MERCER CAPITAL

Valuation Services for Credit Union Acquirers

MERCER CAPITAL

BUSINESS VALUATION & FINANCIAL ADVISORY SERVICES

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Mercer Capital's Practice

On average, Mercer Capital provides valuation and advisory services to banks and credit unions annually, ranging in size from assets of less than $100 million to ~$25 billion

Approximately one-third of the banks and credit unions have assets over $1 billion with total assets ranging up to ~$25 billion

Assist on a number of M&A project annually (both buy- and sell- side)

Perform valuations of assets (loans, core deposit intangibles) and liabilities (CD portfolios) obtained in bank M&A transactions annually

Portfolios range from clean to highly distressed, with sizes ranging up to several billion in unpaid principal balance

Provide quarterly valuations to assist clients with estimating the fair value of loan portfolios for disclosure requirements of ASU 2016-01

Mercer Capital's work product has been reviewed and accepted by the major accounting firms

Mercer Capital's Practice

Mercer Capital has experience working with CUs on bank acquisitions and mergers with other CUs. Services provided to CUs include:

- **Pre-Closing** – Providing valuation/advisory/due diligence services related to the target bank
  - **Buy-Side Valuation & Advisory Services** - Mercer Capital can efficiently and effectively analyze the target institution (bank or CU), evaluate the financial effects of the transaction on the buyer, and determine a reasonable valuation range. If appropriate, Mercer Capital can also assist in negotiating the transaction and evaluating alternative financing mechanisms.
  - **Fairness Opinions** – Mercer Capital can support a board's determination that the consideration paid in a transaction is fair to shareholders from a financial point of view.
- **Post-Closing** – Providing valuations of loans, core deposit intangible, and/or CD portfolios to assist with purchase price allocation and preparing pro forma balance sheet at closing.

Mercer Capital's Practice

CoVantage Credit Union
Antigo, Wisconsin

agreed to purchase substantially all of the assets and liabilities of

LincolnWay Community Bank
New Lenox, Illinois

Mercer Capital served as financial advisor to CoVantage CU

– April 2022 –

Georgia's Own Credit Union
Atlanta, Georgia

has agreed to acquire the majority of the assets and liabilities of

Vinings Bank
Smyrna, Georgia

Mercer Capital served as exclusive financial advisor to Georgia's Own Credit Union

– February 2022 –

Robins Financial Credit Union
Robins, Georgia

Has entered into a definitive agreement to acquire

Persons Banking Company
Forsyth, Georgia

Mercer Capital served as exclusive financial advisor to Robins Financial Credit Union

– March 2022 –

First Community CU
Coquille, Oregon

acquired 3 branches from

Umpqua Bank
Roseburg, Oregon

Mercer Capital provided valuation/financial advisory services to First Community CU.

– March 2020 –

Sharonview Federal Credit Union
Indian Land, South Carolina

agreed to purchase two branches of

Bank OZK
Little Rock, Arkansas

Mercer Capital served as a financial advisor on behalf of Sharonview Federal Credit Union

– July 2020 –

Advia Credit Union
Parchment, Michigan

acquired

Golden Eagle Community Bank
Woodstock, Illinois

Mercer Capital served as financial advisor to Advia Credit Union

– July 2019 –

Advia Credit Union
Parchment, Michigan

acquired

Peoples Bank
Elkhorn, Wisconsin

Mercer Capital served as financial advisor to Advia Credit Union

– September 2017 –

Advia Credit Union
Parchment, Michigan

acquired

MidAmerica Bank
Janesville, Wisconsin

Mercer Capital served as financial advisor to Advia Credit Union

– February 2016 –

Community Bank M&A Valuation Themes

Pricing driven by seller earnings and expense savings (but value quoted as a multiple of tangible book value)

Expense savings always a key in pro forma earnings but who gets credit?

