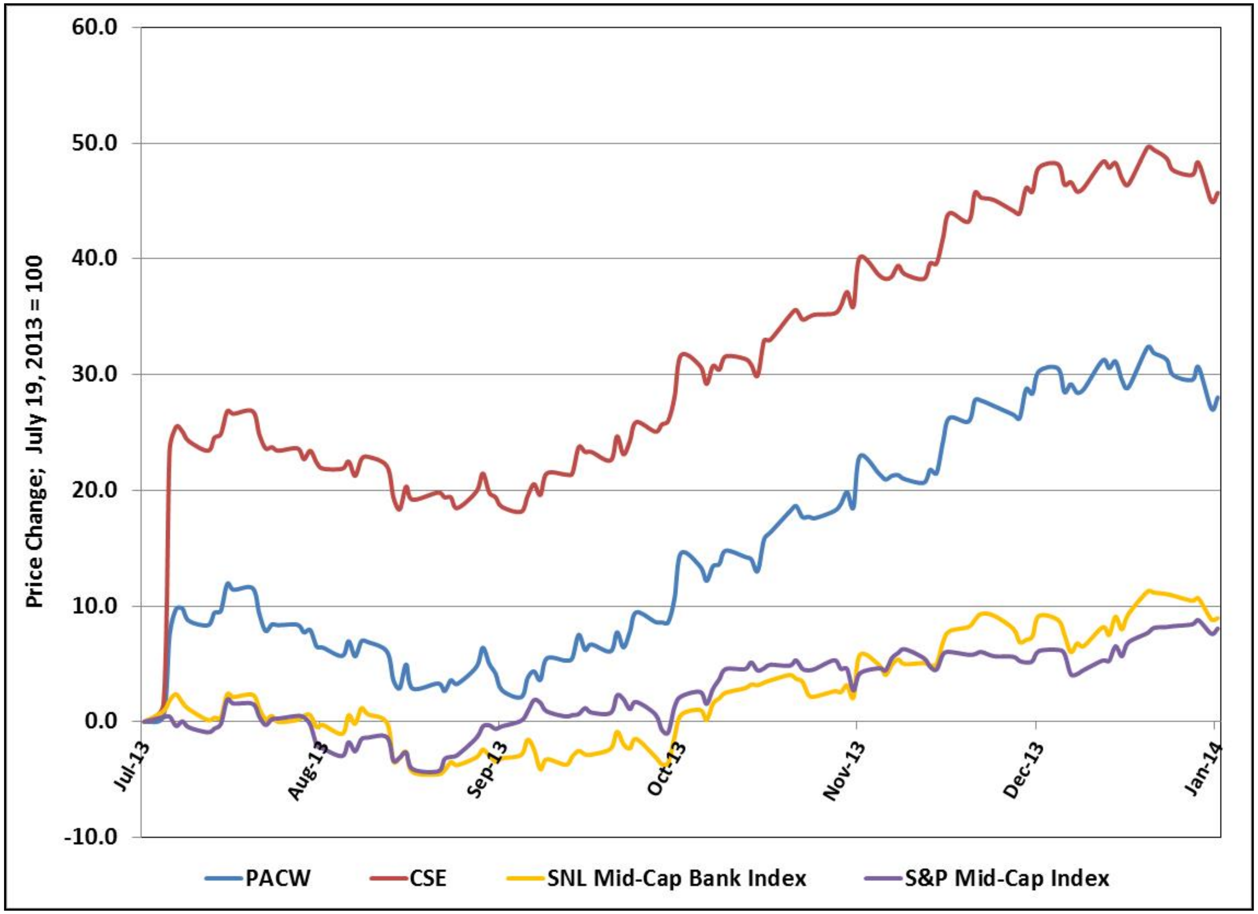
Source: SNL Financial

Specialty Finance

Announced	Buyer	Target	Focus	Price ($M)	P/B (%)	P/E (x)	P/Loans (%)	Comment
11/23/09	People's United Financial Inc.	Financial Federal Corp.	Equipment Lender	$738	163%	16.1x	49%	PBCT had excess liquidity, capital … got asset generator
1/3/12	PacWest Bancorp	Marquette Equipment Fin LLC	Diversified Commercial Lender	$35	NA	7.0x	NA	Avg yield 9% + portfolio diversification
4/3/12	PacWest Bancorp	Celtic Capital Corp.	Niche Commercial Lender	$18	NA	NA	33%	Asset-based lender... Avg line ~$2M, avg loan ~$900K
12/28/12	MB Financial Inc.	Celtic Leasing Corp.	Equipment Lender	$59	226%	NA	NA	$75M+ lease originations / yr … MBFI history w/leasing
6/4/13	Umpqua Holdings Corp.	Financial Pacific Holding Corp	Equipment Lender	$158	264%	8.2x	NA	Originates leases via brokers, avg ticket = $25k
11/18/13	Pacific Premier Bancorp	Infinity Franchise Holdings	Diversified Specialty Lender	$16	NA	NA	21%	Lender to fast food franchises …. CEO came from similar unit @ FFBC
7/22/13	PacWest Bancorp	CapitalSource	Commercial Finance	$2,300	150%	17.8x	NA	Transformative deal for PACW, ~6% loan yield @ CSE Bank … Deal to watch given size, synergies & culture

