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Bank Watch

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Are Market Conditions Driving More FinTech Partnerships and M&A?

This article was originally published in Mercer Capital's ***Value Focus: FinTech*** *First Quarter 2016 newsletter. To subscribe visit* ***http://mer.cr/1holYIf****. You can also follow Mercer Capital's Twitter feed* ***@MercerFinTech****.*

It has been an interesting few weeks for FinTech. After several years where both public and private FinTech markets were trending positively, the tail end of 2015 and the start to 2016 saw market access start to diverge. Although the performance of public FinTech companies as a group was relatively flat through the first quarter of 2016 (see **Public Market Indicators on page 3 of the First Quarter 2016 FinTech newsletter**), signs of weakness emerged in alternative/marketplace lending. Shares of some high profile FinTech companies have struggled. For instance, Square, OnDeck, and Lending Club are down significantly in 2016 (-28%, -53%, and -64%, respectively through May 18). The median return for FinTech companies that went putlic in 2015 was negative 16% since IPO through March 31. Not surprisingly, the broader technology **IPO slowdown** in late 2015 has continued into 2016 with no FinTech IPOs as of mid-May.

However, optimism for FinTech still abounds, which the private markets continue to reflect with robust investor interest and funding levels. During the first quarter, 334 FinTech companies raised $6.7 billion compared to 171 companies raising $3.2 billion during the first quarter of 2015. The second quarter is off to a good start too. Ant Financial (Alibaba's finance affiliate) completed an eye-popping **$4.5 billion capital raise** during April.

While the factors driving the divergence between challenging public markets and private markets that remain open for FinTech financings are debatable, the divergence is unlikely to continue indefinitely. Either public markets reopen or private market financings slow. A less favorable public market creates a more challenging exit environment via IPO both for "unicorns" and non-unicorn private companies alike. Headwinds for private market financings will develop if the current dearth of IPOs extends sufficiently such that private investors curtail funding until the public markets reopen to FinTech IPOs at reasonably favorable valuations.

Consequently, other strategic and exit options beyond an IPO should be considered such as partnering with, acquiring or selling to traditional incumbents (banks, insurers, and money managers). The potential for M&A and partnerships is even more likely in FinTech than other tech sectors, particularly in the U.S., due to the unique dynamics of the financial services industry with the resiliency of traditional incumbents and the regulatory landscape. For example, consider a few of the inherent advantages that traditional banks have over non-bank FinTech lenders:

» **Better Access to Funding.** Prior to 2016, a frothy funding environment with a search for yield among investors limited the funding advantage that traditional banks have relative to less regulated FinTech lenders. However, the winds shifted with the first (and perhaps last) Fed rate hike in December as investors and vocal bankers began to question the credit worthiness of originations. As a result, funding via selling loans to hedge funds and securitizing portfolios tightened dramatically, which once again demonstrated the difficulties with an originate-to-sell funding model.

» **Banks Still Have Strong Customer Relationships.** While certain niches of FinTech have strong demand from consumers and businesses for innovative products and technology, traditional financial institutions still maintain the majority of customer relationships. As an example, **the 2015 Small Business Credit Survey from the Federal Reserve** noted that traditional banks are still the primary source for small business loans with only 20% of employer firms applying at an online lender. The satisfaction rate for online lenders was low (15% compared to 75% for small banks and 51% for large banks). The main reasons reported for dissatisfaction with online lenders was high interest rates and unfavorable repayment terms.

» **Uncertain Regulatory Scrutiny of FinTech.** Both the Federal Reserve and the OCC have commented on ways to regulate financial technology, while the the **Treasury has released a white paper** discussing the potential oversight. Of course, the **CFPB has signaled the potential to increase scrutiny** of FinTech lending. The lack of a banking charter also has been cited as a potential weakness and has exposed certain alternative lenders to lawsuits in some states.

FinTech companies are not the only ones considering their options beyond an IPO. Traditional financial Institutions increasingly realize that they must develop a plan to evolve, survive, and thrive as technology and financial services intersect. For example, **a recent survey** from *BankDirector* noted that boards are focusing more on technology with 75% of respondents wanting to understand how technology can make the bank more efficient and 72% wanting to know how technology can improve the customer experience.

