

Austin Associates Webinar Series

M&A Case Studies

Enhancing Your Community Bank's Value

April 20, 2016



WEBINAR INSTRUCTIONS

April 20, 2016

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- If you have any questions, they should be typed into your “GoToWebinar” participant control panel.
- If you get disconnected, you can either call back via the telephone call-in option or you can use the voice-over-IP option from your participant control panel on your computer and follow the instructions.
- If you are having technical difficulty during the presentation, please call Lisa Cordier 419.517.1763.
- This webinar is being recorded for distribution and will be available on the Austin Associates website (www.austinassociates.com). You will be able to download the presentation from our website after we complete the webinar.

PRESENTERS

Managing Directors of Investment Banking

Craig Mancinotti - Joined the firm in 1982 and co-manages the firm's investment banking and strategic consulting divisions. Received a Bachelor's degree in Business Administration and an MBA from the University of Toledo. Served as an instructor at the Stonier Graduate School of Banking and the Bank Administration Institute School. Served for ten years as a director of a \$400 million Midwest community bank. Annual speaker at "Acquire or Be Acquired" conferences. Licensed rep of IBS (a registered broker dealer) and holds Series 63 and 79 (Investment Banking) licenses.



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Rick Maroney - Joined the firm in 1984 and co-manages the firm's investment banking and strategic consulting divisions. Received a Bachelor's degree in Business Administration and an MBA from the University of Toledo. Served as an instructor at the Stonier Graduate School of Banking. Annual speaker at "Acquire or Be Acquired" conferences. Licensed rep of IBS (a registered broker dealer) and holds Series 63 and 79 (Investment Banking) licenses.



Rick Maroney
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AUSTIN ASSOCIATES OVERVIEW

Consulting and Investment Bankers to Community Banks

- Community bank advisors for more than 40 years
- Specialized services through multiple practice areas

Investment Banking

Strategic Consulting

Financial Management

Technology Solutions

- Owners are consultants/managers
- Over 200 bank/thrift clients in 2015 from 28 states
- Nationally-ranked leader in community bank M&A for 3 decades

M&A EXPERIENCE

Top Financial Advisors in Whole Bank Deals

ALL U.S. DEALS (2007 - YTD 2016)			
Overall Rank	Advisory Firm	Number of Deals	Announced Deal Value (\$M)
1	Keefe, Bruyette & Woods	366	\$50,364.1
2	Sandler O'Neill & Partners, L.P.	336	\$73,271.7
3	Raymond James & Associates, Inc.	112	\$5,360.8
4	Hovde Group, LLC	92	\$4,083.4
5	Sheshunoff & Co. Investment Banking LP	60	\$1,706.0
T-6	FIG Partners, LLC	57	\$2,643.9
T-6	Capital Corporation, LLC	57	\$345.2
8	Austin Associates, LLC	55	\$1,538.2
9	D.A. Davidson & Co.	53	\$2,292.0
10	Commerce Street Capital, LLC	41	\$1,312.2
T-11	RBC Capital Markets, LLC	38	\$16,548.2
T-11	FinPro, Inc.	38	\$909.3
13	J.P. Morgan Securities LLC	37	\$83,688.5
14	KPMG LLP	36	\$501.2
15	Boenning & Scattergood, Inc.	34	\$1,633.6
T-16	DD&F Consulting Group	33	\$1,033.2
T-16	Professional Bank Services Inc.	33	\$578.4
18	Monroe Financial Partners, Inc.	30	\$707.8
T-19	Bank Advisory Group, LLC	27	\$882.2
T-19	Vining-Sparks IBG, L.P.	27	\$342.1
T-19	National Capital, LLC	27	\$190.6

ALL U.S. DEALS (2015)			
Overall Rank	Advisory Firm	Number of Deals	Announced Deal Value (\$M)
1	Sandler O'Neill & Partners, L.P.	61	\$17,468.9
2	Keefe, Bruyette & Woods	44	\$4,140.0
T-3	FIG Partners, LLC	20	\$1,609.6
T-3	Hovde Group, LLC	20	\$773.3
5	Raymond James & Associates, Inc.	17	\$848.2
T-6	Austin Associates, LLC	12	\$647.4
T-6	D.A. Davidson & Co.	12	\$375.9

ALL U.S. DEALS (YTD 2016)			
Overall Rank	Advisory Firm	Number of Deals	Announced Deal Value (\$M)
1	Sandler O'Neill & Partners, L.P.	9	\$5,218.3
2	Keefe, Bruyette & Woods	6	\$1,512.2
T-3	Austin Associates, LLC	5	\$90.5
T-3	Raymond James & Associates, Inc.	5	\$369.7
5	Boenning & Scattergood, Inc.	4	\$72.7

Source: SNL Financial

Note: Data through 03/31/16. More than 100 firms reported in SNL's M&A Advisory rankings. Some deal values not reported and rankings exclude terminated deals.

WEBINAR AGENDA

April 20, 2016

- **Market Update**
 - Factors driving consolidation
 - M&A pricing trends
- **Buy-Side Perspective**
 - Market reaction to acquisitive companies
 - Buy-side case studies
- **Strategic Mergers**
 - Unique attributes to negotiating a deal
 - Strategic merger case studies



MARKET UPDATE

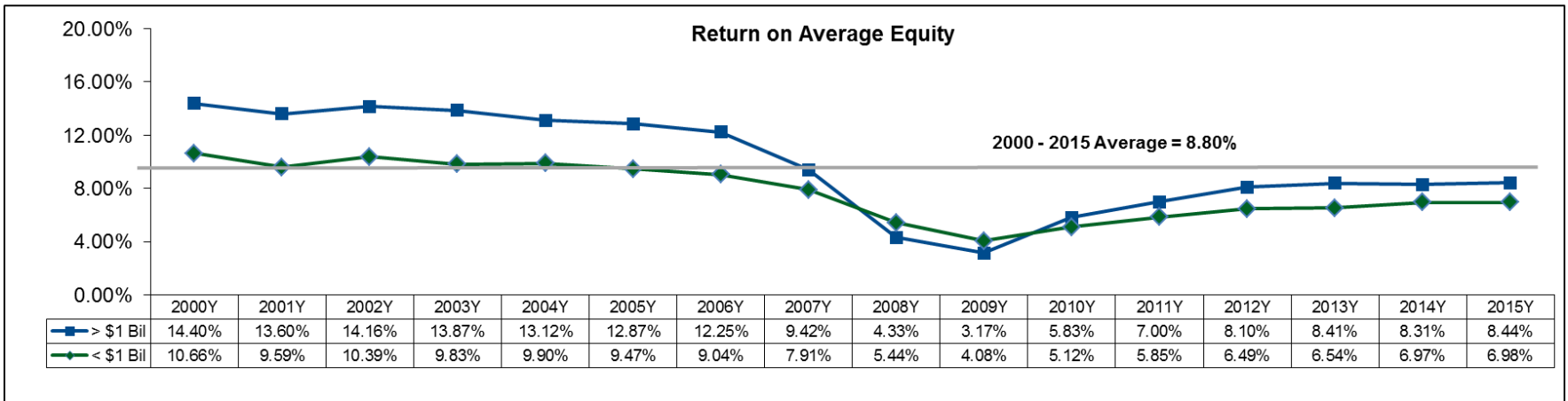
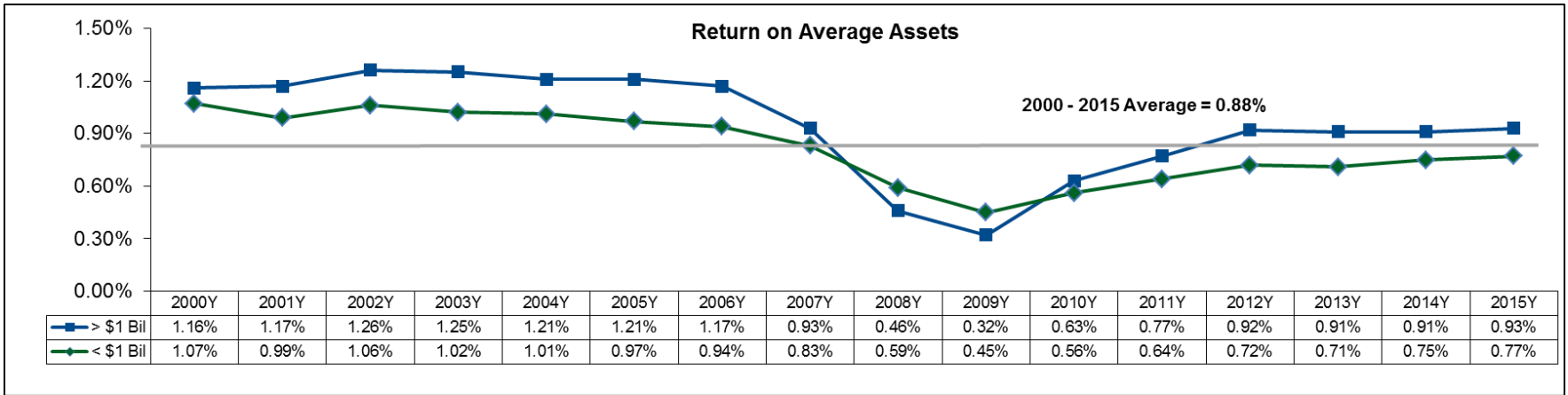
“TOP THREATS TO SMALL BANK PROFITS”