Source: SNL Financial and company presentations

PacWest Out-Performs with CapitalSource



Source: SNL Financial

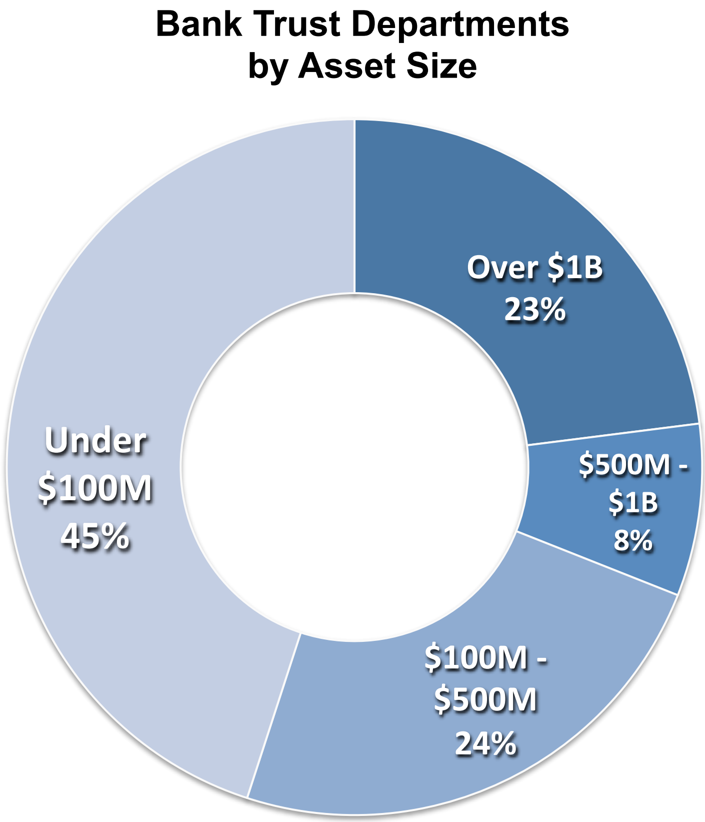
- Expected EPS accretion
- PACW FY14E June 2013 ~ $2.20 per share prior to the announcement of the CSE deal
- FY15E as of Jan 2014 ~$3.00 per share

Banks Interested in Asset Managers…

			AUM	Deal Value /				Deal Val.	Type of Consideration ($ Mil.)		
Announced	Acquirer	Target	($ Mil)	AUM/AUA (%)	Revenue	EBITDA	Net Inc.	(S Mil.)	Cash	Stock	Earnout
02/21/2011	IBERIABANK Corporation	Bank of Florida Trust Company	415	0.30	0.78	NA	NM	1.4	0.7	NA	0.7
02/03/2012	Bryn Mawr Bank Corporation	Davidson Trust Company	1,000	1.05	NA	NA	NA	10.5	7.4	NA	3.2
10/31/2012	Atlas Banc Holdings Corp.	Halen Capital Management, Inc.	NA	NA	NA	NM	NM	0.1	NA	NA	NA
12/6/12	Toronto-Dominion Bank	Epoch Holding Corporation	24,534	2.77	6.54	13.23	23.53	668.4	664.1	NA	NA
04/28/2011	Bank of New York Mellon Corporation	Talon Asset Mgmt. (Wealth Mgmt Dept.)	800	2.00	NA	NA	NA	16.0	11.0	NA	5.0
04/11/2013	Canadian Imperial Bank of Commerce	Atlantic Trust Group, Inc.	NA	1.03	NA	NA	NA	210.0	NA	NA	NA
02/15/2013	New Hampshire Thrift Bancshares	Charter Holding Corp.	NA	0.83	NA	NA	NA	6.2	NA	NA	NA
10/1/11	Wells Fargo & Company	Golden Capital Management, LLC	2,918	NA	NA	NA	NA	NA	NA	NA	NA
04/05/2010	Legacy Bancorp, Inc.	Renaissance Investment Group, LLC	195	NA	NA	NA	NA	NA	NA	NA	NA
8/29/11	U.S. Bancorp	Institutional Trust Business of Union Bank	NA	NA	NA	NA	NA	NA	NA	NA	NA
10/09/2012	Orange County Bancorp, Inc.	Hudson Valley Investment Advisors, LLC	272	NA	NA	NA	NA	NA	NA	NA	NA
1/8/13	Tri-State Capital Holdings, Inc.	Chartwell Investment Partners, L.P.	7,500	0.80	2.00	6.96		60.0	45.0	9.0	15.0
			Median Multiples Paid	**1.03**	**2.00 x**	**10.10 x**					