FinTech presents a number of strategic options, including: developing their own technology solutions; acquiring a FinTech company, or partnering with a FinTech company. One area that has seen more partnerships and M&A lately is wealth management via the industry's response to robo-advisory. Robo-advisers were noted by the CFA Institute as the FinTech innovation most likely to have the **greatest impact on the financial services industry** in the short-term (one year) and medium-term (five years). Among the recent robo-advisor related acquisitions have been **BlackRock's acquisition of FutureAdvisor** in August 2015, **Invesco's acquisition of Jemstep**, and **Ally Financial's acquisition of TradeKing** in April 2016. On the partnering front, **Motif and J.P. Morgan Chase** announced a partnership in October 2015, **UBS announced a major partnership with SigFig** in May 2016, and **Betterment and Fidelity announced a partnership** in October 2014. Community

What We're Reading

With many online lenders beginning to clamor for a special bank charter from the OCC, *American Banker* examines **a long-forgotten "FinTech Bank."**

A **report from SNL** examines the debate between the investment community and bankers in regard to calculating tangible book value dilution and earn back periods in M&A activity.

As most community banks lack publicly traded stock to use as consideration in M&A activity, many are turning to their holding companies as sources of cash through holding company loans, as discussed in "**How Community Banks Can Fund M&A**."

The Wall Street Journal looks at the **billion dollar industry** that has arisen as a result of the Dodd-Frank requirement for large banks to undergo stress tests.

In "**The Perfect Antidote to Dodd-Frank**," Alex J. Pollock offers his support for and gives an analysis of House Financial Services Committee Chairman Jeb Hensarling's Financial CHOICE Act, which many see as a more bank-friendly alternative to Dodd-Frank.

banks will also have an opportunity to enter the robo-advisory fray as **Personal Capital announced a partnership with Alliance Partners** that will allow over 200 community banks offer digital wealth advisory tools.

While we do not yet know which strategy will be most successful, discussions of whether to build, partner, or buy is on the agenda of many boards and executives of both financial institutions and FinTech companies. The right combination of technology and financial services has significant potential to create shareholder value. Any contemplated partnership or merger should be examined thoroughly to ensure that the right metrics are utilized to examine value creation and returns on investment.

The downside is that M&A and significant partnerships also entail significant risks related to execution, culture, litigation, regulation, and corporate reputation. These issues must be balanced with the potential rewards, such as customer satisfaction/retention, shareholder value creation, and return on investment.

If you are interested in considering strategic options and potential partnerships for your financial institution or FinTech company, contact Mercer Capital. Financial institutions have represented our largest industry focus for over thirty years. We have a deep bench with experience with both FinTech companies and traditional financial institutions (banks, asset managers, and insurance companies). We believe this uniquely suits us to assist both.

Jay Wilson, Jr.

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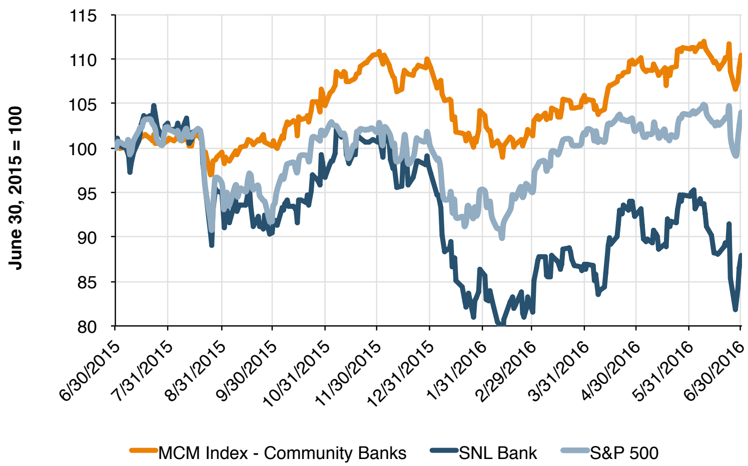
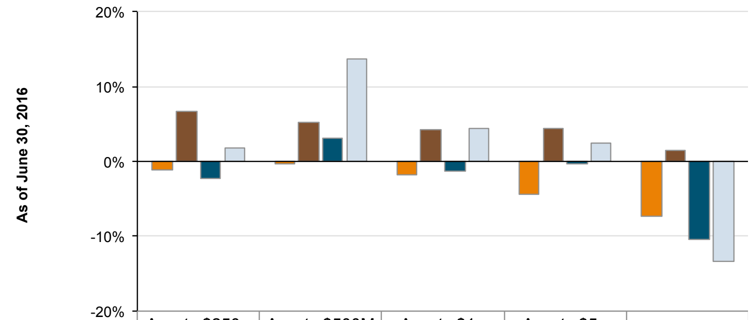
Mercer Capital's Bank Group Index Overview