Vining Sparks survey of 250 banks (American Banker – April 2016)

- Weak macro-economic conditions
- Too much regulation
- Increased funding costs
- Unchanged interest rates
- Loan troubles
- Shrinking loan portfolios

INDUSTRY PROFITABILITY

ROAA and ROAE Since 2000

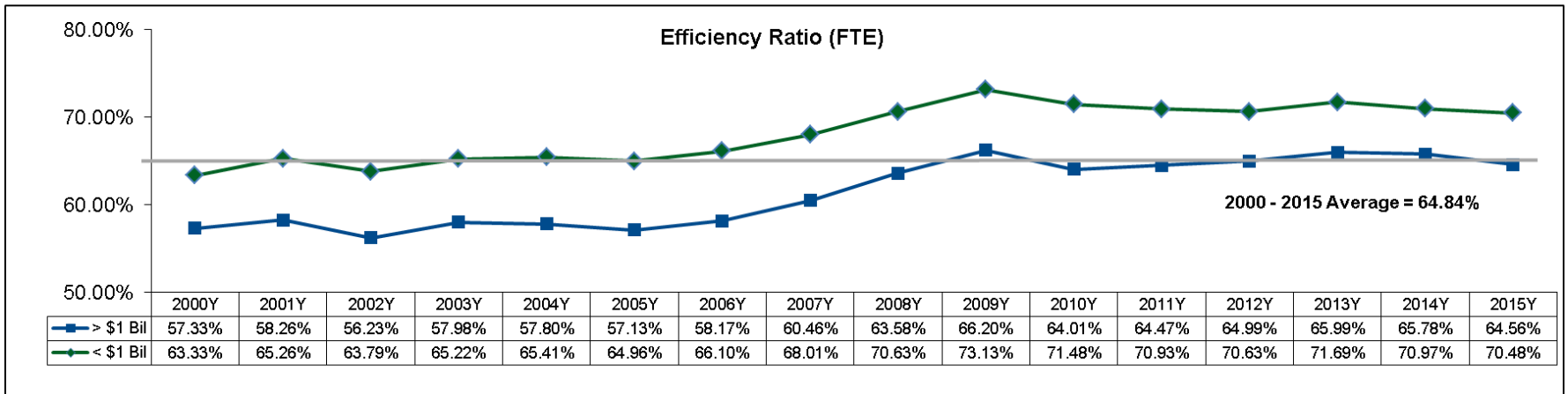
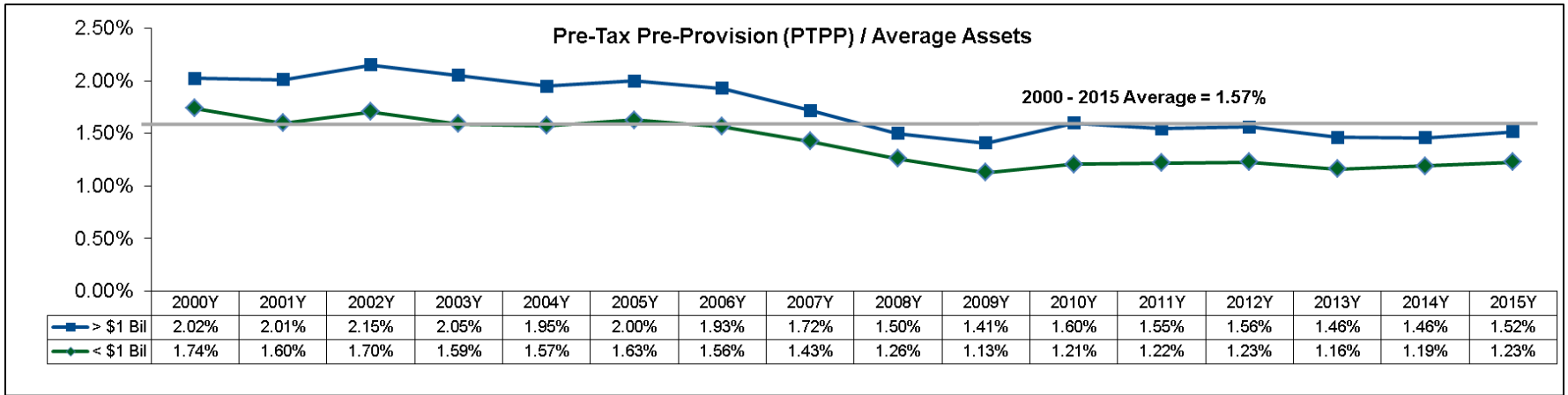


Source: SNL Financial

Note: Results are based on median statistics for all banks and thrifts.

