Return of the Large and Super Regional Buyers?

It is sort of like the pre-crisis days, but not really. Bank acquisition activity involving non-assisted transactions has been gradually building since the financial crisis. The only notable interruption occurred in the second half of 2011 when the downgrade of the U.S. by S&P (but not Moody’s or Fitch) and a funding crisis among many European banks caused markets to fall sharply.

As of November 14, 260 bank and thrift acquisitions had been announced this year according to SNL Financial, which compares to 246 deals for all of 2013. Pricing continues to gradually improve too. The year-to-date average P/TVB is 135% compared to 120% in 2013 and 116% in 2012. In a sense, a declining median P/E points to higher valuations because sellers as a group are posting better profitability than several years ago. The median P/E ratio this year is about 28x compared to 23x in 2013 and 34x in 2012. Figures 1 and 2 on page 3 highlight some of these comparisons for deals both in 2014 and from 2009-2013. Although it will be a subject for a later post in BankWatch, we believe most buyers are paying roughly 10-13x the buyer’s normalized earnings with after-tax cost saves and normalized credit costs.

The heyday of M&A activity for investors was the 1990s when over 500 bank and thrift deals were announced in 1994 and 1998. Deal activity peaked last decade at 323 in 2007. Not coincidentally, cycle peaks in public market bank valuations occurred near the peaks in M&A activity in 1998 and 2007. When viewed as a percent of banks at the beginning of each year, deal activity has been relatively steady with 3-4% of banks being absorbed through acquisition, with the exception of 2008, 2009 and 2011.

One notable aspect of the bank M&A market since the financial crisis has been the absence of larger acquirers other than periodic deals. The primary reason cited has been regulatory challenges as large banks implement tough compliance requirements as part of Dodd-Frank and other regulatory mandates that emerged from the 2008-2009 financial crisis. Also, many bankers and corporate securities attorney have publicly commented (and to us) that the Fed does not want to see merger applications from the largest banks; rather, they want consolidation to occur from the bottom rather than the top of the industry.

M&T Bank Corporation (MTB) remains the poster-child for the industry in terms of what can go awry with a merger application when a compliance issue emerges. M&T announced a deal to acquire then $44 billion asset Hudson City Bancorp on August 27, 2012 for $3.8 billion as shown in Figure 2. Over two years later the deal remains pending due to compliance issues that emerged for M&T, including
some issues related to its 2011 acquisition of Wilmington Trust Corporation. Although on a smaller scale, BancorpSouth (BXS) recently extended by about a year the date of two definitive agreements it had entered into to acquire community banks in Louisiana and Texas due to compliance issues that emerged after the definitive agreements were signed.

CEO Richard Davis of US Bancorp (USB) has opined that acquisitions by larger banks will be episodic and focused like USB’s acquisition of Citizen Financial Group’s Chicago franchise earlier this year rather a broad-based trend. Nevertheless, the return of BB&T Corporation (BBT) to the acquisition market this year may signal larger banks are becoming more comfortable with their regulatory standing to resume acquisitions. In late 2013 BB&T announced a deal to acquire 22 Texas offices from Citigroup Inc. (C); it then announced a second purchase for 41 Texas branches in September. Within a week BB&T announced a $367 million deal for Bank of Kentucky Financial Corporation (BFKY). In November, it announced a $2.5 billion acquisition of Pennsylvania-based Susquehanna Bancshares (SUSQ). See Figure 1 for other details of these transactions.

The largest transaction announced year-to-date is CIT Group’s (CIT) $3.4 billion deal for IMB HoldCo, a privately-held entity that formed OneWest Bank from the failed IndyMac Bank, as shown in Figure 1. The transaction may be an outlier because CIT was under pressure from the Federal Reserve to build a core deposit franchise that does not yet exist in subsidiary CIT Bank, which traces its roots to a Utah industrial loan charter.

