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Bank Watch

ARTICLE

The Community Bank Scale Tax Three Questions for Boards in 2026

In This Issue

The Community Bank Scale Tax Three Questions for Boards in 2026	1
Public Market Indicators	3
M&A Market Indicators	4
Regional Public Bank Peer Reports	5
About Mercer Capital	6

The Community Bank Scale Tax

Three Questions for Boards in 2026

By: Jack Carter, CPA

Community banks came into 2026 in better shape than many expected. Margins and earnings improved, deposits were growing again, loan growth held up, and unrealized losses on securities moved lower. On the surface, the story looks better than a year ago. But that does not mean the pressure is gone.

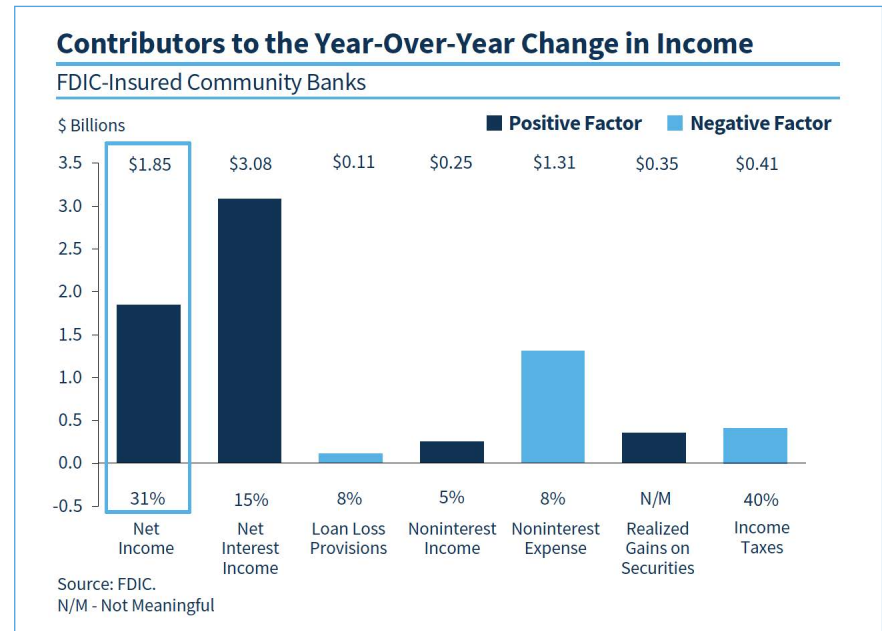
For many community banks, the next big issue is not only rates or loan growth. It is whether the bank is big enough, focused enough, and efficient enough to carry the higher cost of being a modern bank. That cost includes more than salaries and branches. It also includes technology, cybersecurity, vendor management, fraud tools, compliance, and the people needed to run it well. The FDIC's Quarterly Banking Profile shows that despite better net interest margins, the largest drag on earnings is the cost of running a modern bank.

That is where many board conversations should be headed now. The challenge is simple to describe: banking keeps getting more expensive, the cost base is harder to flex, and smaller banks do not always have enough scale to spread those costs out. This does not mean every bank needs to sell but it does mean every bank needs to be honest about what it costs to stay independent.

1. Which costs are truly fixed, and which ones are self-inflicted?

Every bank has unavoidable costs for non-revenue generating activities, such as for risk management, compliance, and cybersecurity. But not every cost deserves the same treatment.

Some banks are carrying real fixed costs. Others are carrying years of built-up complexity: too many vendors, too many products, too many exceptions, too many legacy processes, and too many branches doing less work than they used to.



The distinction between real fixed costs and the just-as-real complexity costs matters. If management treats every expense as untouchable, the bank usually ends up protecting complexity instead of protecting value. Boards should push on that point. Which costs are now part of the price of doing business? And which costs are there because nobody has made the harder cleanup decisions? Those are two very different problems.

2. Are we big enough, or focused enough, to make the model work?

Scale matters in banking, which is not a new point. The part that often gets missed is that scale does not always have to come from simply getting bigger. Scale can come from size. It can also come from focus.

A bank with a strong niche, an efficient branch footprint, a manageable product set, and good expense discipline can often perform better than a larger bank carrying too much overhead. Bigger is not always better if the added size comes with added complexity.

That is an important point for community bank boards. The question is not just, "Do we need to grow?" The better question is, "Do we have a business model that can carry the cost structure we have today?" If the answer is no, the bank has a few options: it can grow, it can simplify, it can narrow its focus, it can outsource more of what does not set it apart, or it can decide that another partner may be better positioned to carry the platform going forward.