INDUSTRY PROFITABILITY

PTPP and Efficiency Ratio Since 2000



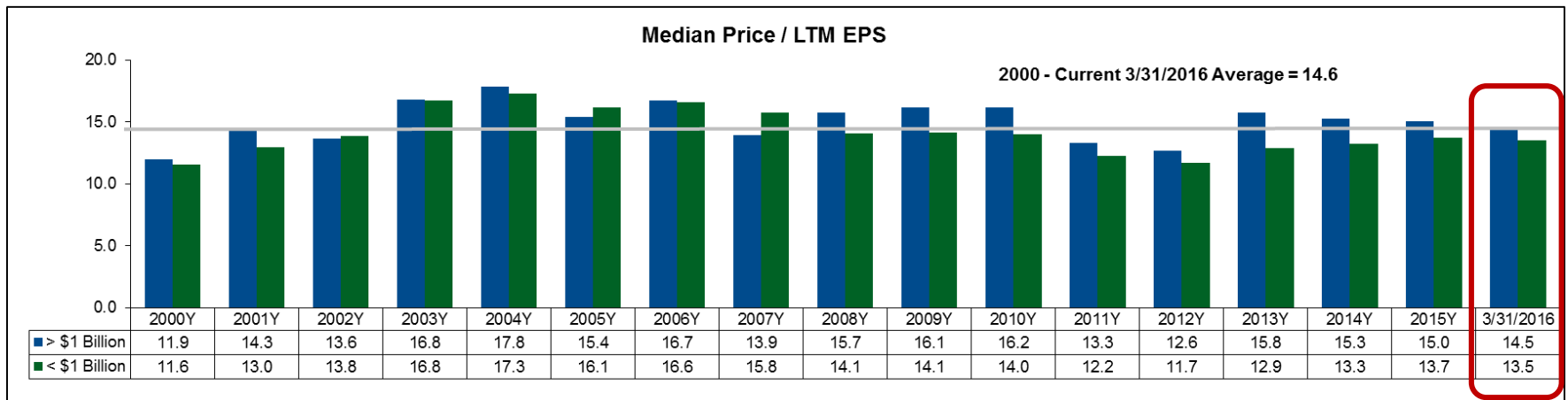
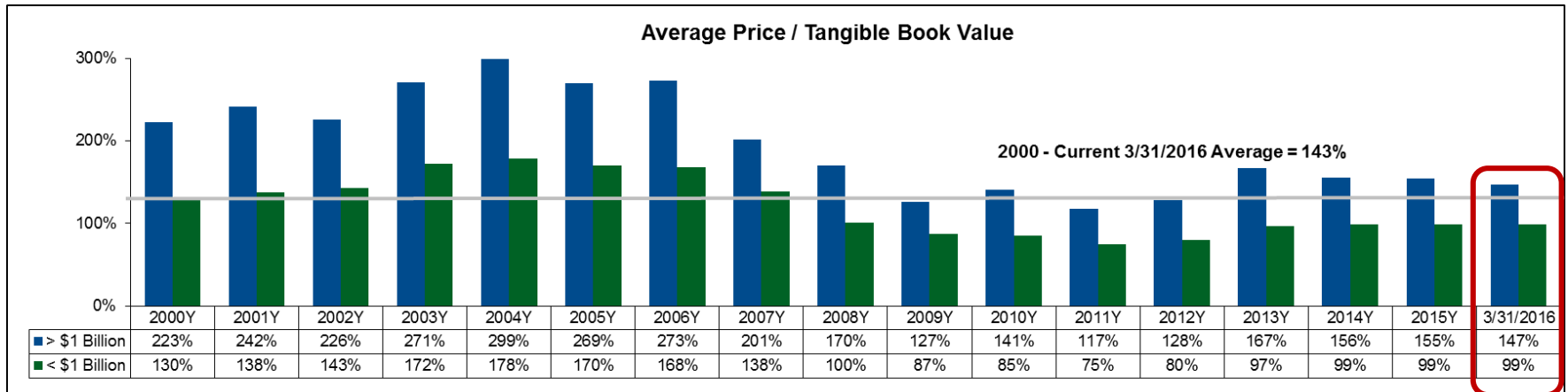
Source: SNL Financial

Note: Results are based on median statistics for all banks and thrifts.

PTPP = Net Interest Income (FTE if available) + Noninterest Income – Noninterest Expense.

BANK EQUITY VALUES

Publicly-Traded Banks & Thrifts Since 2000

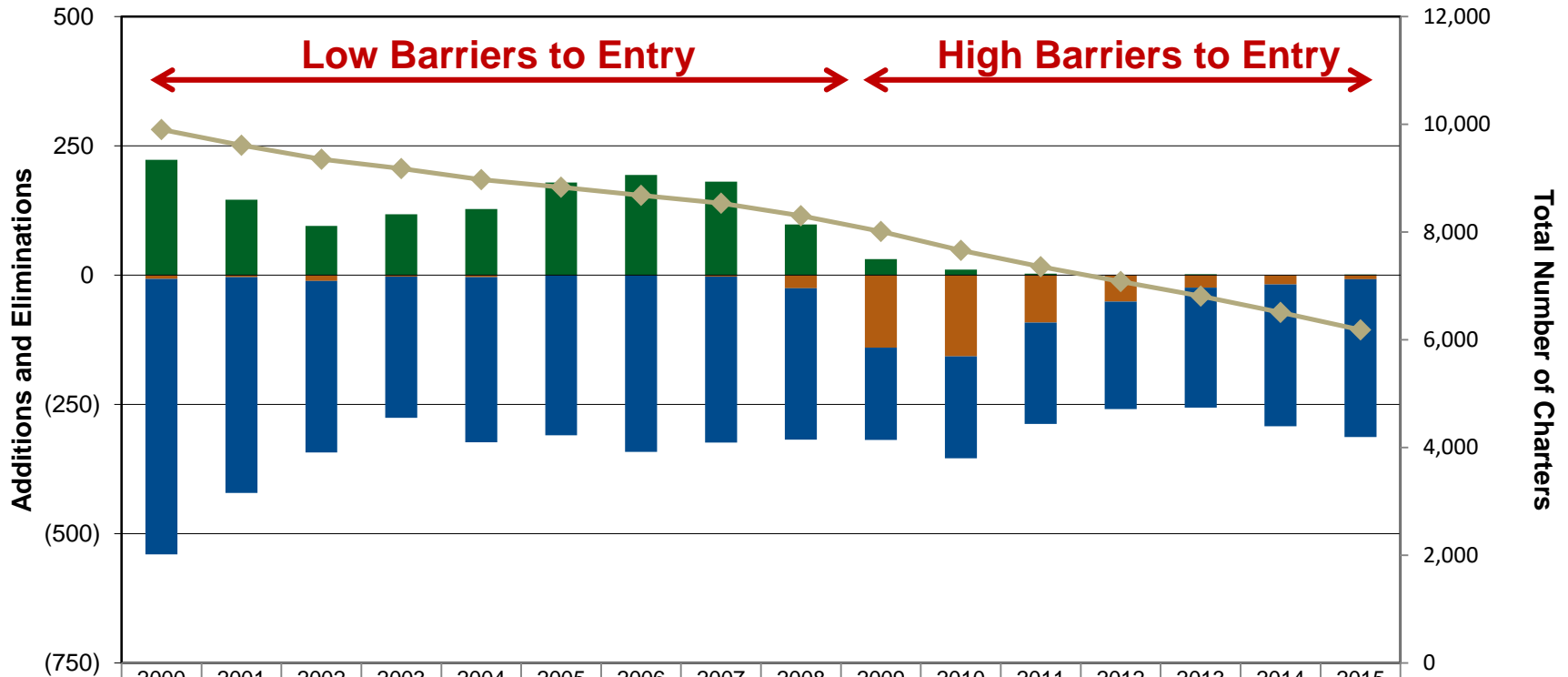


Source: SNL Financial.

Note: Earnings based on core performance, if available. Excludes M&A targets and acquired/defunct companies.

CONSOLIDATION TRENDS

Since 2000



	2000	2001	2002	2003	2004	2005	2006	2007	2008	2009	2010	2011	2012	2013	2014	2015
Mergers	(533)	(417)	(332)	(273)	(319)	(310)	(342)	(321)	(293)	(179)	(197)	(196)	(208)	(232)	(274)	(305)
Failed	(7)	(4)	(11)	(3)	(4)	0	0	(3)	(25)	(140)	(157)	(92)	(51)	(24)	(18)	(8)
New Charter	223	146	95	118	128	179	194	181	98	31	11	3	0	2	0	1
Charters	9,904	9,614	9,354	9,181	8,976	8,833	8,680	8,534	8,305	8,012	7,658	7,357	7,083	6,812	6,509	6,182
Y-Y % Chg.	-3.1%	-2.9%	-2.7%	-1.8%	-2.2%	-1.6%	-1.7%	-1.7%	-2.7%	-3.5%	-4.4%	-3.9%	-3.7%	-3.8%	-4.4%	-5.0%

Source: All data from FDIC's Statistics At A Glance.

