

Prepared for:



By:



September 8, 2014

Community Bank Valuation Themes & Trends



Geographic and Economic Factors

- Market growth potential
- Competitiveness

Bank-Specific Factors

- Earnings
- Growth potential
- Spread business performance
- Management
- Capital
- Asset Quality



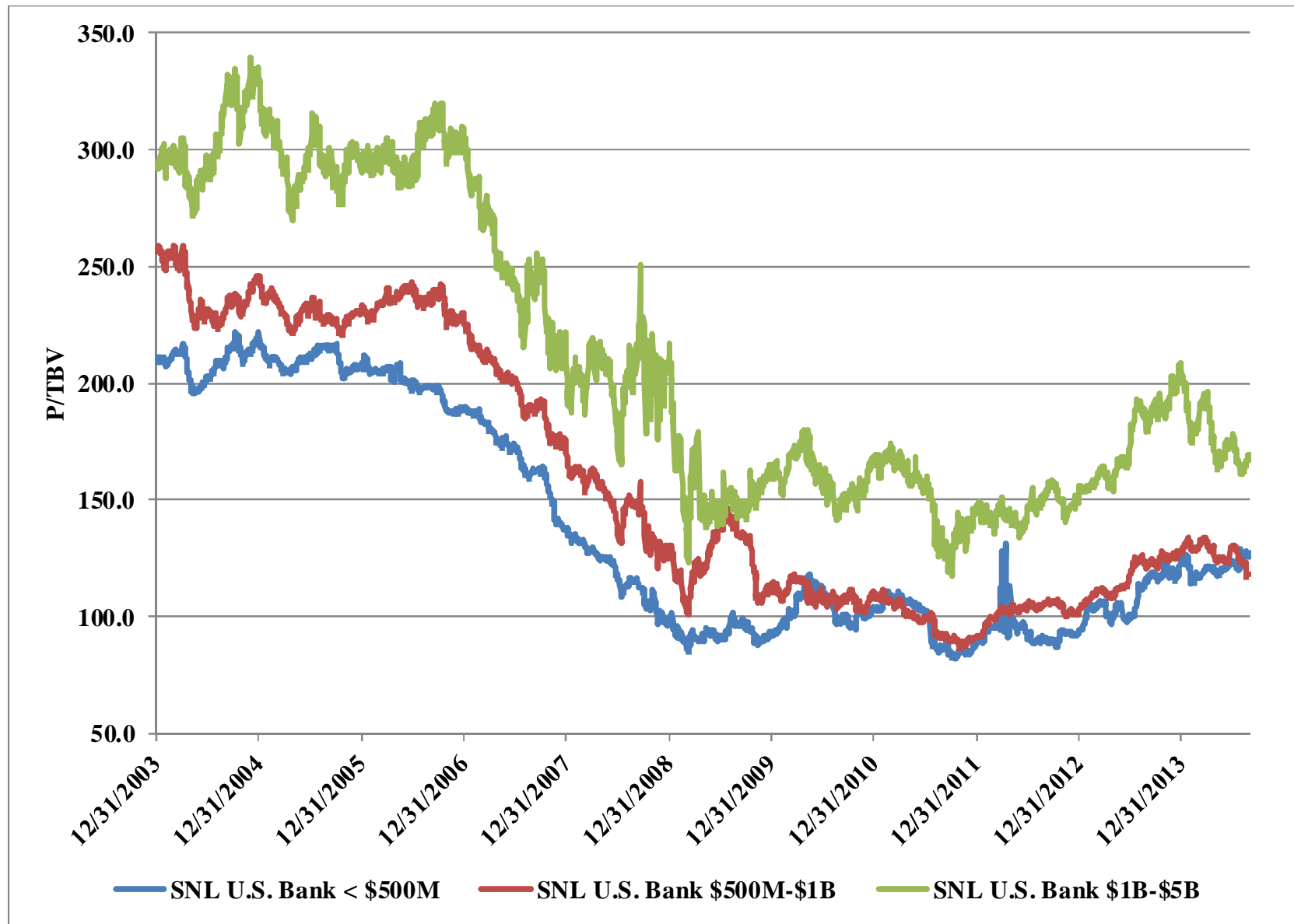
Industry-Specific Factors

- Impact of Dodd-Frank and Basel III on:
 - Business Model
 - Earnings
 - Capital
 - Competitive factors and exit multiples

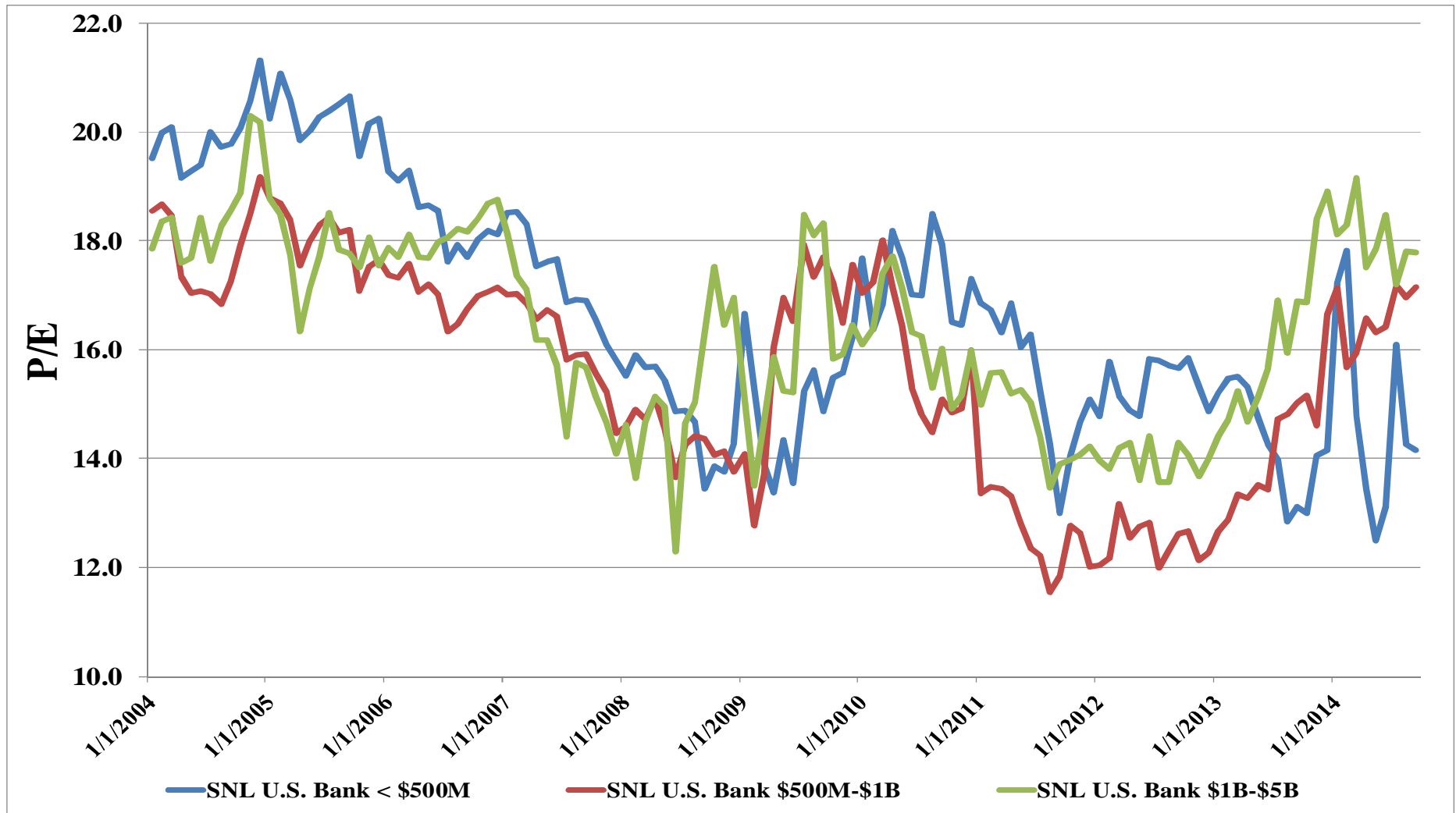
Market Structure Factors

- SEC Registration
- Exchange Listing vs. Marketplace
- Market cap / ADTV
- Index inclusion
- Presence of a dividend

