

# Bank Watch



**July 2015**

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# Bank Watch

## Small Bank Holding Companies Regulatory Update & Key Considerations

During 1980 the Federal Reserve issued the Small Bank Holding Company Policy Statement (“Policy Statement”), which recognized from a regulatory perspective that small bank holding companies have less access to the capital markets and equity financing than large bank holding companies. Although the Fed has sought to limit holding company debt so that the parent can serve as a “source of strength” to its subsidiaries, especially the deposit-taking bank subsidiaries, the Policy Statement allowed small bank holding companies to utilize more debt to finance acquisitions and other ownership transfer-related transactions than would be permitted by large bank holding companies. The Policy Statement initially applied to bank holding companies with assets less than \$150 million; it was amended in 2006 to include bank holding companies with assets up to \$500 million. Effective May 15, 2015, the threshold increased to consolidated assets of less than \$1 billion for both bank holding companies and savings and loan holding companies, provided that the company complies with the Qualitative Requirements and does not:

- i. engage in significant nonbanking activities either directly or through a nonbank subsidiary
- ii. conduct significant off-balance sheet activities (including securitization and asset management or administration) either directly or indirectly through a nonbank subsidiary
- iii. have a material amount of debt or equity securities outstanding (other than trust preferred securities) that are registered with the SEC

Holding companies that meet the above requirements may use debt to finance up to 75% of the purchase price of an acquisition, but are subject to the following ongoing requirements:

- i. parent company debt must be retired within 25 years of being incurred
- ii. parent company debt-to-equity must be reduced to 0.30:1 or less within 12 years of the debt being incurred
- iii. the holding company must ensure that each of its subsidiary insured depository institutions is well capitalized
- iv. the company is expected to refrain from paying dividends until it reduces its debt-to-equity ratio to 1:1 or less

The primary benefit of small bank holding company status is that it creates a larger universe of bank and now savings and loan holding companies that are not subject to the Federal Reserve's risk-based capital and leverage rules, including the Basel III rules. As of year-end 2014, 454 bank holding companies with assets between \$500 million and \$1 billion filed a Y-9C according to SNL Financial LC. From a functional standpoint, small bank (and S&L) holding companies do not file a quarterly Y-9C or Y-9LP; instead these companies only file a Y-9SP semi-annually. Regulatory capital rules for these companies continue to apply to their bank subsidiaries, which represents no change from past practice.

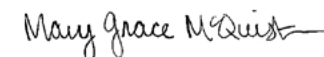
## Implications

Expansion of Policy Statement eligibility is likely to affect strategic and capital planning for small BHCs.

- » Companies that now fall under the Policy Statement oversight can use traditional debt at the holding company level and potentially generate higher returns on equity with a lower cost of capital. Senior debt may be used to replace existing capital such as SBLF preferred stock or fund stock repurchases or dividend distributions.
- » Higher capital requirements for larger bank holding companies, coupled with relaxed capital regulations for small bank holding companies, may provide smaller companies an advantage when bidding on acquisition targets inasmuch as the ability to fund acquisitions with a greater proportion of debt results in a lower cost of capital.
- » S corporation bank holding companies should remain particularly cognizant of the 1:1 debt/equity ratio constraint that should be maintained in order to declare dividends. For S corporations, the inability to declare dividends may result in shareholders being responsible for their pro rata share of the BHC's taxable earnings with no offsetting distributions from the BHC. Since the debt/equity ratio is calculated using equity determined under Generally Accepted Accounting Principles, significant volatility in securities carried as available-for-sale may impair the BHC's ability to declare dividends.

- » If the subsidiary bank holds assets with more onerous risk weightings under the Basel III regime (such as mortgage servicing rights), the holding company may wish to evaluate whether holding such assets at the holding company, rather than the bank, may be more capital efficient.

For more information or to discuss a valuation or transaction advisory issue in confidence, please do not hesitate to contact us.



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## What We're Reading

Jack Milligan of Bank Director has an interesting article, "Is there a Sweet Spot for Bank Stock Pricing?" which relates to bank stock valuation and cites some data from a KBW study presented at a recent bank conference.