Recent examples show the range of choices. Community Bank used a branch purchase from Santander to build scale in a target market; Five Star Bank's parent chose to wind down BaaS and refocus on its core franchise; Mechanics Bank exited indirect auto and later outsourced servicing of the run-off portfolio; and Susquehanna chose to partner with C&N for greater scale, resiliency, and efficiency. In sum, there are plenty of proven options and choices.

But doing nothing is also a choice. And in many cases, it is the most expensive one.

3. How much does the expense base hurt shareholder value?

This is where strategy turns into valuation. A bank is not credited just for spending money on technology, compliance, or infrastructure. It gets credited when those investments lead to better performance, better returns, better customer retention, better growth, and better risk control.

If the bank carries a heavy cost base without a clear payoff, that usually shows up in weaker earnings and lower returns. Over time, it can also show up in a lower valuation, which matters even if the board has no near-term interest in selling. Valuation is not just about a sale; it is a scorecard on the strength of the franchise. A bank with strong returns and a clear strategy usually has more flexibility. A bank with weaker returns and too much complexity usually has fewer options.

Timing matters. Banks have more breathing room now than they did a few years ago when interest rates increased sharply, with strong earnings and clean asset quality, and that is a good time to revisit strategic and technological plans.

The issue in 2026 is not simply whether a community bank can remain independent. The issue is whether it can earn that independence after paying the ever-growing cost of being a modern bank.

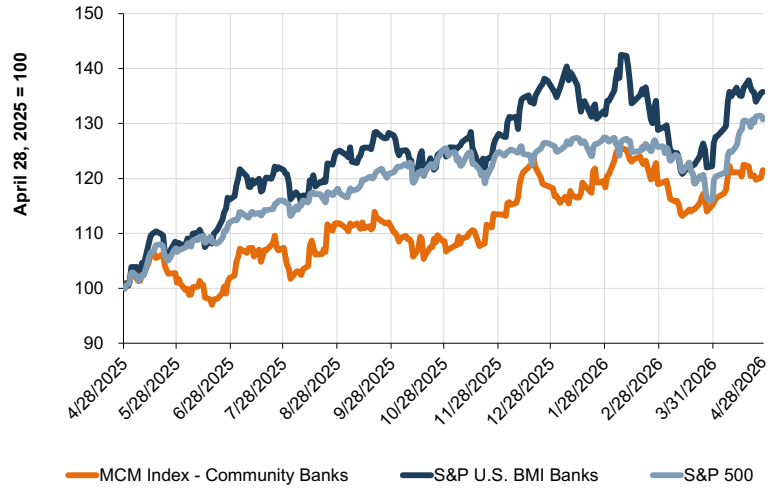
The banks that will stand out are not necessarily the biggest banks. They are the ones that know what they do well, run a cleaner model, and make sure their cost base supports the franchise instead of weighing it down. For some institutions, that will support long-term independence. For others, it may lead to a different conclusion.

Either way, the discussion should start with a hard look at the expense base. In a lot of cases, the pressure to sell does not begin with a buyer showing up. It begins when the math stops working.

About Mercer Capital

Mercer Capital is a nationally recognized valuation and advisory firm serving financial institutions including banks, credit unions, fintech companies, insurance companies, investment management firms, financial sponsors, and other specialty finance firms. Mercer Capital regularly assists these clients with significant corporate valuation requirements, transactional advisory services, and other strategic decisions.

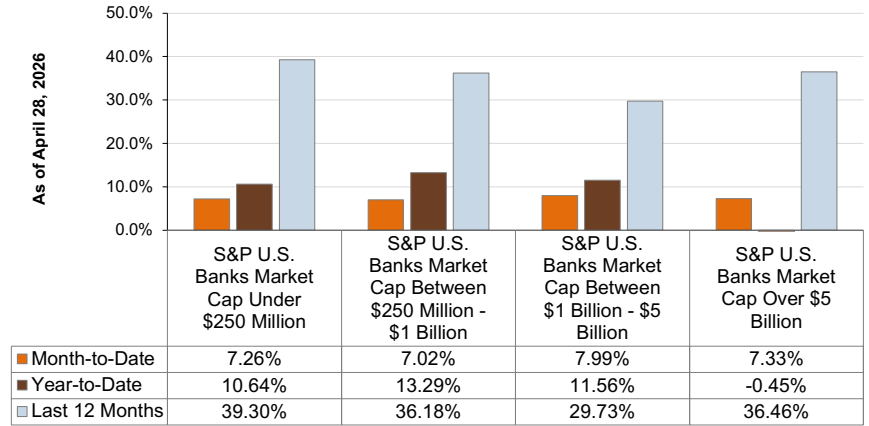
Mercer Capital's Bank Group Index Overview



Source: S&P Capital IQ Pro.