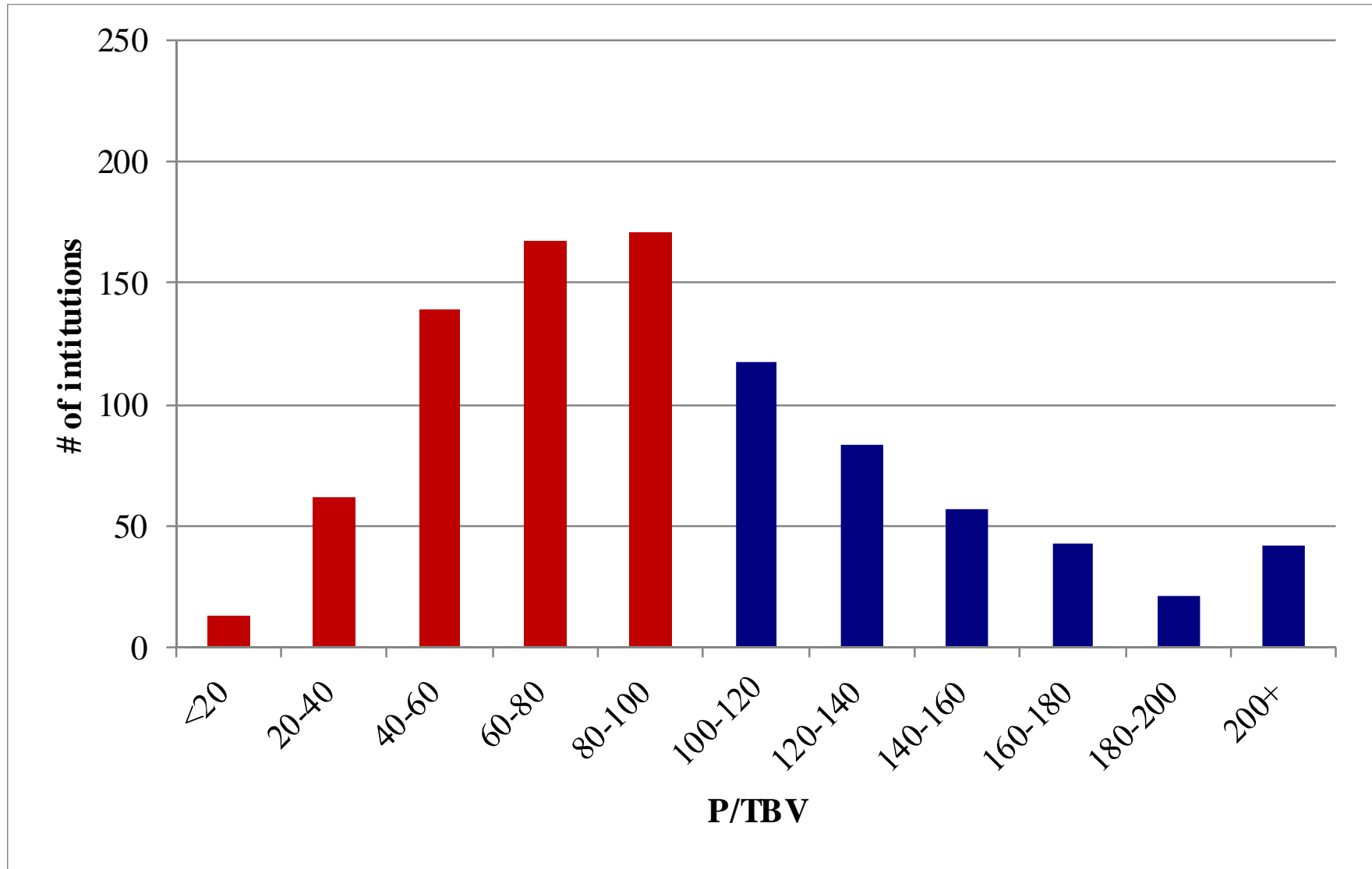
Valuations Continue To Improve - P/TBV



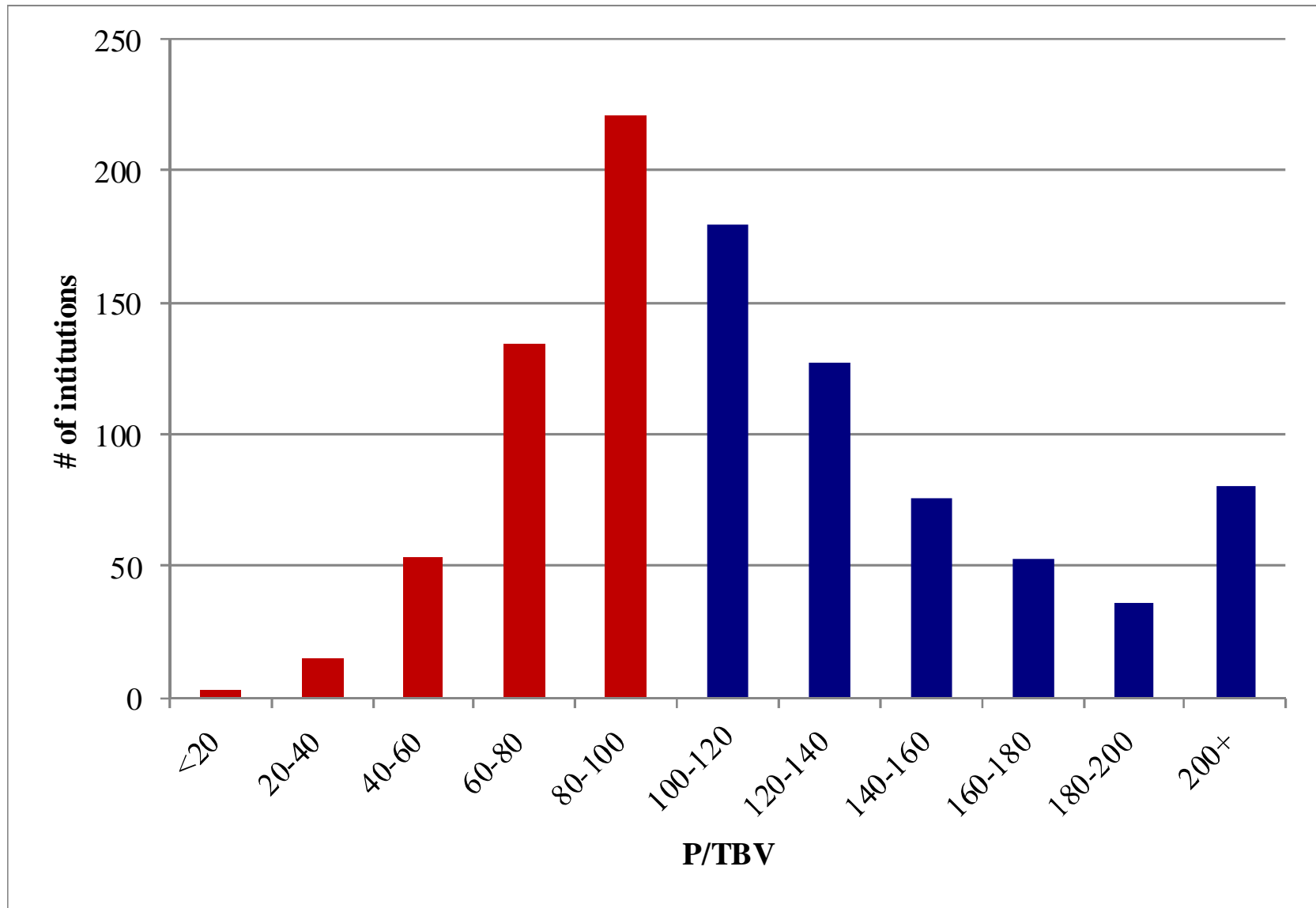
Valuations Continue To Improve - P/ LTM Earnings



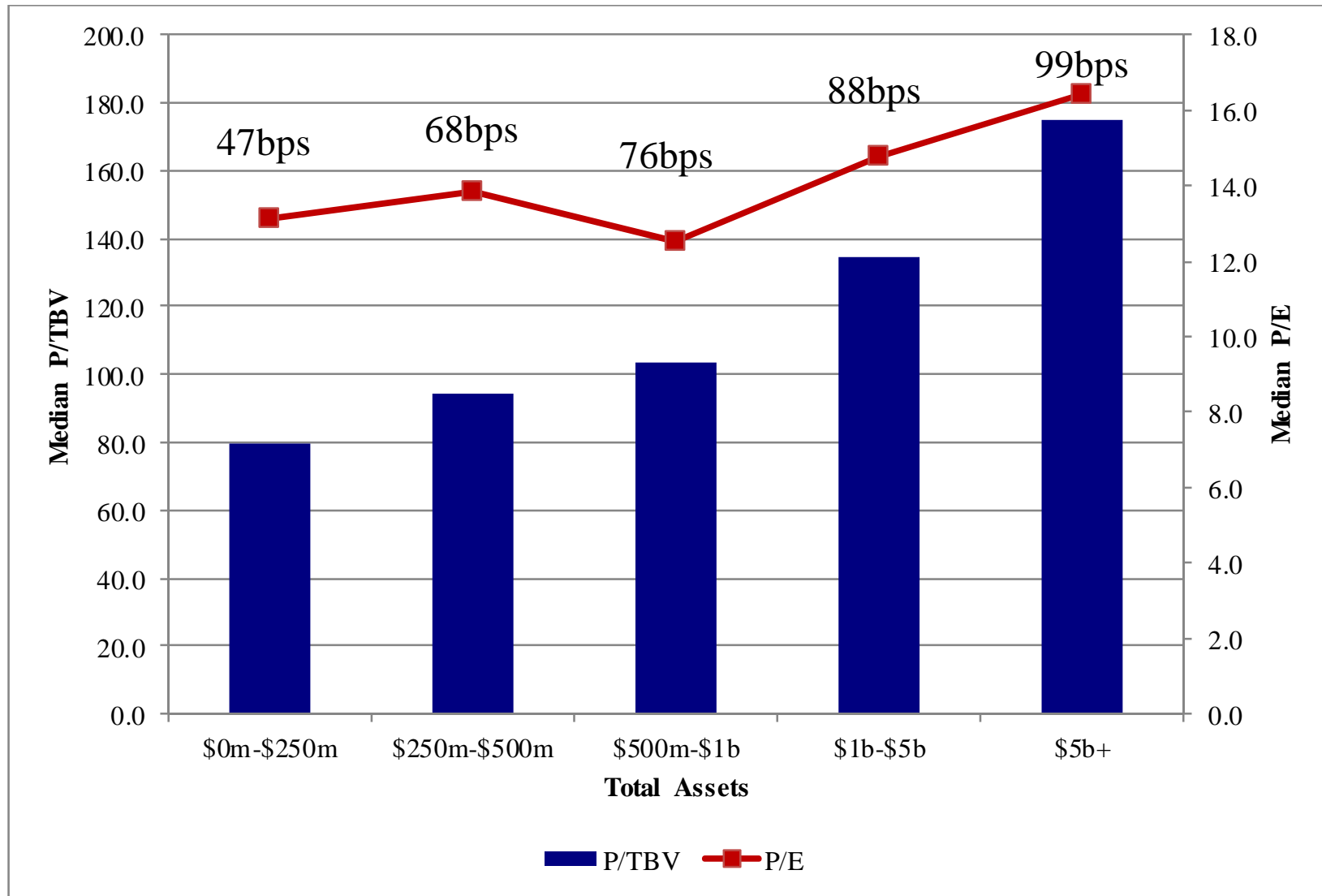
National Institutions by P/TBV Bands - 2009