<http://mer.cr/1K4xq6S>

Michael Shumaker and Steve Schaffer of Bryan Cave have a compelling article on BankDirector.com entitled "Employee Stock Ownership Plans: Another Tool for Family-Owned Banks."

<http://mer.cr/1fDHzh2>

CK Lee of Commerce Street Capital has a nice piece on how to use strategic planning to drive value on BankDirector.com.

<http://mer.cr/1gxAFdi>

# 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



Sponsored by SNL Financial  
Presenters from Mercer Capital and  
Sutherland Asbill & Brennan

### An Introduction to Business Development Companies

In the hunt for yield, investors are increasingly setting their sights on business development companies (BDCs), which offer public equity 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

### An Overview of the Leveraged Lending Market and Bank Participation in the Market

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.

View webinar on SNL Financial's site at <http://mer.cr/VRc9JV>

### Understanding Deal Considerations

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.

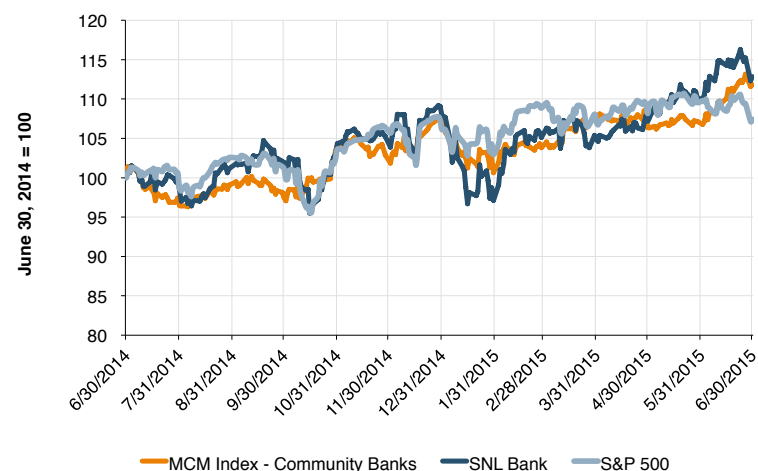
View replay at <http://mer.cr/bnkweb2>

### Basel III Capital Rules Finally Final: What Does It Mean for Community Banks?

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.

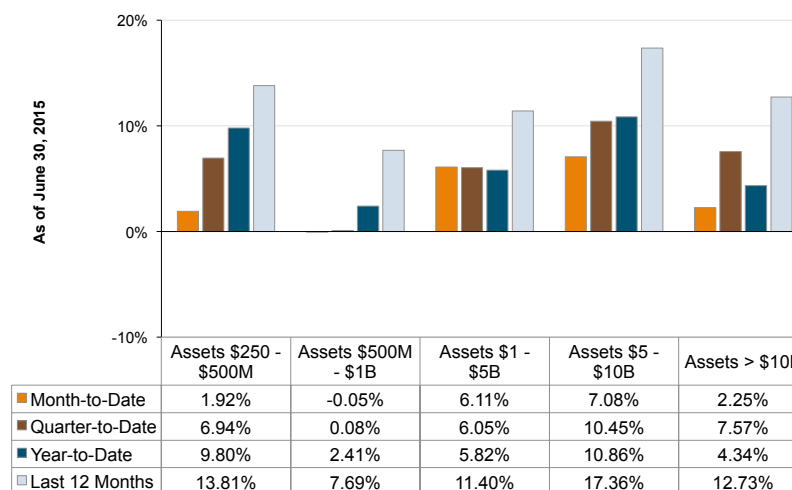
View replay at <http://mer.cr/capital-rules-webinar>