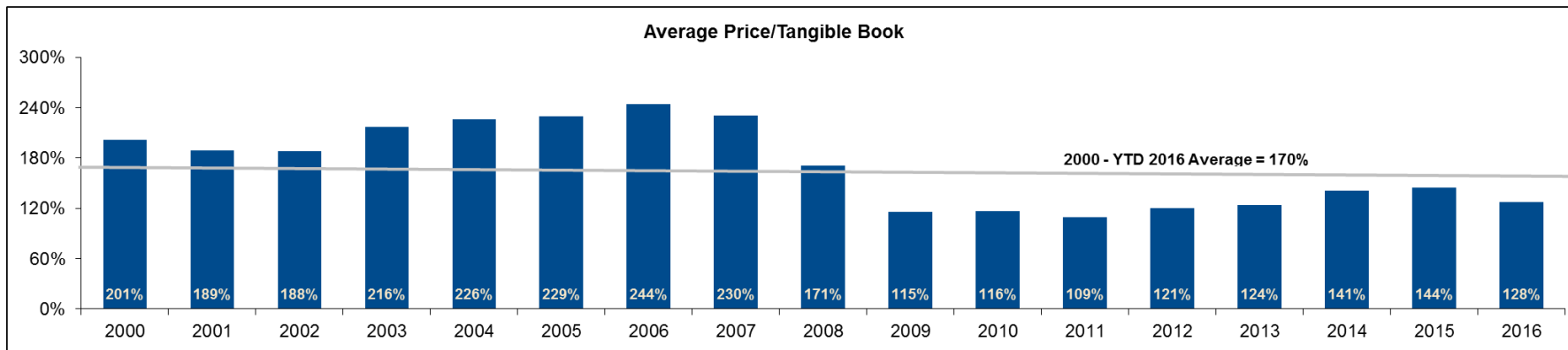
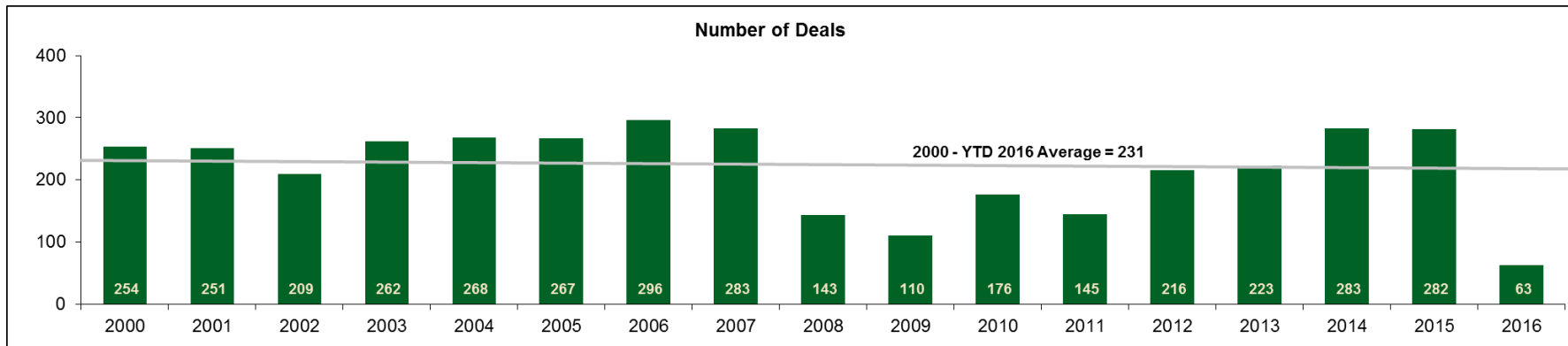
FUTURE OF DE NOVO BANKS

FDIC Release – April 6, 2016

- Rescinded FIL 50-2009 which had extended the de novo status period from 3 to 7 years
- The FDIC noted that new regulations, guidance and risk management practices for all banks address the objectives of FIL 50-2009
- FDIC Chairman, Martin J. Gruenberg noted:
 - “The entry of new banks has helped preserve the vitality of the community banking sector over time.”
 - “De novo institutions fill important gaps in our local banking markets, providing credit and services to communities that may be overlooked by larger institutions.”
 - “The FDIC welcomes applications for deposit insurance.”

ANNUAL M&A VOLUME & PRICING

Since 2000

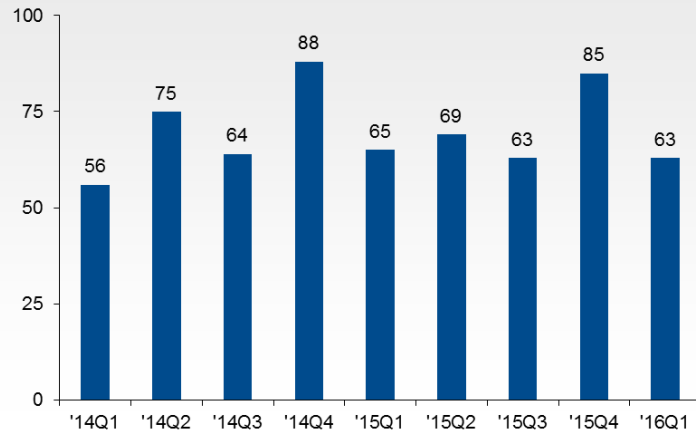


Source: SNL Financial.
 2016 data through March 31, 2016. (YTD 2016 # of deals have been annualized for average calculation)