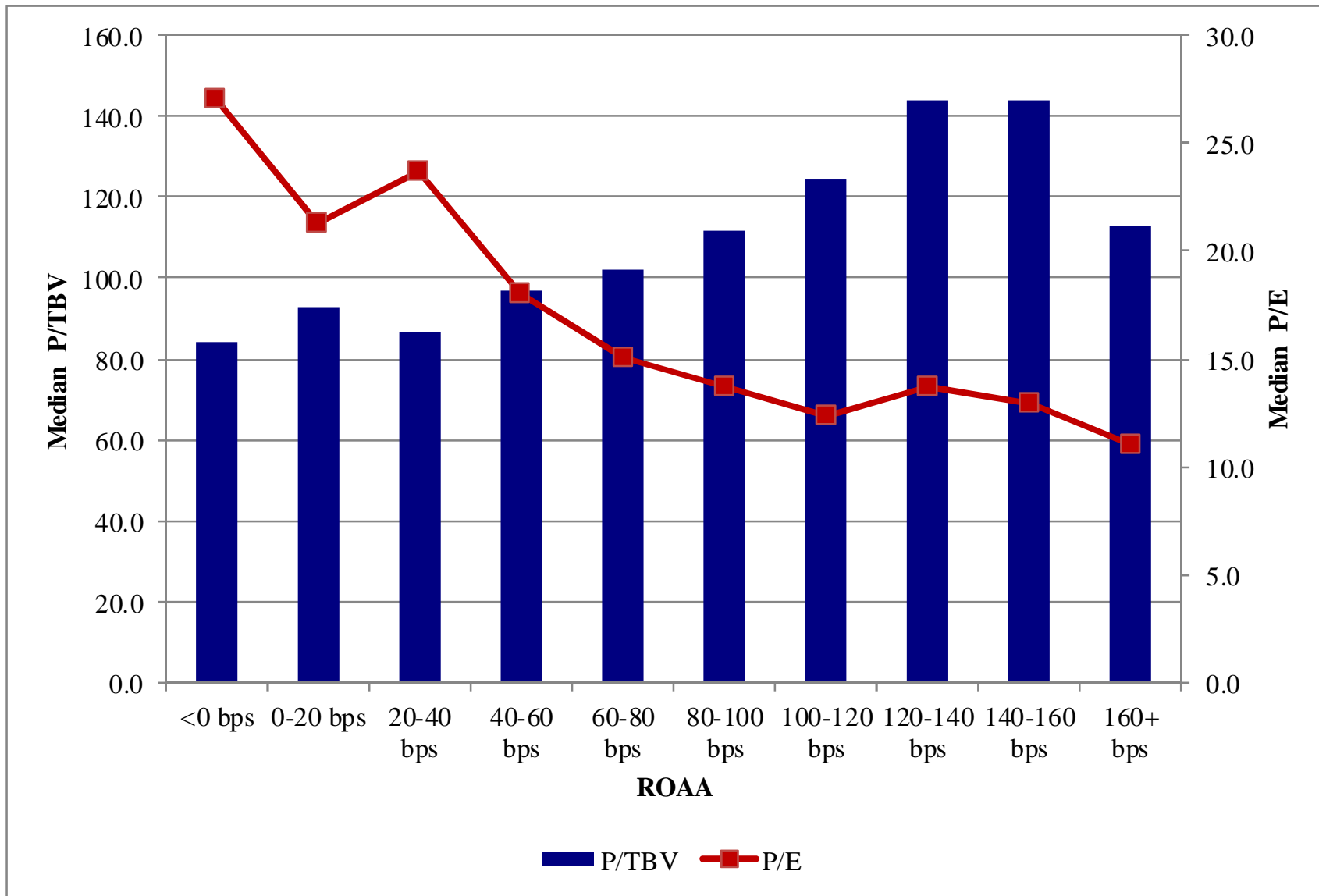
National Institutions by P/TBV Bands - Today



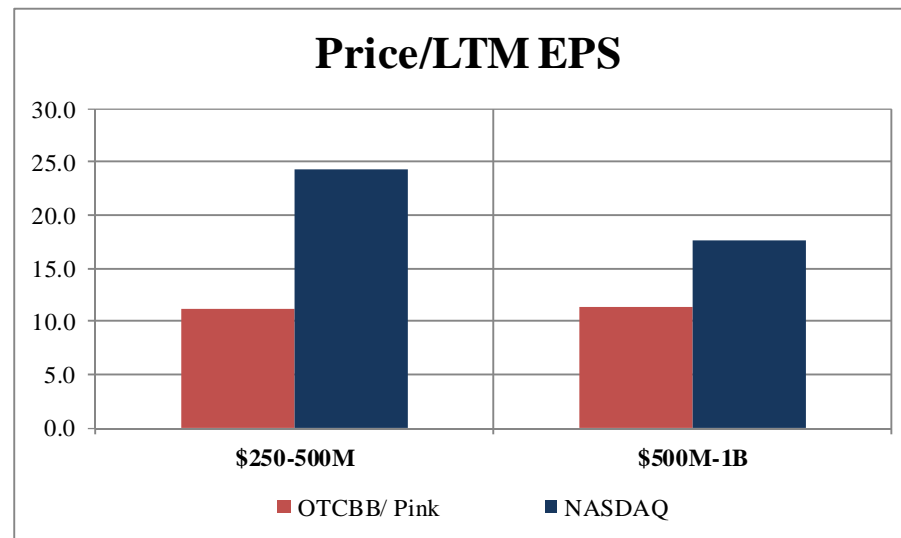
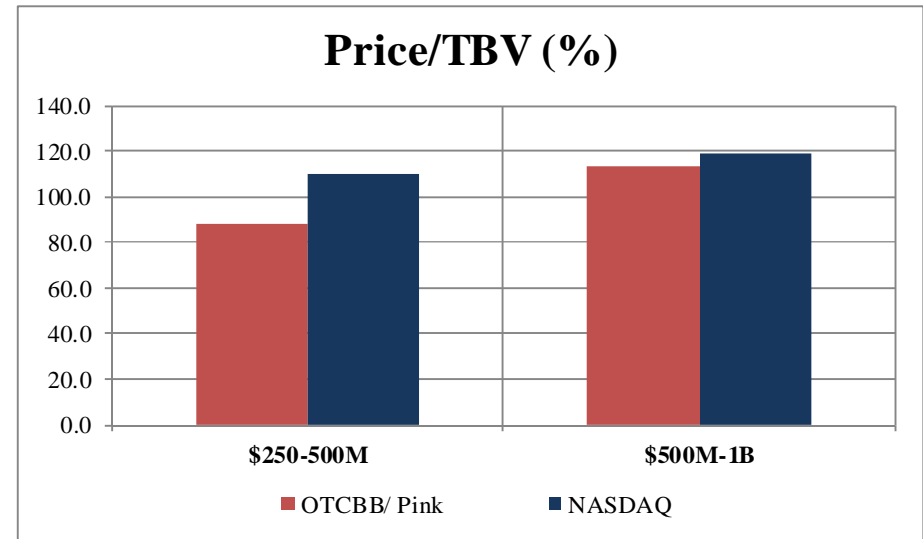
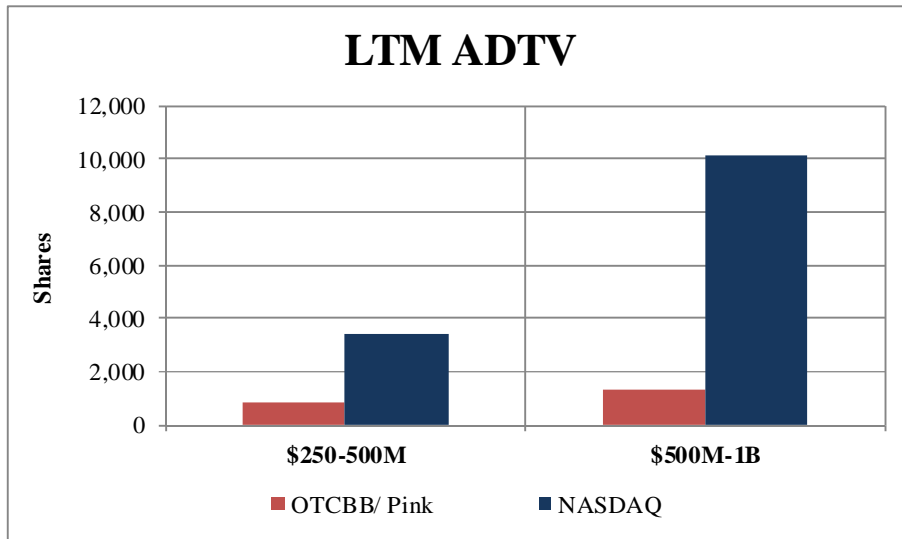
Valuation by Asset Size - National