Trust Departments: Build-up or Shut-down?

- Roughly 1,500 Banks have trust departments
  - But only ~30% are large enough to be consistently profitable (>$500MM)
- Roughly 10,500 Registered Investment Advisers (RIAs)
  - But only ~40% are large enough to be consistently profitable (>$500MM)



Asset management can be attractive…

- Enhance non-interest fee income – easily accretive
- Asset management revenue has different market sensitivity – lowering overall revenue risk to changes in interest rates
- Asset management has minimal capital requirements – improving ROE
- Asset management has attractive internal rates of return – recurring revenue stream and substantial margins
- Leverages bank model as a distributor of financial services – through financial intermediaries like trust, other RIAs, broker-dealers, and family offices

In both cases, assets drive earnings, but returns to capital and labor vary widely

Bank Economics

Earning Assets	$1,000,000,000
x Net Interest Margin	3.50%
= Revenue	$35,000,000
- Operating Expenses*	30,000,000
= Pre-Tax, Pre-Provision Income	$5,000,000
Implied Margin	*14.3%*
Required Equity Capital	$100,000,000
* ~250 Employees, 15 branches	
Implied Profit Per Employee	*$20,000*

Asset Manager Economics

AUM/AUA/AUC	$1,000,000,000
x Realized Fee Schedule	0.60%
= Revenue	$6,000,000
- Operating Expenses**	4,000,000
= Operating Income (EBIT)	$2,000,000
Implied Margin	*33.3%*
Required Equity Capital	$1,000,000
** < 20 employees, one office	
Implied Profit Per Employee	*$100,000*

Both exhibit revenue sensitivity to the market, but in different ways

For Banks…

- Net Interest Margin affected by loan and deposit pricing competition, shape of the yield curve, mix of loans vs. bonds, and deposit vs. wholesale funding
- Volume of assets generally unaffected by market

For Asset Managers…

- AUM primarily affected by market conditions
- Fee schedule typically changes little over time

Pro: Can determine run-rate profitability every day

Con: Can't forecast reliably because market direction is unknowable

Pricing of services works very differently…

Banks

» Net Interest Margin

Asset Managers

» Realized Fee Schedule

- Graduated for larger accounts
- Often negotiated
- Fairly consistent over time

» Fee schedules NEVER improve

» Indexing and ETFs haven't put pressure on active management fees yet…

…but asset attrition matters to both

Banks

- Scheduled Asset Attrition
  - Loan Amortization
- Unscheduled Asset Attrition
  - Refinancing

Asset Managers

- Scheduled Distributions
  - Trust / endowment payouts
  - Pension obligations
  - Older clients spend down assets
- Unscheduled Asset Attrition
  - Manager termination
  - Asset allocation rebalancing

- Asset Attrition is real

Sometimes failures of marketing are masked by the success in the market…

	2013	2012	2011	2010	2009	Cumulative
Starting Assets Under Management (AUM)	**1,237,500,000**	**1,172,500,000**	**1,140,000,000**	**1,110,000,000**	**1,000,000,000**	
New Business	5,000,000	0	10,000,000	15,000,000	5,000,000	**35,000,000**
Client Contributions (Withdrawals)	10,000,000	5,000,000	7,500,000	(5,000,000)	(15,000,000)	**2,500,000**
Terminations	(15,000,000)	(20,000,000)	(15,000,000)	(55,000,000)	(30,000,000)	**(135,000,000)**
Net Business Gained / Lost	**0**	**(15,000,000)**	**2,500,000**	**(45,000,000)**	**(40,000,000)**	**(97,500,000)**
Change in Market Value	**150,000,000**	**80,000,000**	**30,000,000**	**75,000,000**	**150,000,000**	**485,000,000**
Ending AUM (Starting AUM + Net Flows + Δ in MV)	**1,387,500,000**	**1,237,500,000**	**1,172,500,000**	**1,140,000,000**	**1,110,000,000**	
Management Fee Revenue	$7,000,000	$6,300,000	$6,100,000	$6,000,000	$5,750,000	
÷ Average AUM	1,312,500,000	1,205,000,000	1,156,250,000	1,125,000,000	1,110,000,000	
= Approximate Realized Fee	0.53%	0.52%	0.53%	0.53%	0.52%	