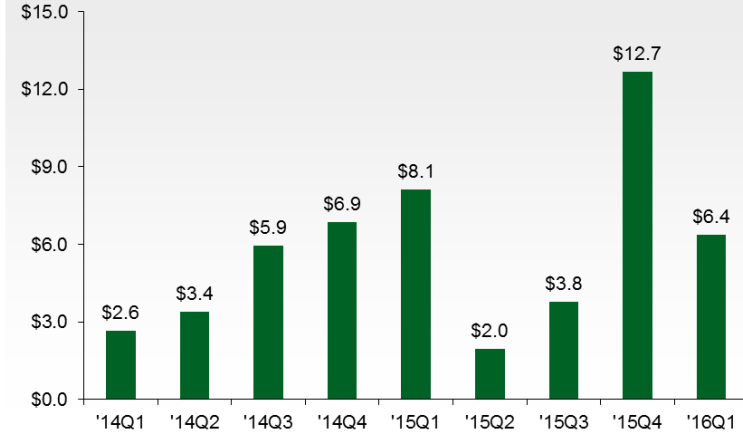
QUARTERLY M&A DATA

1Q 2014 – 1Q 2016

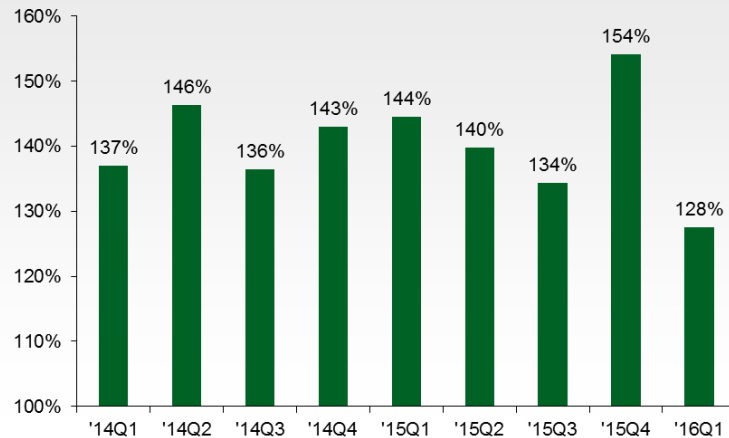
Quarterly M&A Transaction Activity



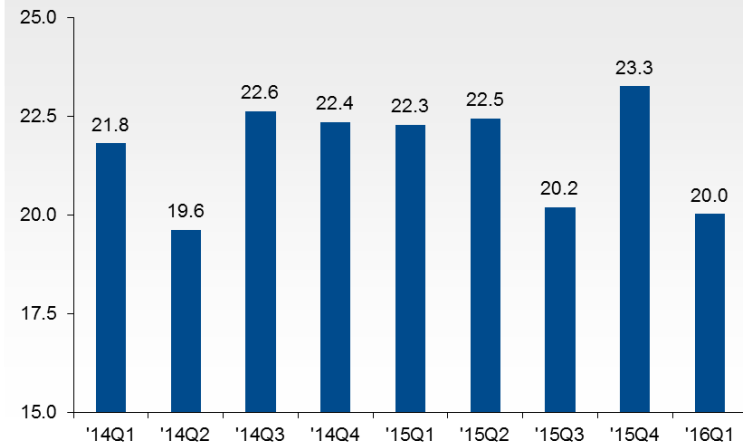
Quarterly M&A Deal Value (\$Billions)



Average Price / Tangible Book Value



Median Price / Earnings



M&A PRICING STATS

Current Market Update 2015 – YTD 2016

	#	Total Assets (\$'000)	Tangible Equity/Assets	LTM ROAA	LTM ROAE	NPAs/Total Assets	Average Price/Book	Average Price/Tg Book	Median Price/LTM EPS
Deals By Seller's Assets									
> 1.0 Billion	26	\$2,295,070	9.41%	0.86%	8.09%	1.21%	169%	184%	21.4
\$500 Million - \$1.0 Billion	33	\$647,487	9.74%	0.76%	6.78%	1.28%	155%	163%	24.2
\$100 - \$500 Million	157	\$195,831	10.15%	0.58%	5.53%	1.35%	130%	132%	22.1
< \$100 Million	125	\$50,252	10.68%	0.33%	2.91%	0.83%	113%	115%	23.0
Deals by Seller's ROAE									
> 10%	50	\$264,692	9.93%	1.19%	12.00%	0.80%	172%	176%	14.0
5% - 10%	120	\$203,428	10.39%	0.74%	6.78%	1.12%	148%	153%	21.1
0% - 5%	106	\$116,369	10.62%	0.31%	2.95%	1.16%	121%	125%	37.1
< 0%	54	\$66,576	9.53%	-0.54%	-5.94%	3.79%	91%	93%	NM
Deals by Seller's NPAs/Total Assets									
< 1%	144	\$123,295	10.30%	0.65%	5.69%	0.31%	148%	154%	23.3
1% - 3%	105	\$162,355	10.49%	0.60%	5.71%	1.73%	142%	146%	21.4
3% - 5%	40	\$138,080	10.20%	0.23%	2.50%	3.95%	116%	122%	25.1
> 5%	26	\$106,264	8.53%	-0.52%	-8.65%	7.34%	82%	84%	32.4
Deals by Region									
Mid Atlantic	38	\$233,979	9.96%	0.57%	5.30%	1.16%	130%	141%	22.8
Midwest	145	\$94,116	10.36%	0.54%	5.13%	1.17%	129%	133%	18.8
Northeast	16	\$207,027	9.96%	0.40%	4.34%	1.30%	130%	132%	35.5
Southeast	69	\$245,565	10.20%	0.61%	6.13%	2.04%	144%	146%	22.2
Southwest	42	\$123,590	10.10%	0.59%	5.79%	0.44%	146%	154%	22.3
West	34	\$149,393	10.92%	0.38%	3.69%	1.10%	131%	138%	25.8
All Bank & Thrift Deals	345	\$143,213	10.27%	0.57%	5.18%	1.22%	135%	141%	22.4

Source: SNL Financial. YTD 2016 data through March 31, 2016.

Note: Based on median statistics. S-Corporation selling companies have been adjusted to C-Corporation status using a 34% tax rate.

BUY-SIDE PERSPECTIVE

BUY-SIDE PERSPECTIVE

Conventional Wisdom

“Acquisitions are notoriously dangerous. Most, not all, acquisitions fail to increase the acquirer's shareholder value.”

Source: Recent M&A Deals Suffer from Overly Rosy Projections [American Banker article – January 4, 2016]

“PROOF” OF CONVENTIONAL WISDOM ??

- Analysis screened for Buyers that have underperformed the banking sector
- SNL compiled list of deals from January 1, 2011 to December 7, 2014
 - Deal value at least \$250 million
 - No MOEs
 - Target less than 75% of buyer’s assets
 - 30 deals made the cut
- “Relative Total Return” – Buyer’s stock price change relative to SNL Bank & Thrift Index
 - 5 of the 30 buyers were down more than 4% on deal announcement date
 - Median relative total return on announcement date – negative 1.5%

Source: Banks in the Penalty Box [American Banker article – December 11, 2015]

RECENT HIGH PROFILE DEALS

Negative Market Reaction

	KeyCorp/ First Niagara	New York Community/ Astoria
Announcement Date	10/30/15	10/29/15
Deal Value	\$4.2 billion	\$2.0 billion
Seller Assets	\$39 billion	\$15 billion
Seller Assets/Buyer Assets	41%	31%
1 Day Price Change	(7.2%)	(13.8%)
5 Day Price Change	(4.3%)	(15.0%)
12/31/15 Price Change	(1.4%)	(14.8%)

CHALLENGING CONVENTIONAL WISDOM

Austin Associates, LLC Research

Screen Criteria

- Deal announcement in 2014 and 2015
- Publicly traded buyer
- Deal value \$25M to \$100M
- 85 transactions met criteria

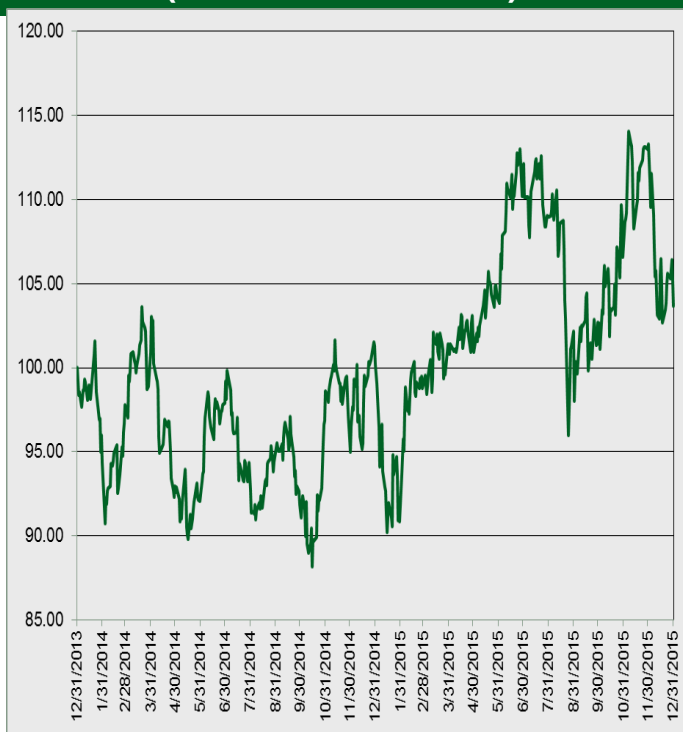
Buyer “Relative Total Return” v. KBW Regional Bank Index