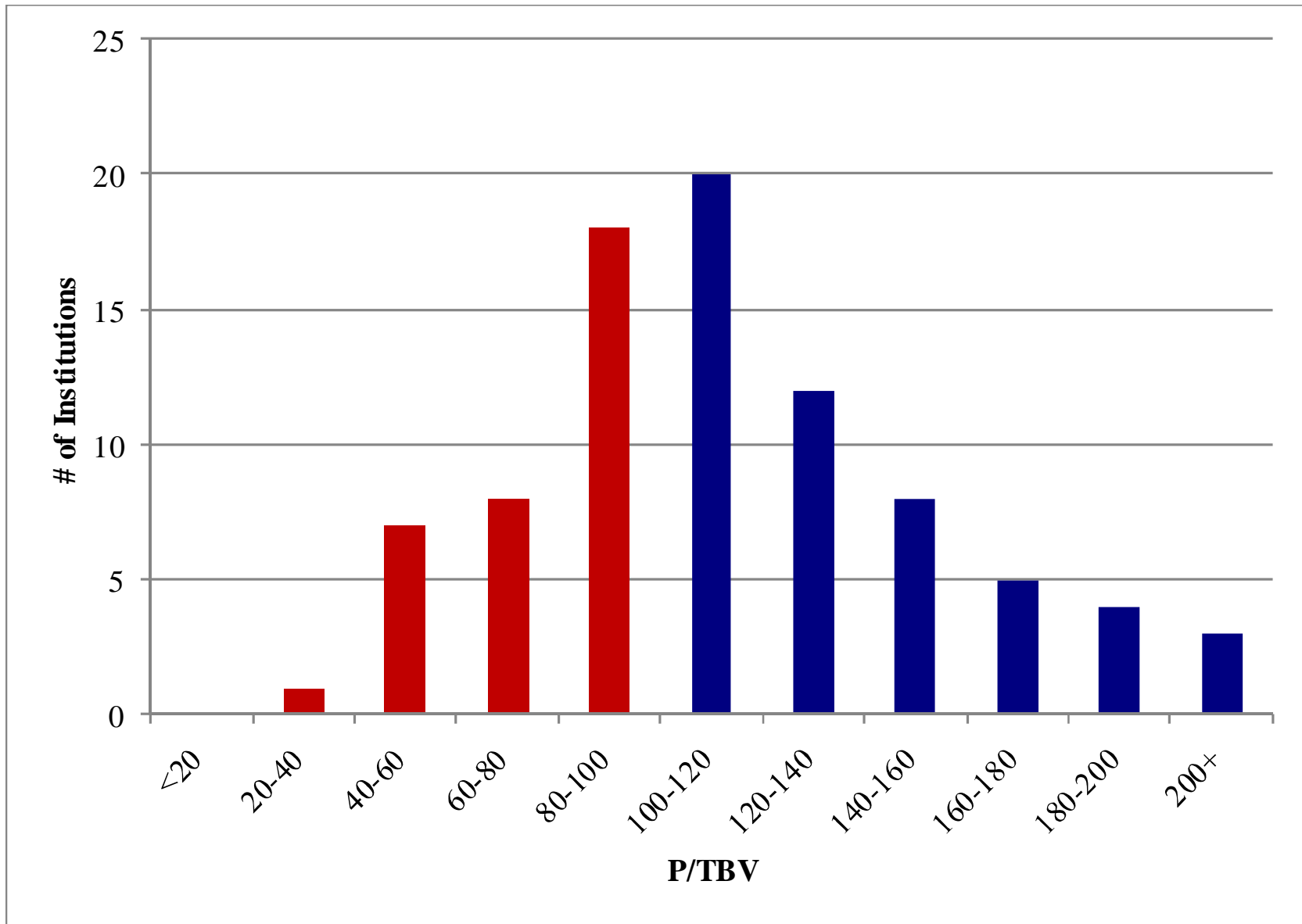
Valuation By ROA Bands - National



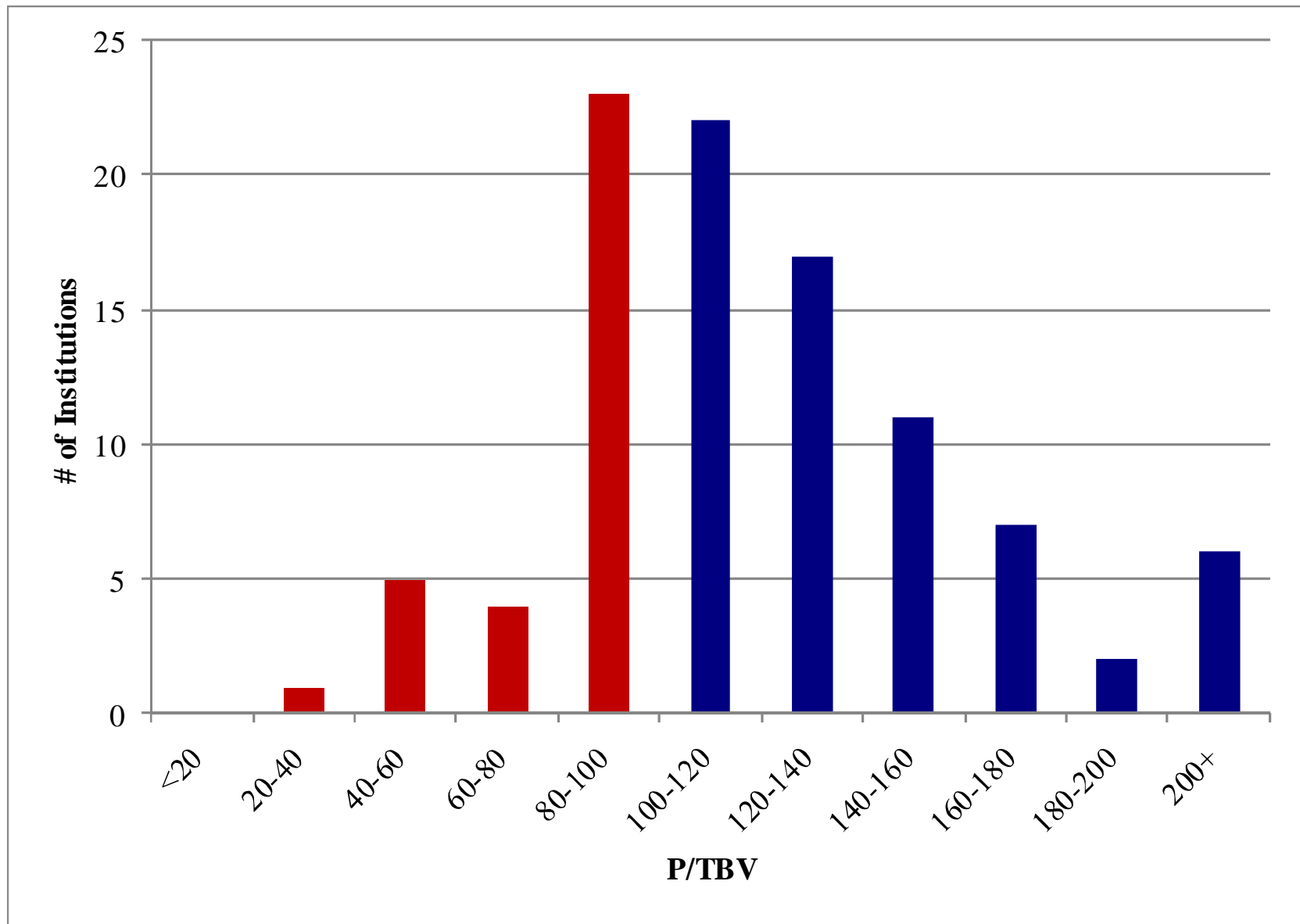
Valuation by Size & Exchange < \$1 BN Nationally



Pennsylvania Institutions by P/TBV Bands - 2009



Pennsylvania Institutions by P/TBV Bands - Today



PA Stock Performance – Assets of \$1 BN+

Institution Name	Ticker	Exchange	Total Assets (\$'000) MRQ	Market Cap. (\$M)	Avg. Daily Volume One Year	Price/ LTM EPS (x)	Price/ TBV (%)	Dividend Yield (%)	Total Return (%) One Year	Total Return (%) Three Year	Total Return (%) Five Year	Institutional Ownership (%)
<i>> \$5 Billion in Assets</i>												
Susquehanna Bancshares, Inc.	SUSQ	NASDAQ	18,506,626	1,929.6	1,381,474	11.6	129.1	3.5	(16.4)	84.2	110.3	74.4
Fulton Financial Corporation	FULT	NASDAQ	17,033,639	2,170.9	1,123,839	13.4	139.4	2.8	(0.1)	50.6	83.7	55.2
F.N.B. Corporation	FNB	NYSE	15,019,247	2,105.3	904,136	15.8	220.6	3.8	9.0	72.0	142.8	66.3
National Penn Bancshares, Inc.	NPBC	NASDAQ	8,618,373	1,408.1	681,280	15.1	168.1	4.0	2.2	71.7	120.4	64.1
Northwest Bancshares, Inc.	NWBI	NASDAQ	7,902,316	1,184.2	541,412	17.6	132.6	4.2	4.2	36.2	75.0	63.6
First Commonwealth Financial Corporation	FCF	NYSE	6,300,222	836.9	447,743	17.2	148.7	3.1	26.4	149.8	68.5	61.1
Group Mean			57,206,346	7,768.8	1,022,850	14.6	154.9	3.4	5.6	75.9	108.8	66.7
Group Median			15,019,247	1,929.6	904,136	15.1	145.9	3.5	4.2	71.7	110.3	64.1
<i>\$1-5 Billion in Assets</i>												
Customers Bancorp, Inc.	CUBI	NASDAQ	5,635,728	484.6	130,259	14.2	118.2	NA	21.2	NA	NA	74.3
S&T Bancorp, Inc.	STBA	NASDAQ	4,788,030	747.9	52,856	14.2	178.8	2.7	14.4	67.8	131.6	48.2
Beneficial Mutual Bancorp, Inc. (MHC)	BNCL	NASDAQ	4,425,734	1,028.8	105,246	NM	213.4	NA	46.9	88.2	51.3	23.1
Metro Bancorp, Inc.	METR	NASDAQ	2,868,928	329.2	28,384	17.2	132.8	NA	16.8	149.5	38.6	76.7
Univest Corporation of Pennsylvania	UVSP	NASDAQ	2,197,252	310.7	41,423	14.5	143.9	4.2	4.7	68.3	14.7	46.0
CNB Financial Corporation	CCNE	NASDAQ	2,156,665	238.9	23,983	11.4	163.7	4.0	3.7	48.7	28.5	31.6
Bryn Mawr Bank Corporation	BMTC	NASDAQ	2,131,225	407.7	30,930	15.0	211.7	2.6	22.3	84.3	92.2	68.0
ESB Financial Corporation	ESBF	NASDAQ	1,940,450	224.3	15,043	13.4	137.9	3.2	8.3	54.2	57.5	15.5
Peoples Financial Services Corp.	PFIS	NASDAQ	1,731,106	384.2	13,485	41.4	220.0	2.4	49.4	103.3	246.1	18.9
ESSA Bancorp, Inc.	ESSA	NASDAQ	1,559,178	135.2	26,628	15.3	85.8	2.4	13.4	13.5	(0.7)	37.6
Citizens & Northern Corporation	CZNC	NASDAQ	1,256,205	245.2	22,700	14.3	139.2	5.2	6.0	57.2	30.5	28.8
Penns Woods Bancorp, Inc.	PWOD	NASDAQ	1,222,847	218.5	10,713	16.0	186.6	4.1	1.5	55.6	78.8	20.8
Codorus Valley Bancorp, Inc.	CVLY	NASDAQ	1,200,638	120.0	4,393	10.3	118.0	2.3	31.8	168.3	334.2	31.0
Orrstown Financial Services, Inc.	ORRF	NASDAQ	1,167,308	131.8	12,821	13.4	129.3	-	(0.2)	19.8	(53.5)	30.8
Fox Chase Bancorp, Inc.	FXCB	NASDAQ	1,105,072	205.2	22,705	28.4	115.6	2.8	5.0	48.1	101.1	65.7
Republic First Bancorp, Inc.	FRBK	NASDAQ	1,065,134	168.7	77,147	NM	151.4	NA	36.0	141.1	(27.2)	46.1
AmeriServ Financial, Inc.	ASRV	NASDAQ	1,063,717	62.2	21,999	13.2	75.6	1.2	3.1	63.7	69.5	39.7
ACNB Corporation	ACNB	NASDAQ	1,045,925	113.9	3,662	12.2	113.5	4.0	16.1	43.1	93.2	8.5
Franklin Financial Services Corporation												
Group Mean			2,142,286	308.7	35,799	16.5	146.4	2.9	16.7	75.0	75.7	39.5
Group Median			1,645,142	231.6	23,344	14.2	138.5	2.8	13.9	63.7	57.5	34.6