Both business models are labor intensive, but in different ways

Banks are labor intensive

- Lots of people

Asset managers are labor intensive

- Expensive people
- Ties back to profit per person

- Primary source of cultural conflict
- Commonly represents 70% to 80% of operating expenses

Asset managers complain about regulation, until they learn what bankers endure…

Bank Regulatory Capital

- High and rising (?)

Asset Manager Regulatory Capital

- Varies, and is rising
- But still minimal by comparison
- Much more significant for trust services

For both, scale matters…

Scale matters for Banks

- Hence this conference

Scale matters for Asset Managers

- Scale >> Margin >> Risk
- Operating leverage play: to a point
- $300MM AUM to be viable
- $500MM AUM to be consistently profitable
- Margins tend to max out between $3B and $5B AUM

- Operating leverage is often over-promised and over-forecast

Although the P&L starts with assets, value is a function of earnings

Banks

- Just as bank transactions are cited in terms of price to book…

Asset Managers

- ... Asset manager transactions are often disclosed as price to AUM
  - But “Activity” metrics are commonly misleading
  - And whisper numbers are often overstated
    - Earnouts included as if fully earned and undiscounted
    - Actual multiples paid are rarely reported

- Total consideration usually 6x-12x EBITDA

But deal structure in asset managers is very different from bank transactions

Banks

» Earnouts are very rare in bank transactions

Asset Managers

» Earnouts are the norm in asset manager transactions
  - Relational, performance based business
  - Commonly 30%-50% of deal value

» Don't pay twice!

And due diligence is very different…

Banks

- Bank acquisition due diligence focuses on downside protection
  - Credit risk
  - Compliance

Asset Managers

- Asset manager acquisition due diligence focuses on upside protection
  - Clients must consent to move accounts
  - Staff retention maintains intellectual capital and relationships
  - 3rd party verification of investment performance

- Audits from a reputable firm and 3rd party custody of client assets

Tri-State Capital announces purchase of Chartwell Investment Partners (January 8, 2014)

- Tri-State Capital Holdings (TSC)
  - Pittsburgh bank with assets of $2.2 billion and equity of $290 million
  - IPO last year; implied market capitalization of ~$350MM
  - No-branch model looking for ways to leverage bank for high value added relationships in a financial services distribution model
- Chartwell Investment Partners
  - Founded 1997 and based in Philadelphia area
  - Provides Small to Mid-Cap Equity and fixed income management for ~ 150 institutional and private investors
  - Mutual Fund Product – Chartwell Small Cap Value Fund (CWSVX)

TSC acquisition of Chartwell

	Disclosed 2013E	Est. Ongoing	
Average AUM for 2013	$6,310,000,000	na	Approximate; Disclosed
Current AUM	na	$7,500,000,000	Approximate; Disclosed
Realized Average Fee	0.396%	0.400%	Higher fees on Equity AUM
Revenue	$25,000,000	$30,000,000	Revenue grows with AUM
Implied Operating Expense	$19,000,000	$21,375,000	Assumes 12.5% Δ in Ongoing OpX
EBITDA	$6,000,000	$8,625,000	2013 Disclosed; Implied Ongoing
EBITDA Margin	*24.0%*	*40.4%*	2013 Disclosed; Implied Ongoing
Initial Consideration	$45,000,000	$45,000,000	Disclosed
Earnout	na	15,000,000	Earnout if 2014 EBITDA > $8.5MM
Total Consideration	$45,000,000	$60,000,000	Earnout likely to be paid
Implied Multiple	*7.5*	*7.0*	Earnout 6x Δ in EBITDA

TSC acquisition of Chartwell

For TSC

- Diversified revenue
- Added non-interest income
- Capital commitment minimal
- Accretive to earnings
- Styles the bank as upscale distributor of value-added financial services

For CIP

- Owners take money off the table, but stay involved
- Upside potential if they can tap bank's client base to distribute products through other channels
- Earnout all but assured

Final Thoughts

- **#1 determinant of return that investors and buyers control is the purchase price**
- Don’t lie to yourself to win the deal
- Price cures price … margin of safety matters
- Realistic assessment of the target’s earning power and synergies
- Do not let other peoples problems become your problem
- Credit businesses are always cyclical – price accordingly

Q & A

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