Return Stratification of U.S. Banks

by Asset Size



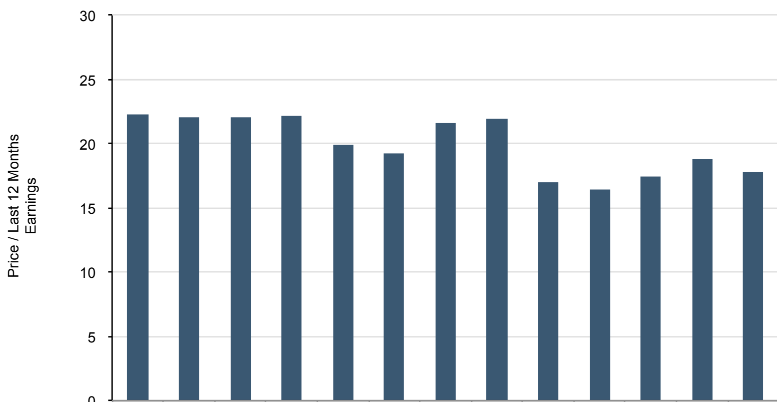
	Assets $250 - $500M	Assets $500M - $1B	Assets $1 - $5B	Assets $5 - $10B	Assets > $10B
Month-to-Date	-1.12%	-0.30%	-1.73%	-4.39%	-7.38%
Quarter-to-Date	6.68%	5.24%	4.17%	4.45%	1.44%
Year-to-Date	-2.28%	3.15%	-1.29%	-0.28%	-10.38%
Last 12 Months	1.83%	13.63%	4.42%	2.47%	-13.40%

Median Valuation Multiples

	Median Total Return				Median Valuation Multiples as of June 30, 2016					
Indices	Month-to-Date	Quarter-to-Date	Year-to-Date	Last 12 Months	Price/ LTM EPS	Price / 2016 (E) EPS	Price / 2017 (E) EPS	Price / Book Value	Price / Tangible Book Value	Dividend Yield
Atlantic Coast	-1.48%	3.42%	1.97%	13.82%	16.8x	15.6x	13.8x	109%	125%	2.0%
Midwest	-0.73%	6.45%	2.28%	11.68%	14.0x	13.7x	12.5x	115%	134%	2.2%
Northeast	2.22%	6.70%	4.19%	9.44%	14.2x	13.6x	11.8x	114%	122%	3.1%
Southeast	-0.90%	4.26%	-2.22%	7.27%	14.2x	15.2x	13.1x	104%	112%	1.5%
West	-2.47%	4.38%	-0.66%	10.14%	15.2x	14.1x	12.1x	114%	121%	2.5%
National Community Banks	-0.63%	4.87%	1.26%	10.38%	14.8x	14.4x	12.8x	114%	125%	2.2%
SNL Bank Index	**-7.03%**	**1.69%**	**-9.59%**	**-12.13%**						

Median Price/Earnings Multiples

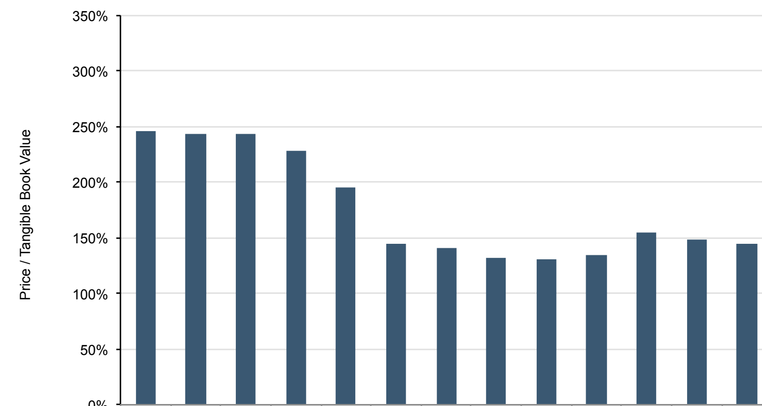
Target Banks' Assets <$5B and LTM ROE >5%



	2004	2005	2006	2007	2008	2009	2010	2011	2012	2013	2014	2015	LTM
U.S.	22.3	22.0	22.0	22.1	19.9	19.3	21.7	21.9	17.0	16.5	17.5	18.8	17.8