	<u>1 Day</u>	<u>5 Days</u>
25 th Pct	-0.3%	-0.8%
Median	0.0%	0.8%
75 th Pct	1.2%	3.3%

DEALS ANNOUNCED IN 2014 AND 2015

Publicly Traded Buyer; Deal Values between \$25M and \$100M

**KBW Regional Bank Index
(12/31/13 – 12/31/15)**



Nominal Total Return

	Post-Announcement		Deal	As of
	<u>1-Day</u>	<u>5-Day</u>	<u>Closing</u>	<u>12/31/15</u>
25 th Pct	-1.2%	-1.1%	-1.9%	0.7%
Median	0.0%	0.9%	3.7%	7.6%
75 th Pct	1.1%	3.0%	10.2%	23.0%

Note: Graph indexed at 100 and based on December 31, 2013 close of 79.07.
(Increased 3.7% from 12/31/2013 – 12/31/2015)

CASE STUDY #1

Home Bancorp, Inc. acquisition of Louisiana Bancorp, Inc.

Deal Overview and Parties Involved

Announced Deal Value \$74.6 million
 Announcement Date 6/18/2015
 Completion Date 9/15/2015

Buyer
Lead Bank Home Bank, NA
 Parent Company Home Bancorp, Inc.
 Exchange/Ticker NASDAQ/HBCP
 Headquarters Lafayette, LA
 # of Offices 27
 # of FTEs 313

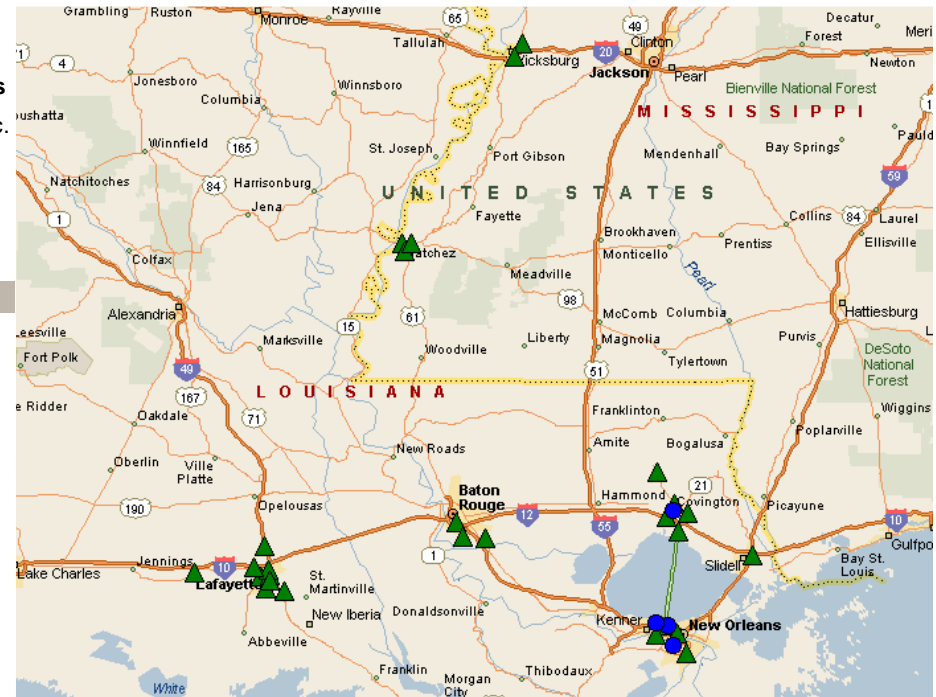
Seller
Lead Bank Bank of New Orleans
 Parent Company Louisiana Bancorp, Inc.
 Exchange/Ticker NASDAQ/LABC
 Headquarters Metairie, LA
 # of Offices 4
 # of FTEs 71

Financial Highlights at Announcement - As of March 31, 2015 (\$000)

Reporting Entity	HBCP	LABC
Total Assets	\$1,233,856	\$330,738
Total Loans	\$927,712	\$276,994
Total Deposits	\$1,026,573	\$200,710
Core Deposits (1)	\$810,642	\$103,222
Total Equity	\$156,782	\$58,946
Tangible Equity	\$152,699	\$58,946
LTM Net Income	\$11,287	\$2,866
LTM ROAA	0.91%	0.88%
LTM ROAE	7.45%	4.94%
LTM Efficiency Ratio	63.4%	65.3%
Total NPAs (2)	\$23,336	\$1,525
NPAs / Total Assets	1.89%	0.46%
Tier 1 Leverage Ratio	12.38%	17.82%
Total RB Capital Ratio	18.32%	NA

(1) Total deposits less time deposits.

(2) NPAs include nonaccrual loans, OREO and restructured loans.



▲ Home Bancorp, Inc.

● Louisiana Bancorp, Inc.

CASE STUDY #1

Home Bancorp, Inc. acquisition of Louisiana Bancorp, Inc.

	Date	HBCP Stock \$	Price Change %
Day Prior	06/17/15	\$22.94	-----
1-Day After	06/19/15	\$24.40	6.4%
5-Days After	06/23/15	\$24.86	8.4%
Closing	09/15/15	\$25.06	9.2%
12/31/15 Price		\$25.98	13.3%

KBW Regional Bank Index Value	Index = 100 6/17/15	HBCP Relative Total Return
86.52	100.0	-----
87.13	100.7	5.7%
89.18	103.1	5.3%
82.38	95.2	14.0%
81.97	94.8	18.5%

CASE STUDY #1

Home Bancorp, Inc. acquisition of Louisiana Bancorp, Inc.

Consideration

- \$74.5 million in total consideration (\$71.2M including benefit from ESOP and MRRP)
- 100% cash

Valuation Multiples

- 126% of tangible book value (121% adjusted for ESOP/MRRP benefit)
- 146% of TBV based on 8% equity to assets
- 26.0 price-to-earnings (24.8x P/E as adjusted)

Key Assumptions

- \$4.4 million pre-tax cost savings (55% of total noninterest expense)
- \$4.2 million gross credit mark
- \$5.5 million of estimated pre-tax merger expenses