## Mercer Capital's Bank Group Index Overview



## Return Stratification of U.S. Banks

by Asset Size

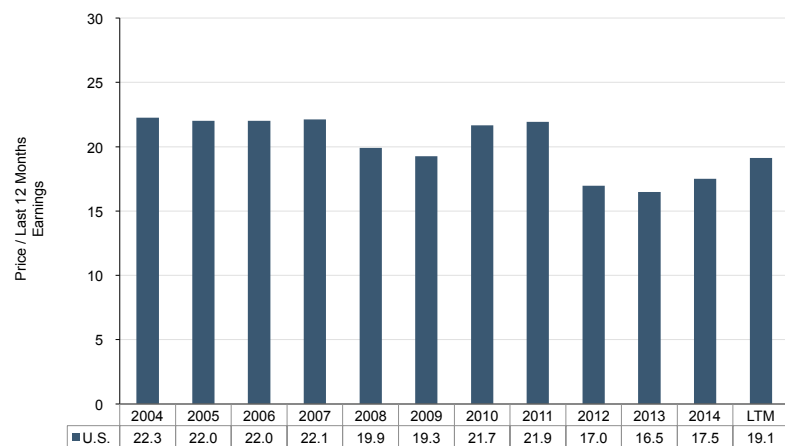


## Median Valuation Multiples

Median Total Return					Median Valuation Multiples as of June 30, 2015					
Indices	Month-to-Date	Quarter-to-Date	Year-to-Date	Last 12 Months	Price / LTM EPS	Price / 2015 (E) EPS	Price / 2016 (E) EPS	Price / Book Value	Price / Tangible Book Value	Dividend Yield
Atlantic Coast Index	3.80%	3.49%	4.91%	14.66%	15.69	15.58	13.01	104.9%	112.6%	2.2%
Midwest Index	4.41%	6.88%	6.45%	13.33%	15.18	14.45	12.80	117.4%	130.4%	2.3%
Northeast Index	3.99%	2.35%	1.99%	5.33%	14.85	14.89	13.20	114.9%	126.8%	3.0%
Southeast Index	5.21%	4.63%	6.23%	21.24%	13.50	15.27	12.82	107.2%	123.5%	1.8%
West Index	4.11%	3.08%	4.02%	10.56%	15.96	15.81	13.57	116.6%	125.8%	2.4%
Community Bank Index	4.36%	3.88%	4.45%	11.81%	15.10	15.03	13.17	113.2%	123.3%	2.3%
<b>SNL Bank Index</b>	<b>2.54%</b>	<b>7.60%</b>	<b>4.63%</b>	<b>12.84%</b>						