PA Stock Performance – Assets \$500 M - \$1 BN

Institution Name	Ticker	Exchange	Total Assets (\$000) MRQ	Market Cap. (\$M)	Avg. Daily Volume One Year	Price/ LTM EPS (x)	Price/ TBV (%)	Dividend Yield (%)	Total Return (%) One Year	Total Return (%) Three Year	Total Return (%) Five Year	Institutional Ownership (%)
1												
<i>\$500 Million - \$1 Billion in Assets</i>												
First National Community Bancorp, Inc.	FNCB	OTCQB	957,875	102.9	2,595	7.4	210.9	-	56.3	150.0	1.2	-
QNB Corp.	QNBC	OTCQB	915,875	88.1	1,272	10.2	106.6	4.2	13.5	38.0	103.5	7.8
Citizens Financial Services, Inc.	CZFS	OTCQB	914,169	163.5	490	12.3	185.6	2.8	21.1	71.1	190.6	1.8
First Keystone Corporation	FKYS	OTCQB	892,763	133.9	681	14.9	160.1	4.3	(3.3)	42.3	101.1	2.2
1st Summit Bancorp of Johnstown, Inc.	FSMK	OTCQB	886,703	90.1	2	9.6	127.2	-	12.0	13.2	40.1	NA
Somerset Trust Holding Company	SOME	OTCQB	873,645	85.8	261	9.0	110.9	3.0	5.8	79.1	155.7	3.1
ENB Financial Corp	ENBP	OTCQB	850,462	86.7	485	11.6	96.8	3.6	7.8	47.6	57.7	0.3
TF Financial Corporation	THRD	NASDAQ	839,566	133.0	7,290	23.4	142.2	1.1	56.4	106.1	169.1	34.9
FNB Bancorp, Inc.	FBIP	OTCQB	831,303	130.6	18	23.2	165.4	2.1	21.3	54.7	59.9	0.0
Integrity Bancshares, Inc.	ITBC	OTCQB	812,000	77.7	NA	9.5	143.0	NA	NA	NA	NA	NA
Harleysville Savings Financial Corporation	HARL	OTCQX	795,548	64.2	1,480	13.4	101.7	5.0	(4.0)	38.4	63.1	2.1
Mid Penn Bancorp, Inc.	MPB	NASDAQ	736,480	55.2	2,189	9.6	107.2	2.5	36.2	94.7	12.6	3.1
Royal Bancshares of Pennsylvania, Inc.	RBPAA	NASDAQ	727,212	49.4	21,956	7.3	88.5	-	19.1	64.7	7.7	17.5
Norwood Financial Corp.	NWFL	NASDAQ	716,862	105.1	2,342	12.6	122.2	4.2	3.8	47.1	23.5	12.3
Embassy Bancorp, Inc.	EMYB	OTCQB	701,468	64.3	2,451	10.6	111.9	0.7	31.2	139.1	NA	0.7
DNB Financial Corporation	DNBF	NASDAQ	685,162	60.3	1,472	17.6	123.9	1.3	20.5	122.9	237.2	22.4
Fidelity D & D Bancorp, Inc.	FDBC	OTCQB	650,306	72.6	461	9.8	103.8	3.3	24.7	84.8	102.1	0.4
Kish Bancorp, Inc.	KISB	OTCQB	645,622	47.2	290	10.2	106.0	4.3	15.0	47.6	51.2	0.6
CCFNB Bancorp, Inc.	CCFN	OTCQB	621,581	82.5	503	12.1	119.1	3.6	6.3	21.2	107.0	0.3
Dimeco, Inc.	DIMC	OTCQB	608,459	65.0	423	10.9	100.6	3.8	(3.1)	30.8	21.8	1.8
Honat Bancorp, Inc.	HONT	OTCQB	586,318	102.2	122	13.9	127.9	1.6	(17.4)	40.9	35.8	NA
Emclair Financial Corp.	EMCF	NASDAQ	583,702	45.0	729	12.9	118.6	3.5	7.3	70.9	72.2	1.2
Malvern Bancorp, Inc.	MLVF	NASDAQ	578,088	71.6	7,154	NM	93.3	-	(8.1)	57.4	36.9	48.5
CB Financial Services, Inc.	CBFV	OTCQB	550,191	45.0	727	10.6	108.9	4.4	0.4	10.9	62.7	1.0
American Bank Incorporated	AMBK	OTCQB	519,495	52.0	324	13.0	128.3	2.6	27.6	63.7	71.8	NA
Prudential Bancorp, Inc. of Pennsylvania	PBIP	NASDAQ	511,945	116.3	26,537	49.8	89.8	1.0	17.2	123.2	14.1	30.0
Group Mean			730,492	84.2	3,290	13.8	123.1	2.5	14.7	66.4	74.9	8.7
Group Median			722,037	80.1	727	11.6	115.2	2.8	13.5	57.4	61.3	1.9

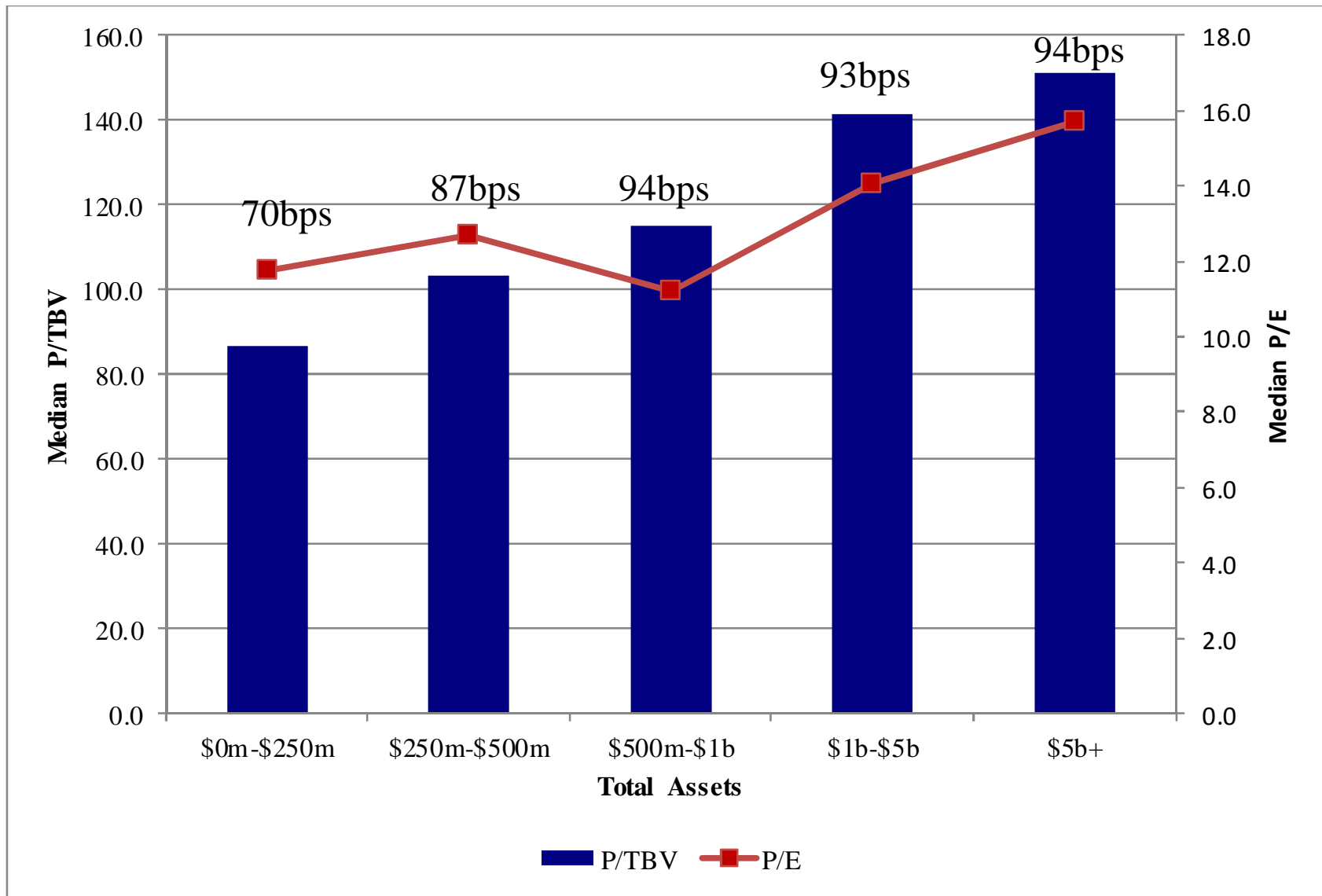
PA Stock Performance – Assets \$250 M - \$500 M