Emerging theme of need to buy to acquire deposits

Historical themes of acquiring growth market or in-market consolidation play

Post-crisis M&A largely among small banks; may be changing post reform

Emergence of more super community banks and small regional banks with publicly traded stock to acquire and seeing a rise in mergers of equals transactions

Emerging trend of credit unions acquiring banks

Community Bank M&A Valuation Themes

Acquirers (and investors) are buying earning power, not equity

Basic valuation framework

- Net Income / Assets x Assets / Equity = Net Income / Equity … or
  ROA (Return on Assets) x Leverage = ROE (Return on Equity)
- Net Income / Equity x Price / Earnings = Price / Book … or
  ROTE x P/E = P/TBV

P/E in relation to (core) earnings reflect multiple factors and risk vs. growth considerations … growth potential, franchise quality, risk profile, synergies

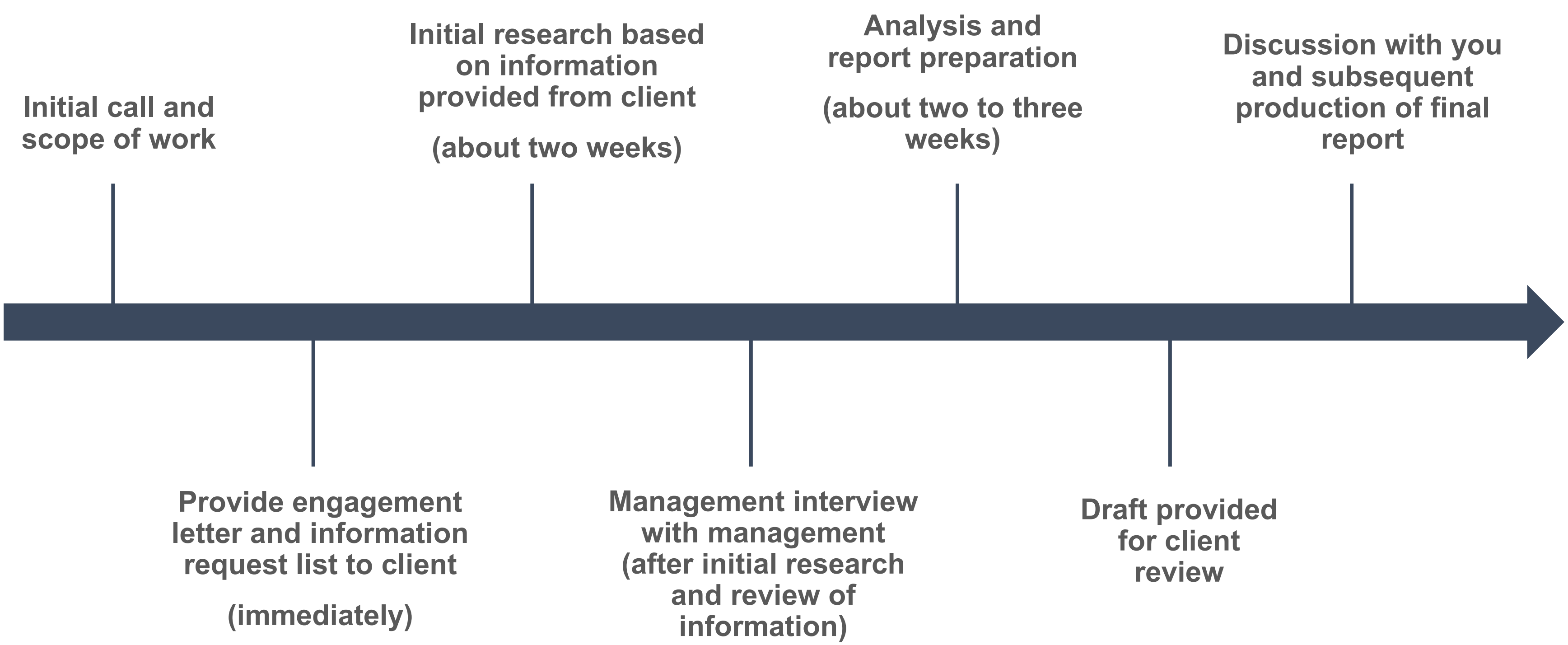
Valuation approaches tend to include both a market approach (comp transaction multiples applied to subject bank) and an income approach (discounted cash flow model)

A reasonable valuation also considers both quantitative and qualitative factors

Value drivers can include key performance indicators at the Target bank as well as considering certain deal considerations and acquirer specific drivers

The typical valuation process for determining the initial valuation range for a Target takes ~ four or five weeks

BUT can be accelerated to accommodate



Financial Reporting For Bank Acquisitions or CU Mergers

In the initial accounting for an acquisition, all assets and liabilities are marked to their fair values, with the most significant marks typically for:

- The loan portfolio; and,
- Depositor customer relationship (core deposit) intangible assets

Fair value marks may also be appropriate on the liability side for time deposit portfolios and longer-term debt instruments such as FHLB advances, subordinated debt, or trust preferred securities.