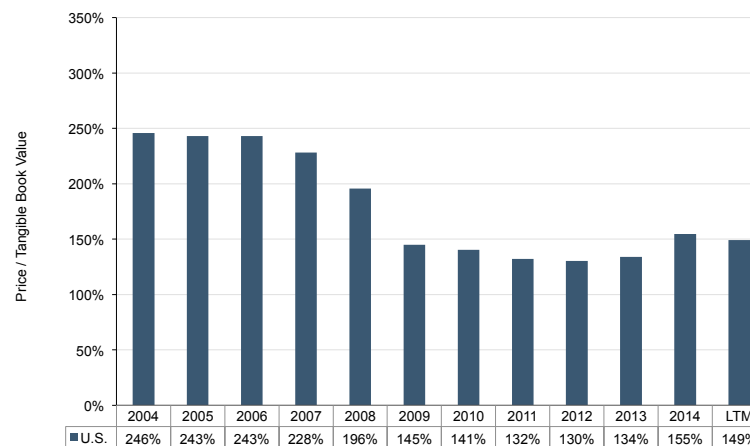
### Median Price/Earnings Multiples

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



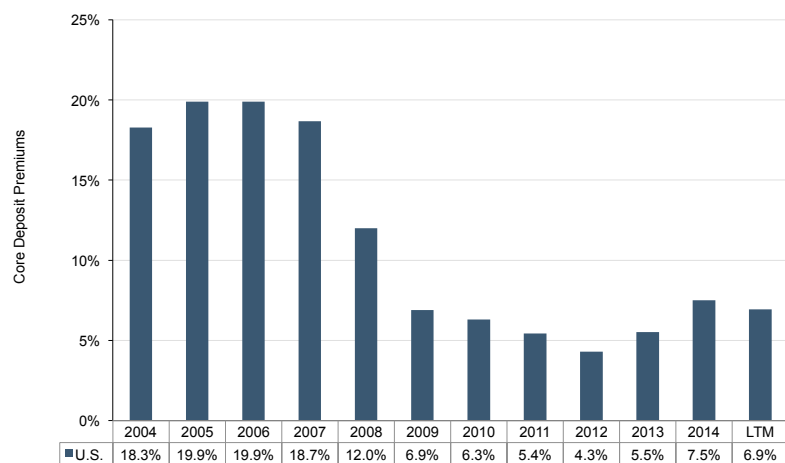
### Median Price/Tangible Book Value Multiples

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

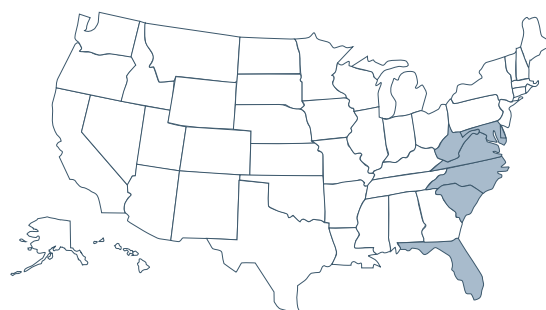
Target Banks' Assets <\$5B and LTM ROE >5%, 12 months ended June 2015

Regions	Price / LTM Earnings	Price / Tang. BV	Price / Core Dep Premium	No. of Deals	Median Deal Value	Target's Median Assets	Target's Median LTM ROAE (%)
Atlantic Coast	20.48	1.67	7.9%	13	81.13	487,470	8.23%
Midwest	18.39	1.52	6.7%	75	41.47	107,691	8.93%
Northeast	19.10	1.48	7.1%	6	133.64	676,218	7.21%
Southeast	17.35	1.37	5.5%	28	29.82	186,921	8.29%
West	18.84	1.48	7.4%	17	59.83	255,891	9.31%
<b>Nat'l Community Banks</b>	<b>19.12</b>	<b>1.49</b>	<b>6.9%</b>	<b>139</b>	<b>45.20</b>	<b>172,502</b>	<b>8.81%</b>

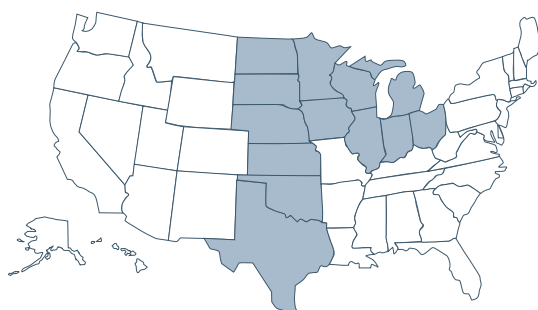
Source: Per SNL Financial

# Mercer Capital's Regional Public Bank Peer Reports

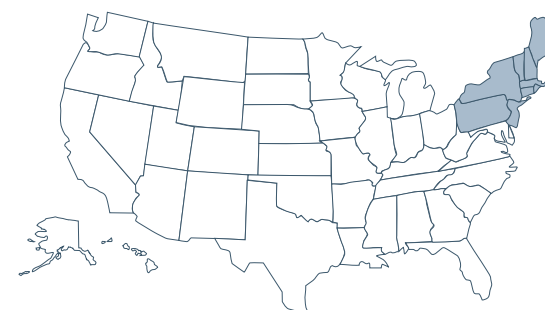
Updated weekly, Mercer Capital's Regional Public Bank Peer Reports offer a closer look at the market pricing and performance of publicly traded banks in the states of five U.S. regions. Click on the map to view the reports from the representative region.