Institution Name	Ticker	Exchange	Total Assets (\$000) MRQ	Market Cap. (\$M)	Avg. Daily Volume One Year	Price/ LTM EPS (x)	Price/ TBV (%)	Dividend Yield (%)	Total Return (%) One Year	Total Return (%) Three Year	Total Return (%) Five Year	Institutional Ownership (%)
<i>\$250 - \$500 Million in Assets</i>												
Northumberland Bancorp	NUBC	OTCQB	482,987	40.9	32	10.3	91.3	2.3	(6.4)	33.5	90.4	NA
Juniata Valley Financial Corp.	JUVF	OTCQB	478,125	74.4	679	18.3	152.1	5.0	6.0	19.0	33.1	-
Hamlin Bank and Trust Company	HMLN	OTCQB	450,822	93.3	4	NA	128.6	4.2	10.7	42.6	89.9	NA
Jonestown Bank and Trust Co.	JNES	OTCQB	447,615	43.5	77	NA	114.7	3.2	11.1	59.5	39.9	NA
Standard Financial Corp.	STND	OTCQX	438,071	56.5	2,385	17.5	87.1	0.9	1.9	29.8	NA	12.2
CBT Financial Corporation	CBTC	OTCQB	437,860	31.3	176	12.8	132.2	3.8	11.9	32.9	113.3	0.3
Riverview Financial Corporation	RIVE	OTCQB	432,882	33.1	NA	15.7	102.6	4.6	NA	NA	NA	0.8
Alliance Bancorp, Inc. of Pennsylvania	ALLB	NASDAQ	430,576	65.6	8,653	47.5	98.4	1.5	6.4	48.0	63.1	51.1
First Community Financial Corporation	FMFP	OTCQB	426,672	56.5	12	15.1	159.0	2.4	28.6	43.2	124.2	-
Allegheny Valley Bancorp, Inc.	AVLY	OTCQB	413,000	41.5	245	13.8	112.2	4.5	2.4	29.8	46.2	-
Commercial National Financial Corporation	CNAF	OTCQB	396,831	60.1	718	9.7	110.6	5.0	5.1	32.6	73.7	1.4
Muncy Bank Financial, Inc.	MYBF	OTCQB	365,215	60.4	429	13.0	158.9	2.3	2.8	93.0	207.4	NA
Mifflinburg Bancorp, Inc.	MIFF	OTCQB	364,585	29.7	2	7.7	77.2	NA	20.0	(31.8)	(31.8)	2.2
New Tripoli Bancorp, Inc.	NTBP	OTCQB	358,209	60.2	-	12.5	140.5	3.5	7.7	35.7	116.5	NA
MNB Corporation	MNBC	OTCQB	354,979	23.2	30	15.3	85.3	3.5	(11.2)	49.1	84.6	NA
West Milton Bancorp, Inc.	WMBC	OTCQB	349,278	50.8	85	10.5	150.6	2.6	28.7	95.4	82.3	NA
Mars National Bank	MNBP	OTCQB	346,100	33.0	2	37.4	96.4	2.9	1.7	5.7	17.0	NA
Woodlands Financial Services Company	WDFN	OTCQB	340,434	32.3	48	11.7	105.3	3.6	(0.7)	61.9	194.1	NA
FedFirst Financial Corporation	FFCO	NASDAQ	323,283	49.9	4,178	26.3	100.2	1.5	16.4	52.7	254.4	36.3
Mauch Chunk Trust Financial Corp.	MCHT	OTCQB	322,917	42.6	10	11.9	126.6	2.9	16.9	39.9	67.3	NA
WVS Financial Corp.	WVFC	NASDAQ	309,940	22.4	1,623	24.1	70.3	1.5	3.8	25.6	(23.0)	17.3
William Penn Bancorp, Inc. (MHC)	WMPN	OTCQB	311,461	65.5	1,456	22.5	109.6	1.4	13.6	49.4	41.1	NA
Neffs Bancorp, Inc.	NEFB	OTCQB	309,126	43.8	14	NA	83.3	2.4	1.1	2.7	13.0	0.1
Polonia Bancorp, Inc.	PBCP	NASDAQ	299,266	34.5	3,091	NM	87.7	NA	6.8	86.8	61.5	36.7
York Traditions Bank	YRKB	Pink	297,393	23.4	7	13.8	88.3	-	-	-	-	-
Community Bankers' Corporation	CTYP	OTCQB	284,332	18.4	86	NA	NA	4.0	1.0	8.1	(5.4)	NA
Peoples Limited	PPLL	OTCQB	280,700	24.5	-	9.4	108.7	3.1	7.2	54.9	8.5	NA
Landmark Bancorp, Inc.	LDKB	OTCQB	277,915	22.7	856	12.7	94.7	2.3	8.4	7.7	31.1	NA
Enterprise Financial Services Group, Inc	EFSG	OTCQB	261,589	7.3	196	NA	54.9	-	73.7	14.6	31.2	NA
Group Mean			365,247	42.8	896	16.9	108.1	2.8	9.8	36.5	67.5	11.3
Group Median			354,979	41.5	86	13.8	104.0	2.9	6.6	34.6	61.5	1.1

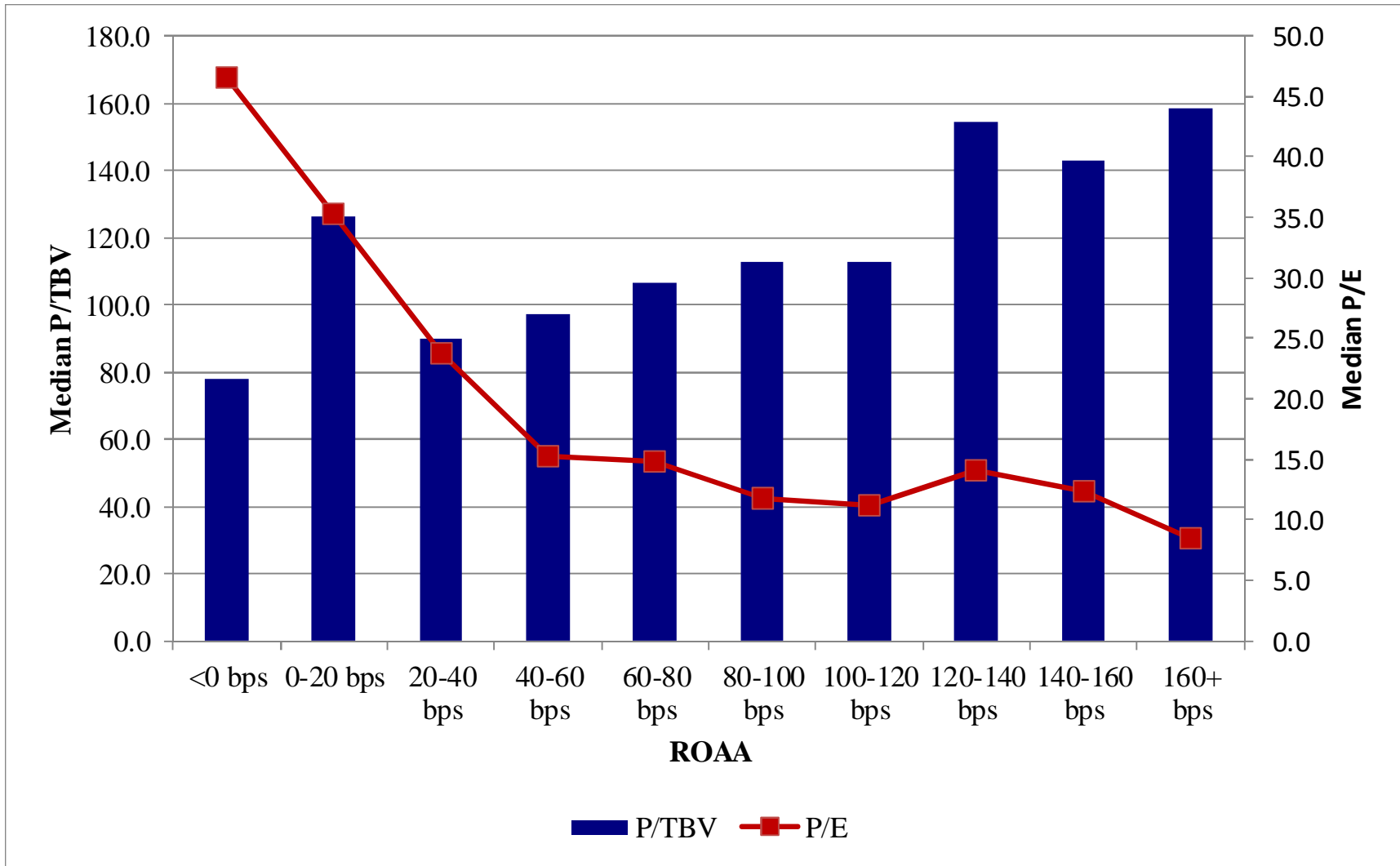
PA Stock Performance – Assets < \$250 M

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<i>< \$250 Million in Assets</i>												
Scottsdale Bank & Trust Company	SDLJ	OTCQB	249,615	22.4	1	NA	49.6	-	6.3	42.3	42.3	NA
Fleetwood Bank Corporation	FLEW	OTCQB	227,007	16.4	25	14.8	81.3	3.3	6.1	(4.8)	(0.1)	NA
JTNB Bancorp, Inc.	JTNB	OTCQB	168,280	11.5	71	13.3	94.7	1.7	5.4	12.7	25.2	NA
First Resource Bank	FRSB	OTCQB	166,265	9.6	791	8.7	78.9	NA	16.5	159.4	132.1	NA
Apollo Bancorp, Inc.	APLO	OTCQB	153,000	20.3	34	14.0	118.9	4.5	2.6	30.2	(64.1)	NA
Eureka Financial Corporation	EKFC	OTCQB	151,872	22.8	237	14.6	99.4	2.2	6.8	60.6	115.9	15.7
Quaint Oak Bancorp, Inc.	QNTQ	OTCQB	140,644	15.7	998	17.2	92.8	1.4	10.3	93.3	118.4	9.5
Turbotville National Bancorp, Inc.	TVNB	OTCQB	128,246	15.8	-	9.9	84.2	0.9	3.1	20.7	162.2	NA
UNB Corporation	UNPA	OTCQB	123,638	7.7	11	9.1	59.4	1.5	6.8	33.3	77.6	NA
Clarion County Community Bank	CCYY	OTCQB	121,022	8.9	419	10.3	67.4	1.1	(10.0)	6.6	(15.4)	-
Community First Bancorp, Inc.	CMFP	OTCQB	98,516	4.4	18	12.5	42.9	3.8	(12.1)	(3.3)	3.9	NA
FNBPA Bancorp, Inc.	FNBP	OTCQB	95,125	9.3	36	9.7	92.1	3.4	4.5	19.4	58.0	0.1
United-American Savings Bank	UASB	OTCQB	87,069	6.2	79	11.8	87.7	1.0	(3.5)	57.6	NA	-
FNBM Financial Corporation	FNMN	OTCQB	81,413	12.5	6	NM	109.4	-	129.3	144.5	135.3	NA
Citizens National Bank of Meyersdale	CZNS	OTCQB	79,637	3.7	35	NM	53.9	-	(52.9)	(51.2)	(49.5)	NA
Manor Bank	MANR	OTCQB	27,151	3.7	-	NM	120.9	-	-	16.1	18.5	NA
Group Mean			134,573	11.94	173	12.1	83.3	1.65	7.45	39.84	50.69	5.06
Group Median			41,729	10.56	35	12.1	86.0	1.40	4.96	25.46	42.26	0.08
Pennsylvania Mean			4,815,314	656.1	83,329.0	15.0	118.5	2.6	11.9	54.8	70.9	23.2
Pennsylvania Median			564,140	62.2	727.0	13.1	112.0	2.8	6.8	48.4	62.7	15.5