We do not know whether Davis is right about large bank M&A activity being episodic rather than on the cusp of picking-up. What is apparent is that the operating environment for banks remains challenging with pressure on NIMs, increasing regulatory costs and limited opportunities to improve fee income. As a result, we see no reason deal activity will slow from the 3-4% of the industry being absorbed each year other than as a result of a sharp drop in markets and/or a downturn in credit. The return of BB&T and the addition of the likes of First Horizon National Corporation (FHN) should, at the margin, support activity and maybe pricing to the extent it supports investor and banker confidence in the sector.

Recent Bank Speech

Issues, Trends and Developments in Banking Industry Valuations

With the banking industry facing new regulations and other pressures, this session focuses on the current environment at banks and valuation techniques appropriate for rendering valuation opinions that are consistent with this environment. Attendees will:

» Understand the current environment facing depository institutions and its effect on their valuation
» Appreciate unique factors affecting the valuation of depository institutions that are not present in the valuation of non-financial companies
» Identify and execute valuation methodologies consistent with this environment

Download the slides at http://mer.cr/1EVqRRf.

What We're Reading

Elizabeth Dexheimer of Bloomberg wrote an article on today’s changing market with mergers and acquisitions following the financial crisis.
http://mer.cr/1qOVfo3

Jeff Davis of Mercer Capital has interesting article taking a look at key takeaways from the Federal Reserve’s 2014 Shared National Credit exam nuggets.
http://mer.cr/1sNzBAm

Al Dominick of Bank Director has a nice article discussing the importance of earnings in measuring a bank’s value.
http://mer.cr/1vkNX1Z

Emily McCormick of Bank Director has the preliminary findings of Bank Director’s 2015 Bank M&A Survey.
http://mer.cr/1Hah3oE

John Allison, CEO of the Cato Institute and former chairman and CEO of BB&T, has an interesting series on “Creating a Win-Win in M&A.” Part 1 of the series talks about his logic for bank’s to consider in using M&A as part of a growth strategy.
http://mer.cr/1qetkDs
## Figure 1: Top 12 Bank Deals for 2014

<table>
<thead>
<tr>
<th>Announce Date</th>
<th>Buyer</th>
<th>Seller</th>
<th>Seller Assets ($M)</th>
<th>Deal Value ($M)</th>
<th>Price/ TBV (%)</th>
<th>Price/ Net Inc. (x)</th>
</tr>
</thead>
<tbody>
<tr>
<td>7/22/14</td>
<td>CIT Group Inc.</td>
<td>IMB HoldCo LLC</td>
<td>21,807</td>
<td>3,369</td>
<td>102</td>
<td>13.7</td>
</tr>
<tr>
<td>11/12/14</td>
<td>BB&amp;T Corp.</td>
<td>Susquehanna Bancshares Inc.</td>
<td>18,583</td>
<td>2,501</td>
<td>172</td>
<td>16.6</td>
</tr>
<tr>
<td>11/5/14</td>
<td>Banner Corp.</td>
<td>Starbucks Bancshares Inc.</td>
<td>4,087</td>
<td>702</td>
<td>148</td>
<td>37.5</td>
</tr>
<tr>
<td>6/10/14</td>
<td>First Citizens Bancshares Inc.</td>
<td>First Citizens Bancorp.</td>
<td>8,532</td>
<td>676</td>
<td>118</td>
<td>14.2</td>
</tr>
<tr>
<td>11/5/14</td>
<td>Sterling Bancorp</td>
<td>Hudson Valley Holding Corp.</td>
<td>3,120</td>
<td>538</td>
<td>188</td>
<td>NM</td>
</tr>
<tr>
<td>9/8/14</td>
<td>BB&amp;T Corp.</td>
<td>Bank of Kentucky FinCorp.</td>
<td>1,858</td>
<td>367</td>
<td>218</td>
<td>17.4</td>
</tr>
<tr>
<td>10/29/14</td>
<td>WesBanco Inc.</td>
<td>ESB Financial Corp.</td>
<td>1,945</td>
<td>353</td>
<td>214</td>
<td>19.8</td>
</tr>
<tr>
<td>4/29/14</td>
<td>Southside Bancshares Inc.</td>
<td>OmniAmerican Bancorp Inc.</td>
<td>1,391</td>
<td>314</td>
<td>152</td>
<td>43.6</td>
</tr>
<tr>
<td>5/8/14</td>
<td>Valley National Bancorp</td>
<td>1st United Bancorp Inc.</td>
<td>1,738</td>
<td>313</td>
<td>187</td>
<td>36.1</td>
</tr>
<tr>
<td>1/27/14</td>
<td>Yadkin Financial Corporation</td>
<td>VantageSouth Bancshares</td>
<td>2,046</td>
<td>299</td>
<td>147</td>
<td>49.6</td>
</tr>
<tr>
<td>7/15/14</td>
<td>TowneBank</td>
<td>Franklin Financial Corp.</td>
<td>1,095</td>
<td>278</td>
<td>115</td>
<td>23.1</td>
</tr>
</tbody>
</table>