Median Price/Tangible Book Value Multiples

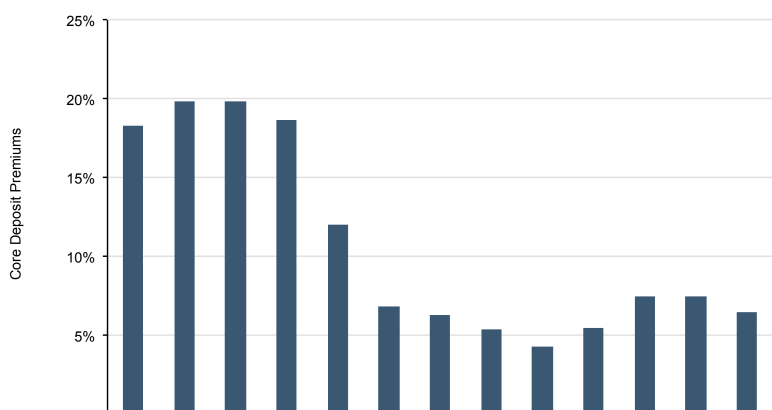
Target Banks' Assets <$5B and LTM ROE >5%



	2004	2005	2006	2007	2008	2009	2010	2011	2012	2013	2014	2015	LTM
U.S.	246%	243%	243%	228%	196%	145%	141%	132%	130%	134%	155%	148%	145%

Median Core Deposit Multiples

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



	2004	2005	2006	2007	2008	2009	2010	2011	2012	2013	2014	2015	LTM
U.S.	18.3%	19.9%	19.9%	18.7%	12.0%	6.9%	6.3%	5.4%	4.3%	5.5%	7.5%	7.5%	6.5%

Median Valuation Multiples for M&A Deals

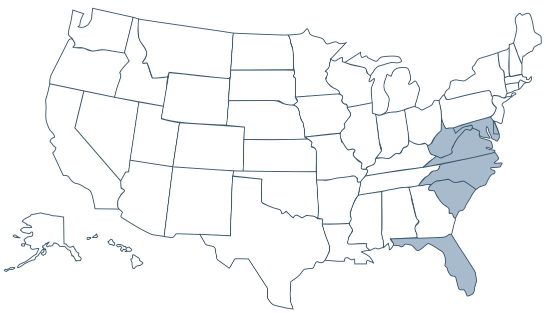
Target Banks' Assets <$5B and LTM ROE >5%, 12 months ended June 2016

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	17.7x	147%	6.0%	23	50.23	410,011	8.09%
Midwest	17.5x	141%	5.5%	66	22.48	138,205	8.60%
Northeast	21.9x	149%	9.3%	9	78.47	495,016	7.12%
Southeast	16.4x	157%	9.3%	24	63.36	233,766	11.34%
West	15.3x	144%	7.9%	14	48.75	242,061	11.05%
National Community Banks	**17.8x**	**145%**	**6.5%**	**136**	**44.09**	**206,482**	**8.78%**

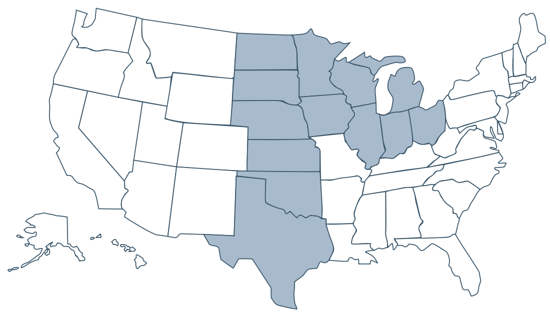
Source: Per SNL Financial

Mercer Capital's Regional Public Bank Peer Reports

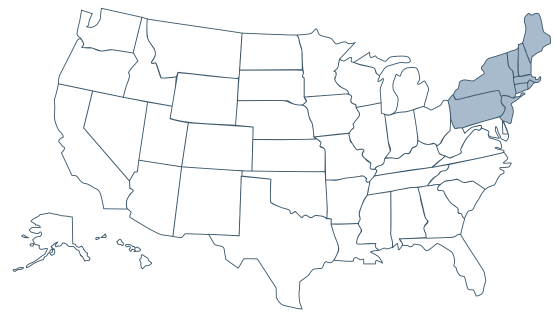
Updated weekly, Mercer Capital's Regional Public Bank Peer Reports offer a closer look at the market pricing and performance of publicly traded banks in the states of five U.S. regions. Click on the map to view the reports from the representative region.