Return Stratification of U.S. Banks

by Market Cap



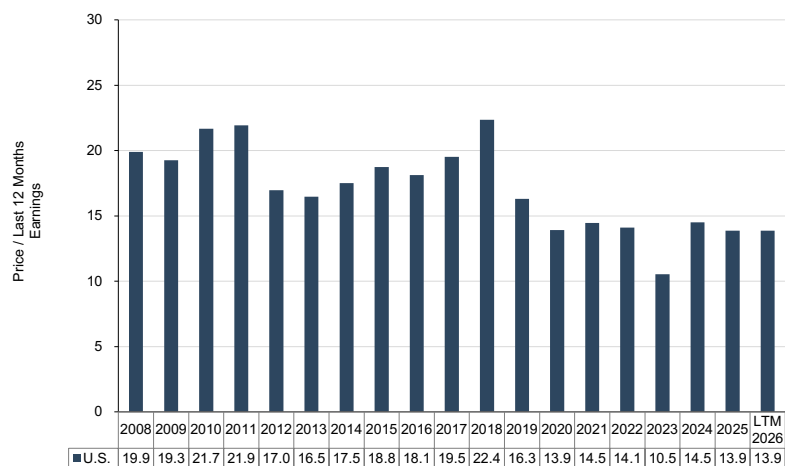
Source: S&P Capital IQ Pro.

	Total Return			Regional Index Data as of April 28, 2026					
	Month-to-Date	Year-to-Date	Last 12 Months	Price/LTM EPS	Price / 2026(E) EPS	Price / 2027(E) EPS	Price / Book Value	Price / Tangible Book Value	Dividend Yield
Atlantic Coast Index	6.0%	9.3%	28.2%	11.8x	10.6x	9.7x	117%	128%	2.4%
Midwest Index	5.7%	5.9%	26.9%	11.8x	10.4x	9.9x	107%	131%	2.7%
Northeast Index	6.3%	9.1%	26.3%	10.8x	9.5x	9.0x	117%	138%	2.9%
Southeast Index	2.4%	3.7%	30.3%	11.9x	9.1x	8.7x	101%	124%	2.1%
West Index	5.8%	3.7%	12.8%	12.3x	10.3x	9.0x	101%	116%	2.6%
Community Bank Index	5.1%	4.0%	21.5%	11.7x	9.8x	9.3x	113%	128%	2.6%
S&P U.S. BMI Banks	7.4%	0.7%	35.8%	na	na	na	na	na	na

Source: S&P Capital IQ Pro.

Median Price/Earnings Multiples

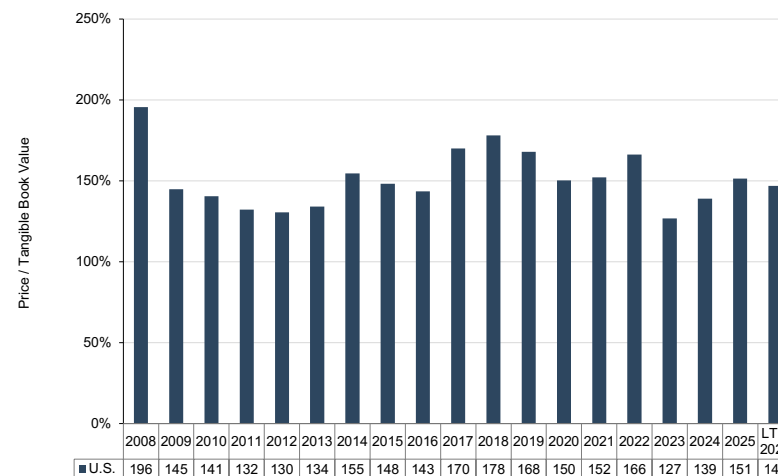
Target Banks' Assets <\$5B and LTM ROE >5%



Source: S&P Capital IQ Pro.