Valuation by Asset Size - Pennsylvania



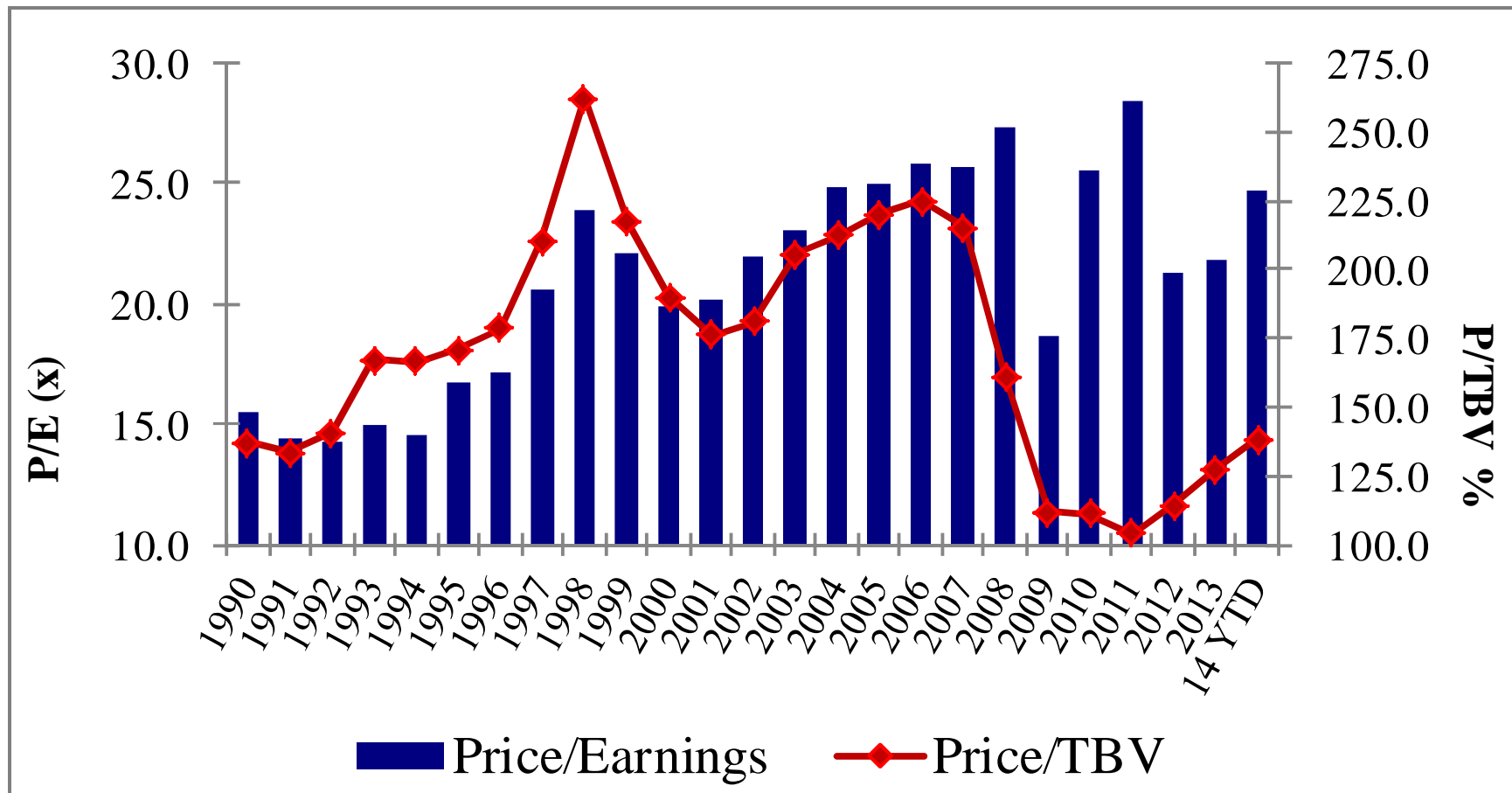
Valuation by ROA Bands - Pennsylvania



Investor Themes – 2014 & Beyond

- ***Institutional investors moving "down the ladder"*** in asset size as opportunities become more scarce in the larger liquid names and the more attractively valued smaller names experience more stability.
- ***Investors are anticipating a very busy year for issuance.*** Subsiding geo-political noise is presenting a more favorable issuance environment in which the window opens longer and wider.
- ***Entry points remain critical.*** As much of the industry's investible dry-powder remains in the Private Equity sector, decision makers continue to rely on estimated IRRs as a crucial benchmark for the approval process.
- ***Funds are reducing minimum check sizes.*** As viable re-capitalization opportunities fade, some funds are taking advantage of potential investments they previously excluded.
- ***Investment decisions continue to migrate*** from P/TBV valuations to more historical P/E multiple valuations.
- ***Growth oriented opportunities garner more support than low valuations investments.*** Avoidance of "bear trap" scenarios becoming a dominate investor theme as many recapitalized issues remain mired with legacy issues and reputational wounds.
- ***Investors awarding strategic buyers*** as acquirers' share prices are more frequently increasing following acquisition announcements (versus declining due to arbitrage effects).
- ***Management remains a core investment component*** as investors tend to bet more on the "jockey" than the "horse." Demographics and geography remain core issues to determining franchise attractiveness.
- ***Adjustments to balance sheets will continue to drive capital issuance*** as new regulatory rules are implemented. TARP dividend rate increases to 9% and SBLF rate increase approaches in 2016. Increasing interest rates driving AOCI to losses; rapidity of move of greater concern than the move itself.

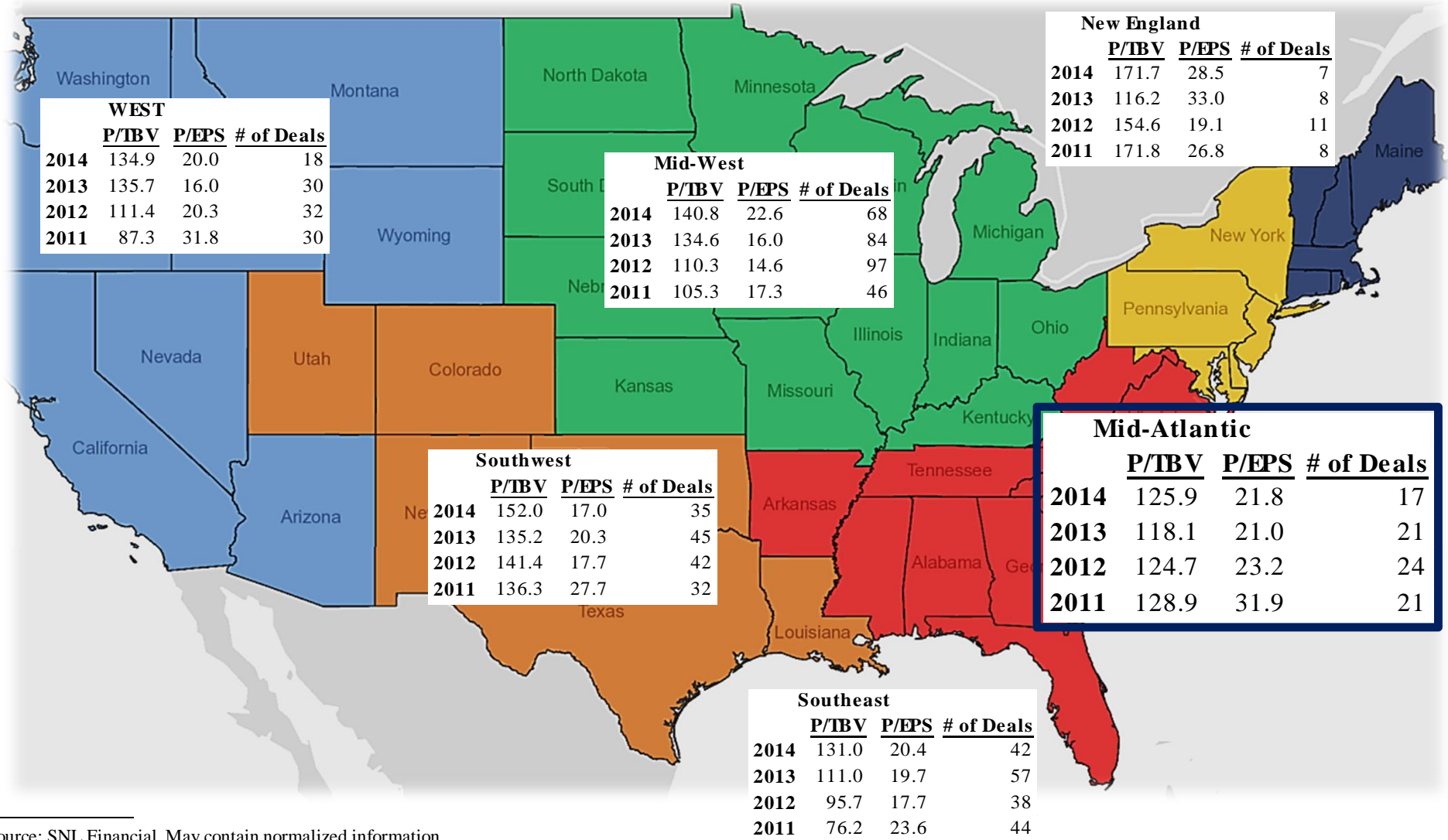
National M&A Median P/E Pricing Multiples Have Rebounded And Are Now In Focus



Source: SNL Financial as of 9/2/2014.

Median financial data for announced whole bank transactions, contains normalized information

Regional M&A Exit Pricing



Source: SNL Financial. May contain normalized information.