Source: SNL Financial Data, as of November 14, 2014

## Figure 2: Top 12 Bank Deals for 2009-2013

<table>
<thead>
<tr>
<th>Announce Date</th>
<th>Buyer</th>
<th>Seller</th>
<th>Seller Assets ($M)</th>
<th>Deal Value ($M)</th>
<th>Price/ TBV (%)</th>
<th>Price/ Net Inc. (x)</th>
</tr>
</thead>
<tbody>
<tr>
<td>6/16/11</td>
<td>Capital One Financial Corp.</td>
<td>ING Bank FSB</td>
<td>92,222</td>
<td>9,000</td>
<td>102</td>
<td>31.9</td>
</tr>
<tr>
<td>12/17/10</td>
<td>Bank of Montreal</td>
<td>Marshall &amp; Isley Corp.</td>
<td>51,887</td>
<td>4,096</td>
<td>98</td>
<td>NM</td>
</tr>
<tr>
<td>8/27/12</td>
<td>M&amp;T Bank Corp.</td>
<td>Hudson City Bancorp Inc.</td>
<td>43,590</td>
<td>3,813</td>
<td>85</td>
<td>NM</td>
</tr>
<tr>
<td>6/20/11</td>
<td>PNC Financial Services Group</td>
<td>RBC Bank (USA)</td>
<td>27,376</td>
<td>3,450</td>
<td>97</td>
<td>NM</td>
</tr>
<tr>
<td>7/22/13</td>
<td>PacWest Bancorp</td>
<td>CapitalSource Inc.</td>
<td>8,483</td>
<td>2,382</td>
<td>177</td>
<td>5.4</td>
</tr>
<tr>
<td>9/11/13</td>
<td>Umpqua Holdings Corp.</td>
<td>Sterling Financial Corp.</td>
<td>9,940</td>
<td>1,995</td>
<td>173</td>
<td>19.1</td>
</tr>
<tr>
<td>3/12/12</td>
<td>Mitsubishi UFJ Finl Grp Inc</td>
<td>Pacific Capital Bancorp</td>
<td>5,850</td>
<td>1,516</td>
<td>225</td>
<td>21.5</td>
</tr>
<tr>
<td>8/19/10</td>
<td>First Niagara Finl Group</td>
<td>NewAlliance Bancshares Inc.</td>
<td>8,712</td>
<td>1,498</td>
<td>165</td>
<td>24.6</td>
</tr>
<tr>
<td>12/22/10</td>
<td>Hancock Holding Co.</td>
<td>Whitney Holding Corp.</td>
<td>11,517</td>
<td>1,486</td>
<td>164</td>
<td>NM</td>
</tr>
<tr>
<td>1/18/11</td>
<td>Comerica Inc.</td>
<td>Sterling Bancshares Inc.</td>
<td>5,040</td>
<td>1,029</td>
<td>232</td>
<td>NM</td>
</tr>
<tr>
<td>9/13/12</td>
<td>FirstMerit Corp.</td>
<td>Citizens Republic Bancorp Inc.</td>
<td>9,670</td>
<td>943</td>
<td>130</td>
<td>2.6</td>
</tr>
<tr>
<td>5/24/13</td>
<td>Banco de Credito e Inversiones</td>
<td>CM Florida Holdings Inc.</td>
<td>4,609</td>
<td>881</td>
<td>191</td>
<td>14.5</td>
</tr>
</tbody>
</table>