Key Financial Metrics

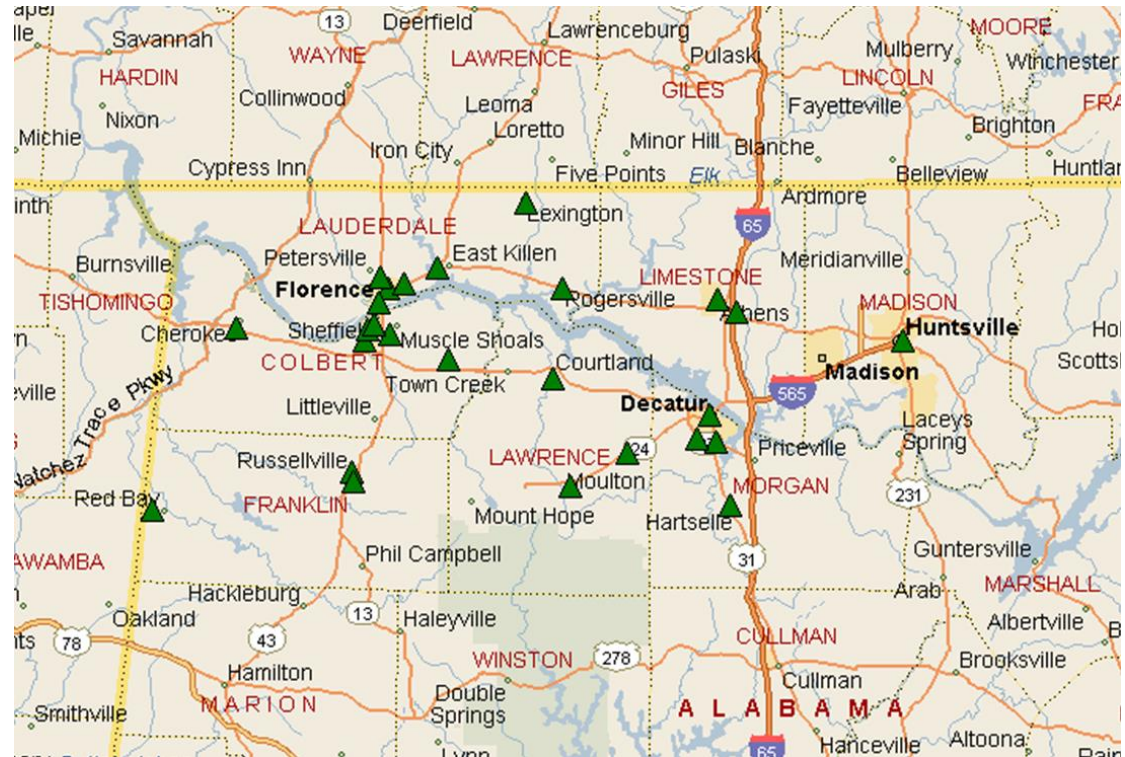
- 35% accretive to 2016 estimated EPS
- < 10% tangible book value dilution at closing; 3.5 year payback
- IRR > 20%
- Pro forma tangible common equity decreases from 12.4% to 9.6%; leverages excess capital

CASE STUDY #2

BancIndependent, Sheffield, Alabama

Company Profile

- Private
- C-Corporation
- \$1.2 billion in assets
- 5 acquisitions over 9 years



CASE STUDY #2

BancIndependent, Sheffield, Alabama

Branch Deal September 2001

- 2 branches from Union Planters Corporation (Memphis, TN)
- \$40 million in total deposits
- Sheffield and Tuscumbia, AL offices

Branch Deal September 2002

- 2 branches from First Southern Bancshares (Florence, AL)
- \$21 million in total deposits
- Florence and Rogersville, AL offices

Branch Deal November 2005

- 17 branches from Colonial BancGroup, Inc. (Montgomery, AL)
- 13 full-service offices and 4 limited service offices
- \$376 million in total deposits and \$64 million in loans

Whole Bank Deal December 2008

- Citizens Bancorp of Lawrence (Montgomery, AL)
- Subsidiary bank = Citizens Bank, Moulton, AL
- \$115 million in total assets

Non-Bank Deal August 2009

- Regions Interstate Billing Services, Inc. (Birmingham, AL)
- Factoring / Commercial Billing Services
- Approximately \$75 million in accounts receivable

BANK INDEPENDENT

Financial Highlights – Balance Sheet (\$Millions)

Bank-Level	2000Y	2001Y	2002Y	2003Y	2004Y	2005Y	2006Y	2007Y	2008Y	2009Y	2010Y	2011Y	2012Y	2013Y	2014Y
Total Assets	\$312	\$367	\$412	\$423	\$410	\$764	\$702	\$743	\$897	\$955	\$989	\$1,041	\$1,082	\$1,102	\$1,176
Total Intangibles	\$0	\$2	\$3	\$3	\$2	\$27	\$25	\$24	\$29	\$28	\$27	\$26	\$25	\$25	\$24
Total Equity	\$29	\$33	\$35	\$36	\$37	\$83	\$86	\$87	\$93	\$117	\$121	\$132	\$131	\$135	\$139
Tangible Common Equity	\$29	\$31	\$32	\$34	\$35	\$56	\$61	\$63	\$64	\$89	\$94	\$106	\$106	\$110	\$115
Parent Company															
Common Equity	\$30	\$33	\$35	\$37	\$37	\$53	\$56	\$57	\$62	\$65	\$69	\$71	\$75	\$80	\$84
Tangible Common Equity	\$30	\$31	\$32	\$34	\$35	\$26	\$31	\$33	\$32	\$37	\$42	\$45	\$50	\$56	\$60
TARP (2009) / SBLF (2011)	\$0	\$0	\$0	\$0	\$0	\$0	\$0	\$0	\$0	\$21	\$21	\$30	\$30	\$30	\$30
Trust Preferred Securities	\$0	\$0	\$0	\$0	\$0	\$31	\$31	\$31	\$31	\$31	\$31	\$31	\$31	\$31	\$31
Long-Term Debt	\$0	\$0	\$0	\$0	\$0	\$0	\$0	\$0	\$0	\$0	\$0	\$0	\$0	\$0	\$0

BANK INDEPENDENT

Financial Highlights – Profitability (\$Millions)

Bank-Level	2000Y	2001Y	2002Y	2003Y	2004Y	2005Y	2006Y	2007Y	2008Y	2009Y	2010Y	2011Y	2012Y	2013Y	2014Y
PTPP	\$4.5	\$4.9	\$6.4	\$5.3	\$4.0	\$5.1	\$9.6	\$11.8	\$10.6	\$16.2	\$21.3	\$21.6	\$20.4	\$17.5	\$18.5
Provision Expense	\$0.0	\$0.0	\$2.8	\$0.9	\$0.6	\$0.5	\$0.7	\$1.1	\$3.8	\$4.7	\$6.3	\$4.4	\$2.7	\$2.6	\$2.6
Net Income	\$3.5	\$3.8	\$3.1	\$3.7	\$2.9	\$3.6	\$6.6	\$8.1	\$5.6	\$7.9	\$10.3	\$12.2	\$12.4	\$10.8	\$11.1
PTPP / Avg. Assets	1.35%	1.51%	1.67%	1.29%	0.97%	1.08%	1.32%	1.65%	1.33%	1.76%	2.22%	2.14%	1.92%	1.62%	1.65%
ROAA	1.04%	1.16%	0.80%	0.91%	0.70%	0.77%	0.91%	1.13%	0.70%	0.85%	1.07%	1.21%	1.17%	1.00%	1.00%
ROATCE	12.42%	12.65%	9.82%	11.44%	8.40%	7.90%	11.27%	13.12%	8.88%	10.29%	11.21%	12.19%	11.69%	10.01%	9.91%
Parent Company															
Net Income	\$3.5	\$3.8	\$3.1	\$3.8	\$2.9	\$3.4	\$5.3	\$6.8	\$4.6	\$6.8	\$9.3	\$11.1	\$11.4	\$9.8	\$10.2
ROAA	1.04%	1.16%	0.80%	0.91%	0.71%	0.73%	0.73%	0.94%	0.57%	0.73%	0.97%	1.10%	1.07%	0.90%	0.90%
ROACE	12.43%	12.05%	8.91%	10.41%	7.81%	8.65%	9.84%	12.05%	7.77%	9.41%	11.84%	14.23%	14.74%	12.28%	11.88%
ROATCE	12.33%	12.53%	9.72%	11.40%	8.39%	11.19%	18.59%	21.25%	14.07%	19.78%	23.55%	25.40%	24.11%	18.45%	17.61%
Dividends	\$1.2	\$1.3	\$1.4	\$1.4	\$1.4	\$1.4	\$2.8	\$2.8	\$2.8	\$3.7	\$4.0	\$3.8	\$4.9	\$2.8	\$3.5