At Mercer Capital, we work extensively with our clients to analyze loans and other acquired assets and liabilities both when assessing a target initially and when accounting for the transaction at the closing date. Our valuation analyses provide all the information you need to meet the complex financial reporting requirements for an acquisition.

The next few slides provide some detail regarding valuation techniques for financial reporting for bank acquisitions

Loan Portfolio Valuation Overview

Financial assets and liabilities are valued using the income approach, which calculates the present value of a stream of future income or cash flows generated by the instruments. Typical steps for loans include:

Stratification

Identify and segregate purchased credit impaired loans

PCI (Purchase credit impaired) loans typically valued individually (smaller loans may be pooled)

Non-PCI loans pooled. Pool characteristics include collateral type (e.g., closed-end residential) and payment structure (e.g., fixed versus adjustable rate; amortizing versus interest only)

Valuation

Expected cash flows derived using:

- Contractual payment terms
- Probability of default and loss given default estimates
- Prepayments

Expected cash flows discounted using spreads observed from similar assets, funds transfer pricing, or recently originated loans

Purchase Credit Impaired Loans

The identification of purchased credit impaired loans includes discussions with buyer or target personnel knowledgeable of the acquired loans but also considers the following factors:

Objective Factors

- Loan grading (initially target's grades, then updated based on buyer's adjustments)
- Delinquency history
- Impaired status
- TDR status

Other Factors

- Third-party loan review commissioned by target
- Buyer's due diligence files

Loan Valuation: Credit Loss Estimates

The expected cash flow forecast for PCD (purchased credit deteriorated) loans tends to be more specific to each loan, whereas the cash flow forecast for non-PCD loans typically adopts a more homogeneous approach

PCD Loans

For the more material PCI loans, credit loss estimate considers:

1. Collateral support
2. Borrower's or guarantor's ability to support the loan
3. Delinquency history
4. Loan structure (e.g., amortizing versus interest only)
5. Loan type

Analysis typically is provided individually for the larger PCI loans. Smaller PCI loans, such as residential mortgage or consumer loans, may be aggregated

Non-PCD Loans

Loss estimates generally developed by loan type for pass-rated loans and are driven by PD/LGD assumptions

Within each loan type, though, differences may exist. For example, delinquent loans may have higher loss estimates than current loans. Deposit-secured loans would have a credit loss estimate of 0%.

Larger non-PCI classified loans, if any exist, may be evaluated based on the five factors utilized for PCI loans

Valuation Overview: Intangible Assets

Intangible assets such as core deposits are valued using the income approach, which calculates the present value of a stream of future income or cash flows generated by the intangible assets. Relevant factors include:

Depositor Relationships

A "fully loaded" cost of funds, reflecting:

- Interest cost of funds
- Servicing costs
- Non-interest income

Cost of alternative funds (e.g., FHLB)

Future account attrition rates (based on target's historical attrition)

Discount rate for projected earnings

Valuation Overview: Intangible Assets

Term liabilities such as time deposits and subordinated debt/trust preferred securities also are valued using the income approach:

- Contractual cash flows projected through maturity of the instrument, potentially subject to early payoff assumptions
- Discount rates determined using:
  - For CDs, (a) rates on target's recently issued CDs, (b) target's current rate sheet rates, or (c) peer bank rates in local marketplace
  - For subordinated debt/trust preferred securities advances, (a) recent pricing on issuances of subordinated debt and other bank capital instruments, (b) yields on publicly-traded capital instruments with similar structures, (c) spreads on debt with similar risk

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