Source: SNL Financial Data, as of November 14, 2014
Mercer Capital’s Resources for Depository Institutions

The Financial Institutions Group of Mercer Capital works with hundreds of depository institutions and other financial institutions annually providing a broad range of specialized resources for the financial services industry.

Newest Webinar

An Introduction to Business Development Companies

In the hunt for yield, investors are increasingly setting their sights on business development companies (BDCs), which offer stock market investors access to portfolios of private equity investments. This webinar explored the features that have contributed to the growth in BDCs, underlying asset classes to which BDCs offer investors exposure, and highlighted the key performance metrics for evaluating BDCs. Our panel discussed relevant regulatory developments affecting BDCs, reviewed the portfolio valuation procedures and assumptions that influence quarterly profits, and explored the relative performance of key market benchmarks.

View webinar on SNL Financial’s site at http://mer.cr/ZnauO7
Complimentary Download of Slides at http://mer.cr/1tuwzal

Webinars Available for Replay

<table>
<thead>
<tr>
<th>An Overview of the Leveraged Lending Market and Bank Participation in the Market</th>
<th>Understanding Deal Considerations</th>
<th>Basel III Capital Rules Finally Final: What Does It Mean for Community Banks?</th>
</tr>
</thead>
<tbody>
<tr>
<td>There has been a flurry of media reports this year that regulators—especially the OCC—are intensifying scrutiny of leveraged lending. In this webinar we took a look at one of the fastest growing markets that has emerged post crisis.</td>
<td>Key issues that we see when banks combine as it relates to valuing and evaluating a combination are reviewed. This is particularly critical when the consideration consists of shares issued by a buyer (or senior merger partner) whose shares are either privately held or are thinly traded.</td>
<td>Finalized at last, the regulations provide direction for bank capital management decisions. This webinar, co-sponsored by Mercer Capital and Jones Day, reviews the final rules and assesses their impact on community banks.</td>
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Mercer Capital’s Public Market Indicators