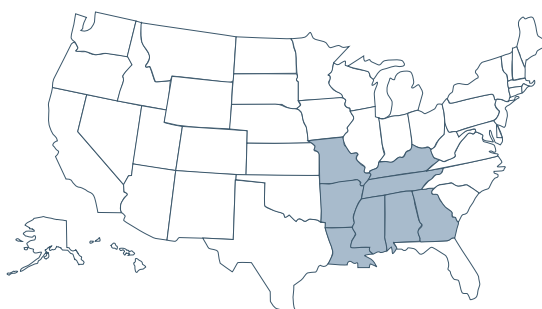
**Atlantic Coast**



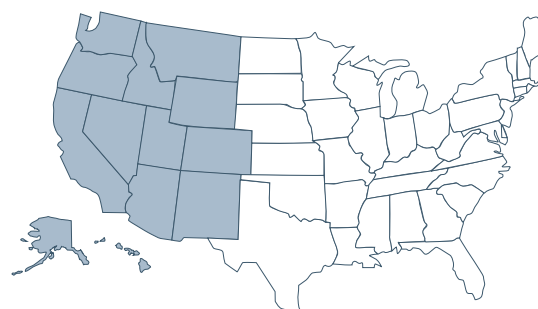
**Midwest**



**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.

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* (2011), *Acquiring a Failed Bank* (2010), *The Bank Director's Valuation Handbook* (2009), and *Valuing Financial Institutions* (1992), Mercer Capital professionals speak at industry and educational conferences.

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](http://www.mercercapital.com).

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# Erickson Partners

## Merges with Mercer Capital



**Mercer Capital**, a national business valuation and financial advisory firm specializing in Corporate Valuation, Litigation Support, Financial Reporting Valuation, and Transaction Advisory Consulting, and **Erickson Partners, Inc.**, a Texas-based Valuation and Litigation Support firm, announce their merger effective July 1, 2015.

Mercer Capital, with its strong presence throughout the Southeast and Midwest, and Erickson Partners, with its strong presence in Texas and Oklahoma, are a perfect fit.

Both firms maintain the highest standards of quality for financial analysis and client service and believe deeply in hiring and developing the best professionals.

"The culture of both firms is so similar and that was important to us. The professionals of Erickson Partners are well-known in the valuation profession as some of the best and brightest. Their work product and reputation are stellar. This merger not only allows us to broaden our geographic reach but also our industry expertise," said **Matt Crow**, President of Mercer Capital.

Erickson Partners enhances Mercer Capital's broad base of industry concentrations with their exceptional history working with and knowledge of professional sports franchises and the energy sector.

"Over our 30 plus year history, Mercer Capital has developed several industry concentrations. By adding the knowledge, insight, and expertise of Don Erickson, Bryce Erickson, and the rest of the professionals of Erickson Partners, we now bring deep experience and insight to a broader range of industries than we could as separate firms," said **Chris Mercer**, CEO of Mercer Capital.

"Combining with Mercer Capital, we will now be able to offer new or expanded services that complement our existing services, as well as additional industry expertise," said **Bryce Erickson**, Managing

Director of Erickson Partners. "In addition to our sports franchise and energy industry concentrations, we will be able to offer deep industry concentrations in construction and building materials, agribusiness, manufacturing and financial institutions, which includes depository institutions, insurance companies, fintech companies, asset management firms, and PE firms."

"The combined firm will have over 40 valuation professionals positioned in five markets throughout the southwest and southeast. Such a deep bench will provide us with a tremendous opportunity to better serve the expanding needs of our clients," said **Don Erickson**, President of Erickson Partners. "Joining with Mercer Capital gives us national resources that will benefit our clients in Texas and beyond."

### About Mercer Capital

Mercer Capital is a national business valuation and financial advisory firm offering corporate valuation, litigation support, financial reporting valuation, and transaction advisory consulting services to a national client base. Clients include private and public operating companies, financial institutions, asset holding companies, high-net worth families, and private equity/hedge funds.

### About Erickson Partners, Inc.

Erickson Partners is a professional valuation and advisory firm specializing in business valuation, litigation support, financial investigations and strategic corporate advisory services. Founded by Don & Bryce Erickson, Erickson Partners has served large and small clients by providing complex financial and economic analysis, leading to reasonable valuation opinions that withstand scrutiny.

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