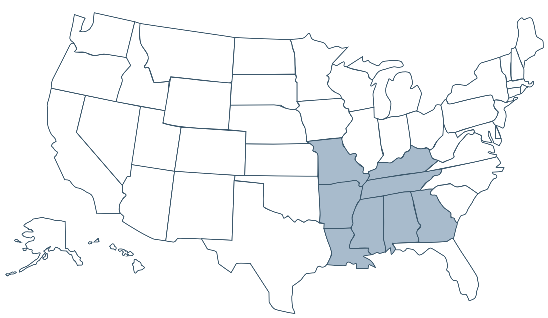
Atlantic Coast



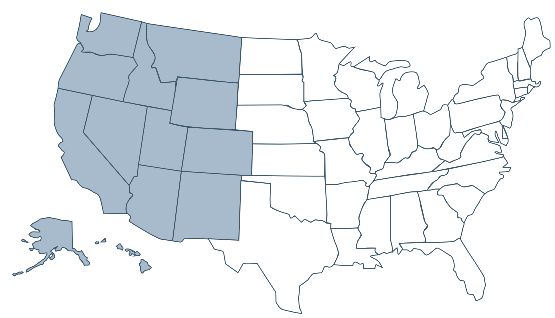
Midwest



Northeast



Southeast



West

Simmons First National Corporation Agrees to Acquire Citizens National Bank

Mercer Capital Served as Financial Advisor to Citizens National Bancorp, Inc. and Rendered a Fairness Opinion

Transaction Overview

- Simmons First National Corporation (Nasdaq: "SFNC" or "Simmons") announced May 18, 2016 that it has entered into a definitive stock purchase agreement with Citizens National Bancshares Inc. to acquire Citizens National Bank ("CNB" or "Citizens").
- According to the terms of the agreement, Simmons will acquire all of the outstanding common stock of CNB in a transaction valued at about $81 million based on the company's 10-day average stock price of $45.18. The purchase price will consist of 835,741 shares of SFNC common stock and $40.3 million in cash. Additionally, immediately prior to the purchase Citizens National Bank will declare a $3.0 million special one time dividend that will be paid to Citizens National Bancorp, Inc. and subsequently distributed to the CNB shareholders prior to closing.
- Regarding the merger, Paul Willson, CEO and Chairman of Citizens, said, "We have worked with Mercer Capital for a number of years and Jeff Davis the past several years. Our Board and I appreciate their thoughtful insight about shareholder value creation, the banking industry, and the public and M&A markets for banks."
- Completion of the transaction is expected in the third quarter of 2016

Simmons First National Corp.
Pine Bluff, Arkansas

has agreed to acquire

CITIZENS NATIONAL BANK
Athens, Tennessee

Mercer Capital served as a financial advisor & rendered a fairness opinion on behalf of Citizens National Bancorp, Inc.

May 2016

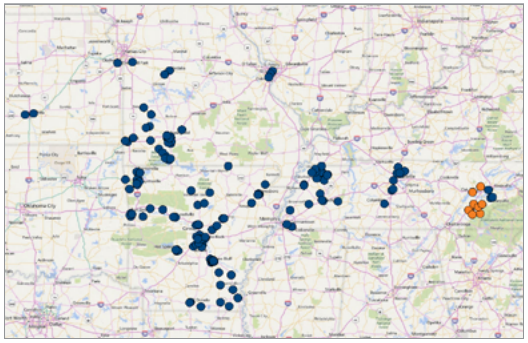
Transaction Metrics (as of 3/31/16)

Aggregate Transaction Value and Special Dividend ($000) [1]	$81,070
Approximate Consideration Mix Plus Special Dividend – Stock / Cash (%)	47% Stock / 53% Cash
Price / 3/31/2016 Tangible Common Book Value (%)	127%
Price / 3/31/2016 Tangible Common Book Value (8% Adjusted) (%) [2]	140%
Price / LTM Net Income (C-Corp Adjusted) [3]	18.5x
Price / LTM Core Income (C-Corp Adjusted) [3, 4]	20.2x
Core Deposit Premium [5]	3.9%

[1] Based on Aggregated deal value includes ~3MM special one time dividend payable to the shareholders prior to closing
[2] Capital Adjusted for 8% capital at 3/31/2016, dollar for dollar consideration for all excess capital
[3] Assumes a 35% C-Corp Tax Rate
[4] Net of one time items
[5] Core deposits represent 95.76% of total deposits per SNL Financial

Source: SNL Financial

Pro Forma Branch Franchise



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- 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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