November 2014

Mercer Capital’s Bank Group Index Overview

Return Stratification of U.S. Banks
by Asset Size

Median Valuation Multiples

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<tr>
<th>Indices</th>
<th>Month-to-Date</th>
<th>Quarter-to-Date</th>
<th>Year-to-Date</th>
<th>Last 12 Months</th>
<th>Price/ LTM EPS</th>
<th>Price / 2014 EPS</th>
<th>Price / 2015 (E) EPS</th>
<th>Price / Book Value</th>
<th>Price / Tangible Book Value</th>
<th>Dividend Yield</th>
</tr>
</thead>
<tbody>
<tr>
<td>Atlantic Coast Index</td>
<td>8.53%</td>
<td>8.53%</td>
<td>7.45%</td>
<td>13.41%</td>
<td>16.55</td>
<td>19.68</td>
<td>14.68</td>
<td>108.8%</td>
<td>119.4%</td>
<td>2.2%</td>
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<tr>
<td>Midwest Index</td>
<td>4.12%</td>
<td>4.12%</td>
<td>5.55%</td>
<td>13.49%</td>
<td>14.14</td>
<td>13.93</td>
<td>13.23</td>
<td>113.3%</td>
<td>131.1%</td>
<td>2.0%</td>
</tr>
<tr>
<td>Northeast Index</td>
<td>7.94%</td>
<td>7.94%</td>
<td>3.86%</td>
<td>8.21%</td>
<td>14.63</td>
<td>14.97</td>
<td>13.12</td>
<td>122.2%</td>
<td>137.5%</td>
<td>2.7%</td>
</tr>
<tr>
<td>Southeast Index</td>
<td>4.91%</td>
<td>4.91%</td>
<td>6.64%</td>
<td>14.53%</td>
<td>12.33</td>
<td>14.16</td>
<td>13.87</td>
<td>115.0%</td>
<td>117.0%</td>
<td>1.6%</td>
</tr>
<tr>
<td>West Index</td>
<td>8.37%</td>
<td>8.37%</td>
<td>8.28%</td>
<td>13.17%</td>
<td>16.52</td>
<td>18.52</td>
<td>14.50</td>
<td>125.8%</td>
<td>141.5%</td>
<td>1.9%</td>
</tr>
<tr>
<td>Community Bank Index</td>
<td>7.25%</td>
<td>7.25%</td>
<td>5.19%</td>
<td>11.28%</td>
<td>14.94</td>
<td>15.70</td>
<td>13.83</td>
<td>118.2%</td>
<td>129.6%</td>
<td>2.1%</td>
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<tr>
<td>SNL Bank Index</td>
<td>2.33%</td>
<td>2.33%</td>
<td>8.13%</td>
<td>17.98%</td>
<td></td>
<td></td>
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</table>
Mercer Capital's M&A Market Indicators

November 2014

Median Price/Earnings Multiples
Target Banks Assets <$5B and LTM ROE >5%

Median Price/Tangible Book Value Multiples
Target Banks Assets <$5B and LTM ROE >5%

Median Core Deposit Multiples
Target Banks Assets <$5B and LTM ROE >5%

Median Valuation Multiples for M&A Deals
Target Banks Assets <$5B and LTM ROE >5%, through October 2014

<table>
<thead>
<tr>
<th>Regions</th>
<th>Price / LTM Earnings</th>
<th>Price / Tang. BV</th>
<th>Price / Core Dep Premium</th>
<th>No. of Deals</th>
<th>Median Deal Value</th>
<th>Target's Median Assets</th>
<th>Target's Median LTM ROAE (%)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Atlantic Coast</td>
<td>19.92</td>
<td>1.60</td>
<td>10.2%</td>
<td>9</td>
<td>56.40</td>
<td>312,005</td>
<td>8.78%</td>
</tr>
<tr>
<td>Midwest</td>
<td>18.03</td>
<td>1.49</td>
<td>6.7%</td>
<td>51</td>
<td>47.20</td>
<td>117,155</td>
<td>8.90%</td>
</tr>
<tr>
<td>Northeast</td>
<td>17.33</td>
<td>1.87</td>
<td>11.2%</td>
<td>8</td>
<td>106.07</td>
<td>615,348</td>
<td>8.66%</td>
</tr>
<tr>
<td>Southeast</td>
<td>14.83</td>
<td>1.61</td>
<td>8.4%</td>
<td>26</td>
<td>74.37</td>
<td>232,106</td>
<td>9.91%</td>
</tr>
<tr>
<td>West</td>
<td>20.21</td>
<td>1.42</td>
<td>6.6%</td>
<td>15</td>
<td>58.98</td>
<td>407,960</td>
<td>8.03%</td>
</tr>
<tr>
<td>Nat'l Community Banks</td>
<td>17.31</td>
<td>1.52</td>
<td>7.6%</td>
<td>109</td>
<td>56.70</td>
<td>225,187</td>
<td>8.94%</td>
</tr>
</tbody>
</table>

Source: Per SNL Financial
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.
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.


The Financial Institutions Group of Mercer Capital publishes *Bank Watch*, a monthly e-mail newsletter covering five U.S. regions. In addition, Jeff Davis, Managing Director, is a regular contributor to SNL Financial.

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

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