Median Price/Tangible Book Value Multiples

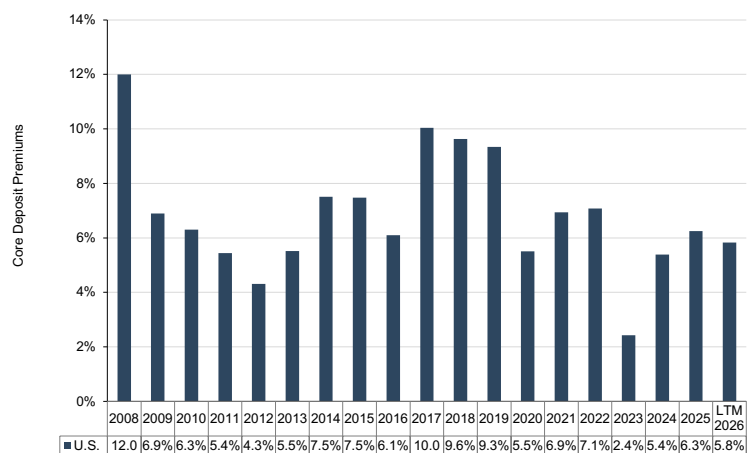
Target Banks' Assets <\$5B and LTM ROE >5%



Source: S&P Capital IQ Pro.

Median Core Deposit Premiums

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



Source: S&P Capital IQ Pro.

Median Valuation Multiples for M&A Deals

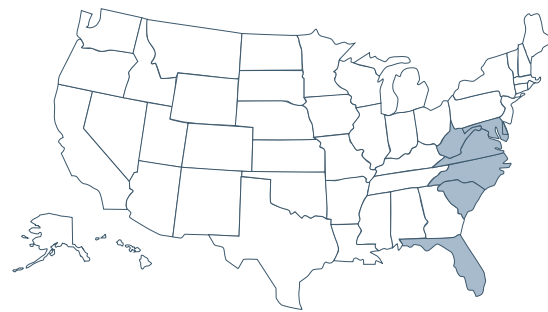
Target Banks' Assets <\$5B and LTM ROE >5%, 12 months ended April 29, 2026

Regions	Price / LTM Earnings	Price/ Tang. BV	Price / Core Dep Premium	No. of Deals	Median Deal Value (\$M)	Target's Median Assets (\$000)	Target's Median LTM ROAE
Atlantic Coast	17.4x	180%	9.2%	4	335.6	1,752,261	9.3%
Midwest	13.8x	149%	6.5%	21	130.7	1,533,551	11.0%
Northeast	14.0x	138%	3.5%	5	99.1	941,604	8.5%
Southeast	13.9x	121%	4.1%	9	79.1	689,339	8.0%
West	16.2x	144%	5.4%	3	176.6	1,235,620	8.5%
National Community Banks	13.9x	147%	5.8%	42	122.7	1,178,973	10.0%

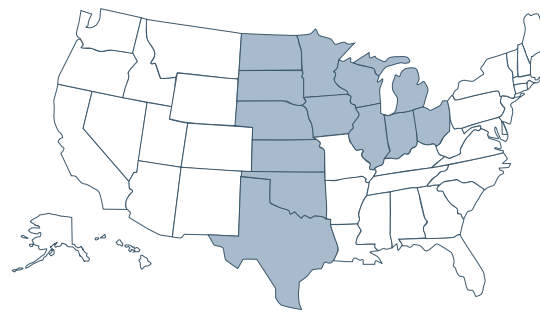
Source: S&P Capital IQ Pro.

Mercer Capital's Regional Public Bank Peer Reports

Updated monthly, 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.



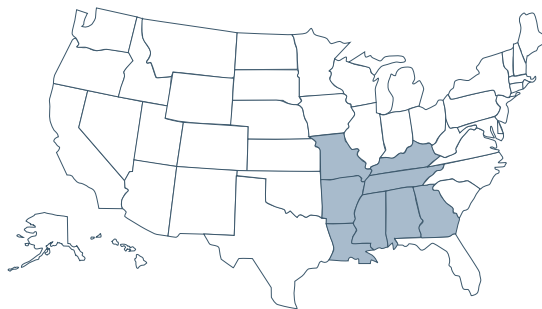
Atlantic Coast



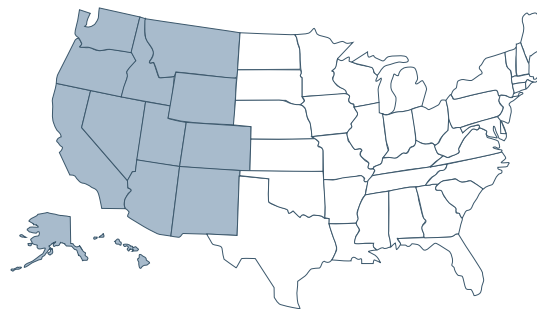
Midwest



Northeast



Southeast



West



OTCQX

with assets greater than \$1.5 billion

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Mercer Capital assists banks, thrifts, and credit unions with significant corporate valuation requirements, transaction advisory services, and other strategic decisions.

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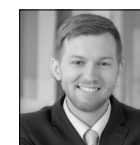
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