BUY-SIDE PERSPECTIVE

Deal Takeaways

- “Think outside the box” ...but don’t forget strategic fit and culture are essential considerations
- Track record of successfully executed deals favorably impresses both regulators and the market
- Transparency of pro forma modeling assumptions is expected; Market pays close attention to reasonableness
- Maintain financial discipline:
 - EPS accretion/dilution
 - Tangible book value (“TBV”) per share dilution/payback period
 - Internal Rate of Return (“IRR”)
 - Pro forma capital ratios/appropriate leverage
 - Market Optics – guideline transaction multiples



STRATEGIC MERGERS

STRATEGIC MERGERS (“MERGERS OF EQUALS”)

Common Characteristics

- Typically an all stock exchange – sometimes involves a special dividend/cash payment to equate value
- Ownership exchange determined by relative value contribution with little to no premium paid to either party
- Value creation comes from: (i) shared cost savings; (ii) revenue synergies; (iii) enhanced ability to grow; and (iv) enhanced trading multiples
- Negotiated “one-off deal” – not a competitive bid process
- Equal or proportionate (to share ownership) representation on the board and C-level management team
- “Best practices” philosophy often followed with other areas

FACTORS INSPIRING STRATEGIC MERGERS

Performance Challenges and Strategic Factors

- Challenging operating environment (loan growth, NIM pressure)
- Slow organic revenue growth (and outlook for growth)
- Compliance and regulatory costs are increasing
- Talent retention and recruitment/management succession
- Inability to compete in traditional M&A transactions
- Smaller community bank stocks trading at a fair market value discount

STRATEGIC MERGER CASE STUDIES

Deal Profiles

	Deal 1	Deal 2	Deal 3
SEC/Private	Both Private	Both Private	Both Private
Asset Sizes	Both < \$100 mil	Both < \$500 mil	Both < \$500 mil
Asset Contribution	55% / 45%	57% / 43%	48% / 52%
Tangible Common Equity Contribution	55% / 45%	62% / 38%	56% / 44%
Net Income Contribution	90% / 10%	70% / 30%	54% / 46%
Relative Market Cap	N.A.	60% / 40%	56% / 44%
Consideration	Stock + Special Dividend	All Stock	All Stock

STRATEGIC MERGERS

Deal 1: Dealing with Financial Contribution Imbalances

- **Issue – Financial/Value Contribution Imbalance**
 - Smaller party's profitability was very low (barely profitable)
 - Pro forma results in all-stock exchange were not acceptable to larger party

- **Resolution: Special Dividend to Smaller Party to “Buy-down” Ownership**
 - Dividend equal to 27% of equity
 - Equity contribution was adjusted from 55%/45% to 63%/37%
 - Exchange ratio resulted in pro forma ownership of 70%/30%

STRATEGIC MERGERS

Deal 1: Dealing with Financial Contribution Imbalances

- **Pro Forma Results**

- Cost savings estimated at 12.0% of combined expenses

	Party A	Party B
Initial TBVPS Change	8.0%	-20.0%
1 st Year EPS Change	0.0%	150.0%
2 nd Year EPS Change	6.5%	175.0%
TBVPS Recovery Period	Immediate	4.1 years
1 st Year Dividends Per Share Change	0.0%	250.0%

STRATEGIC MERGERS

Deal 2: Supporting a Book-for-Book Exchange

▪ Financial Terms

- Parties agreed to a book-for-book exchange early in the negotiation process
- Equity capital contribution (no intangibles at either party) determined ownership and exchange ratio
- Challenge: smaller party contributing 38% of equity, but less than 30% of net income
- Challenge: allocating one-time costs in the transaction
- Concern: perception that smaller party would be getting a “premium” in the deal

STRATEGIC MERGERS

Deal 2: Supporting a Book-for-Book Exchange

▪ Focus Turned to Pro Forma Analysis

- Attributed majority of cost savings to smaller party – adjusted net income with cost savings approximated equity contribution %
- Considered one-time transaction costs as deal-related – no penalty to smaller party
 - Professional fees
 - Branch closing
 - DP termination fees
 - Severance payments
- Considered dividend differential in computing TBV payback period

STRATEGIC MERGERS

Deal 2: Pro Forma Results

- **Pro Forma Results**

- Cost savings estimated at 9.0% of combined expenses

	Party A	Party B
Initial TBVPS Change	-3.5%	-3.7%
1 st Year EPS Change	2.0%	25.0%
2 nd Year EPS Change	15.0%	35.0%
TBVPS Recovery Period	2.7 years	1.5 years
1 st Year Dividends Per Share Change	0.0%	125.0%

STRATEGIC MERGERS

Deal 3: Dealing with Nonfinancial Issues in a “MOE” Transaction

▪ Typical List of Nonfinancial Issues

- Company and bank name - which company/charter survives
- Company and bank headquarters
- Resulting board of directors - # of seats each / titles
- Resulting CEO and transition plan, if applicable
- Senior management structure – all C-level positions
- Employment contracts / severance / stay bonuses
- Resulting benefit plans
- Registration or exemption of securities being issued

Note: All of these were in play for Deal 3

STRATEGIC MERGERS

Deal 3: Dealing with Nonfinancial Issues in a “MOE” Transaction

- **Major Nonfinancial Issues in Deal 3**
 - Resolving integration plan – operate with one or two bank charters
 - Determining titles, roles, responsibilities of CEOs (neither ready to retire)
 - Data processing integration – in-house vs. service bureau and excessive termination fee on DP contract

- **Accounting Issues**
 - Accounting “buyer” and “seller” determined
 - Agreed to separate fair value adjustments from exchange ratio analysis
 - Fair value adjustments applied to “seller” including
 - Credit mark on loan portfolio (LLR eliminated)
 - Mark to market the frozen pension plan underfunded liability

STRATEGIC MERGERS

Deal 3: Dealing with Nonfinancial Issues in a “MOE” Transaction

▪ Securities Issues

- Company issuing securities is almost always the accounting buyer
- Both parties in Deal 3 were non-reporting companies
- Securities issued must be either:
 - Registered with the SEC
 - OR
 - Issued under an appropriate exemption (typically intrastate or Reg. D offering)
 - OR
 - State Fairness Hearing
- In this case, parties determined to register with SEC (strategic decision)
 - Added costs of \$150k to register + estimated \$100k/year

STRATEGIC MERGERS

Deal Takeaways

- Strategic mergers can be structured with MOE elements regardless of size and ownership split
- A cash component can be used to equalize capital and/or improve pro forma results
- Agreement on financial assumptions will be necessary:
 - Fair value accounting adjustments
 - Transaction and one-time costs
 - Cost savings and synergies
- Negotiate financial terms in conjunction with nonfinancial issues – “total package”

2016 Austin Webinar Series

***“The Critical Role of Operating Efficiency in
Producing High-Performance Community Banks”***

Wednesday, May 25 at 11 a.m.

Jeff Morris, Managing Director and Principal, Financial Management

M&A Case Studies

Enhancing Your Community Bank's Value

Thank you for joining us today! We would appreciate hearing from you.

If you have questions or comments regarding today's webinar, or if you would like to discuss how Austin Associates can assist your bank with any aspect of M&A, please contact us.

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