Includes announced bank and thrift acquisitions from 1/1/2011-9/2/2014. May include terminated transactions and re-capitalizations involving a change in control

The "Best" Exit Values – The Larger The Bank, The Better The Pricing

Target Assets	2004		2005		2006		2007		2008		2009		2010		2011		2012		2013		2014	
	# Deals	Avg P/TBV (%)	# Deals	Avg P/TBV (%)	# Deals	Avg P/TBV (%)	# Deals	Avg P/TBV (%)	# Deals	Avg P/TBV (%)	# Deals	Avg P/TBV (%)	# Deals	Avg P/TBV (%)	# Deals	Avg P/TBV (%)	# Deals	Avg P/TBV (%)	# Deals	Avg P/TBV (%)	# Deals	Avg P/TBV (%)
\$0-\$250M	176	200.5	199	207.1	199	207.4	197	204.0	112	173.3	84	120.4	124	123.4	100	108.1	151	117.0	143	117.0	115	120.5
\$250-\$500M	24	221.3	28	266.9	34	258.5	27	277.4	9	219.6	9	96.5	18	104.3	18	96.0	27	113.5	33	112.9	30	149.0
\$500M-\$1B	25	242.4	17	285.1	25	310.9	22	259.5	9	147.8	6	113.9	13	120.1	16	106.1	20	114.6	21	130.0	24	164.3
\$1-\$5B	23	287.1	11	286.3	21	353.9	22	269.6	6	201.0	5	102.9	14	85.5	10	134.9	16	143.4	20	162.5	12	150.4
\$5-\$20B	4	278.9	4	312.0	6	357.3	7	351.2	3	114.2	2	114.7	6	111.3	3	229.7	4	146.4	3	172.7	2	110.3
>\$20B	7	370.7	1	279.6	5	390.5	3	332.7	5	85.6	0	0.0	1	97.6	2	99.8	1	84.5	0	0.0	-	0.0
Top 10%	23	404.9	22	387.8	24	437.5	22	414.6	10	310.3	6	207.2	10	226.8	7	194.5	12	215.0	7	185.6	11.0	221.2

- Clearly ... size matters to valuation
- Almost uniformly the best deals involve larger companies
 - Size = efficiency
 - Scale = pricing power
 - Revenue Diversification = earnings consistency

Source: SNL Financial; Industry represents all public banks and thrifts
 P/TBV reflects averages for each year; Excludes Government Assisted Deals

Operating Performance Is Evident to Market and Exit Valuation

- Better performers sell for a better price – the data bear this out

National Exit P/TBV %	2004	2005	2006	2007	2008	2009	2010	2011	2012	2013	2014
<0 bp ROAA	163.5	190.5	194.0	165.6	120.4	102.2	93.5	76.2	86.1	86.1	134.8
0-25 bp ROAA	169.6	165.8	180.9	190.1	141.8	128.5	120.5	114.4	122.0	103.8	107.6
25-40 bp ROAA	165.8	210.1	215.7	196.5	142.7	118.9	118.7	116.4	122.4	115.1	124.5
40-60 bp ROAA	242.3	225.1	216.7	225.9	184.7	145.7	165.3	114.9	128.9	124.9	139.8
60-100 bp ROAA	224.2	214.4	236.8	222.5	177.5	125.9	138.5	131.8	130.0	136.6	144.3
>100 bp ROAA	254.6	256.2	275.1	267.3	221.8	157.5	157.6	146.4	137.5	155.9	161.4

- Not surprisingly, buyers value strong earners

Source: SNL Financial; Industry represents all public banks and thrifts
P/TBV reflects averages for each year; Excludes Government Assisted Deals

Shareholder Value Added

- Capitalization (assuming your capital is “commensurate with the risk profile of the institution”)
- Weighted Average Cost of Capital “WACC”
- Real Cost
- Real Return
- Shareholder Value Added – Are we creating shareholder value?

Strong Earnings Create Shareholder Value

	<u>Example A</u>	<u>Example B</u>	<u>Cost of Capital Assumptions</u>	
Total Assets	400,000,000	400,000,000	Size Premium	4.5%
Capitalization (TCE/TA %)	8%	8%	Equity Risk Premium	5.0%
Capital \$'s	32,000,000	32,000,000	Beta	1
			Risk Free Rate	<u>2.5%</u>
Cost of Capital %	12%	12%	Cost of Capital	12.0%
Cost of Capital \$'s	3,840,000	3,840,000		
Net Income \$'s	3,200,000	4,000,000		
ROA %	0.80%	1.00%		
Corresponding ROE	10.00%	12.50%		
Shareholder Value Added	(640,000)	160,000		
Are we creating value?	NO	YES		

Best Source of Valuation (& Liquidity) is Earnings (An Investors and Regulators Best Friend)

- If you are not given the valuation or liquidity you desire, you have to earn it
- It goes without saying, earnings drive value
- The data shows it, the regulators love it, investors demand it
- Strong earnings allow an institution to dictate its future
- Absent a valuation lift in the public markets, strong earnings create value

Takeaways On Valuation

- We are starting to get back to normal, albeit, a “New Normal”
- Valuation is driven more and more by earnings
 - Not given but earned
- Why is Valuation Important?
 - Investors need it
 - Those that don’t have it need it
 - It’s a differentiator in the New Normal given the lack of growth prospects industrywide
- Size Matters more so than ever
- Performance matters more, particularly for community banks
- Performance can allow you to control your own destiny

Liquidity Issues Community Banks Face



Liquidity & Valuation Challenges Facing Community Banks

- Increased Regulatory Pressures – FRB, FDIC, OCC, Dodd-Frank, Basel III
- Growth – Organic or M&A – what is the best way to stay competitive
- Incompatible public market place options
- Lack of information availability and distribution

Liquidity Planning

- The Board should consider liquidity planning along with its strategic planning
- Shareholders have timely and untimely needs
- Key considerations should include:
 - Time horizon of potential liquidity need
 - One or many shareholders
 - Regulatory matters may get in the way (large share repurchases or other approvals may be needed)
 - The capitalization of the Bank

Benefits of Liquidity

- Draws interest in the company and enhances ability to access the capital markets
- Provides an exit for shareholders when they want it or need it
- Provides “real” pricing support for your stock
- Supports employee benefits and relations
 - Attractiveness of benefit plans
 - Enhances ability to attract and retain top talent

Consequences of Illiquidity

- Investor relations issue
- Inability to access capital markets as freely or timely as necessary when you want it
- Limiting of potential investor pools (investment policy req.)
- Possible capital pressure
- A need to alter the strategic plan
- Or even a forced sale of the bank (if a sale is the only liquidity option)

Liquidity Challenges of Mutuality

- Limited access to capital
 - Constrains growth and the maintenance of a capital cushion
 - Poorly positioned to raise capital quickly if the need arises
- Mutuals can create capital only four ways
 - Internal generation through retained earnings
 - Subordinated Debt
 - Mutual to mutual merger
 - Conversion
- Internal generation of capital may be insufficient to support routine organic growth
 - and is almost always insufficient to support transformational growth

A Mutual's Access to Capital

- Little or no ability to grow through acquisitions
 - Transactions between mutuals rarely occur unless one mutual is distressed
- No ability to participate in equity appreciation of company
 - Attraction and retention of talent can be a challenge
- Mutual culture can sometimes be an impediment to achieving excellence
 - Less entrepreneurial and profit driven
 - Can be prone to complacency

Sources of Shareholder Liquidity

- Go Public – Exchanges (NASDAQ, NYSE)
- Participate in Markets (Pink Sheets, OTC Markets – QB or QX)
- Upstream between markets or to an exchange
- Stay Private – manage yourself
 - Buyback stock – only if excess capital or earnings, and shares below intrinsic value
 - Matching of shareholders - keeping a list of prospective buyers and sellers
 - Need to avoid being viewed as an offering or acting as a broker/dealer
 - Bank cannot be involved
- Sale of the Bank or Holding company - for a more liquid currency or for cash

Public Market Places

Stock Exchanges

- NYSE – must be an SEC Registrant
- NASDAQ – must be an SEC Registrant

OTC Markets (not an exchange)

- OTCQX Banks – *Very New* – limited but conforming listing requirements, moderate fees
- OTCQB – no fees, no additional reporting
- OTC Pink – no listing requirements, no fees
- OTC Bulletin Board – no listing requirements, no fees

The CEO's Desk – *not public and not recommended*

Why Register With SEC?

Pros

- Need SEC registration to list on an exchange and listing to qualify for inclusion in an Index
- Facilitates access to public capital markets – greater transparency and brand awareness of being an SEC registrant
- Many institutional investors can't invest in a non-registrant company

Cons

- Increased accounting and legal fees
- Increase in D&O insurance premiums
- Increased legal exposure to board and management
- Aggravation factor
- Heightened reputation risk

Why List on NASDAQ?

Pros

- Increased liquidity
- Access to public markets: S-3 eligible
- Brand and business recognition
- Accessibility to a broader population of investors (funds, pensions, and other institutional investors)
- Potential for favorable stock pricing if trading volume increases and liquidity discount is eliminated
- Competitive and strategic advantage over banks without a potential for liquid currency
- Exchange listing is needed to qualify for inclusion in Russell

Cons

- Listing fees
- Increased investor accountability
- Risk of non-compliance and delisting
- Stock price more sensitive to market forces
- Risk of new investors with a vision contrary to existing ownership

Russell U.S. Indexes - Construction & Methodology

- Index construction summary
 - Russell produces a family of market cap-weighted U.S. equity indexes. All U.S. indexes are subsets of the Russell 3000E™ Index, which represents approximately 99% of the U.S. equity market
- Purpose
 - Act as a performance standard for active managers, and serve as a proxy for asset allocation purposes
 - Become a purchasable and replicable vehicle for passive investment strategy
- Determining index membership
 - Rank the U.S. common stocks from largest to smallest market capitalization at each annual reconstitution period (May 31)
 - Top 3,000 stocks become the Russell 3000® Index, which measures the performance of the largest 3,000 U.S. companies representing approximately 98% of the investable U.S. equity market
 - Largest 1,000 stocks become the Russell 1000® Index. The Russell 1000 represents approximately 92% of the Russell 3000
 - Next 2,000 stocks become the Russell 2000® Index
 - The smallest 1,000 in the Russell 2000 Index plus the next smallest 1,000 comprise the Russell Microcap Index
- Exclusions
 - Stocks trading below \$1.00
 - Pink sheet and bulletin board stocks

Source: www.Russell.com

OTCQX Banks Market

- Currently, there are approximately 650 community banks that trade on the OTCQB market, which also includes shell companies, bankrupt companies and penny stocks
- OTC Markets Group is launching a new platform exclusively for regional and community banks with the goal of improving the flow of information to investors and increasing visibility for these issuers
- With many banks deregistering due to the JOBS Act, OTC wanted to create an opportunity for these companies to continue to trade and have access to the public markets
- Some of the eligibility requirements include a minimum of \$100 million in total assets, a share price above \$5 per share and at least 50 beneficial shareholders (owning 100+ shares)*
 - Other banking-specific factors will be considered, such as enforcement actions and capital ratios
- ***Included banks will be subject to disclosure requirements with the OTC, including annual audited financial statements, quarterly financials and possibly quarterly earnings releases****
 - Relationships with data providers, including EDGAR, Bloomberg, and Capital IQ
- All OTCQX-listed banks will need a registered transfer agent
- Each bank must have an OTC-registered Corporate Broker (must meet certain requirements)
- Launched in 2Q'14

*This information has not been finalized by OTC Market Group and is subject to change.

Costs & Benefits of Forming a Bank Holding Company

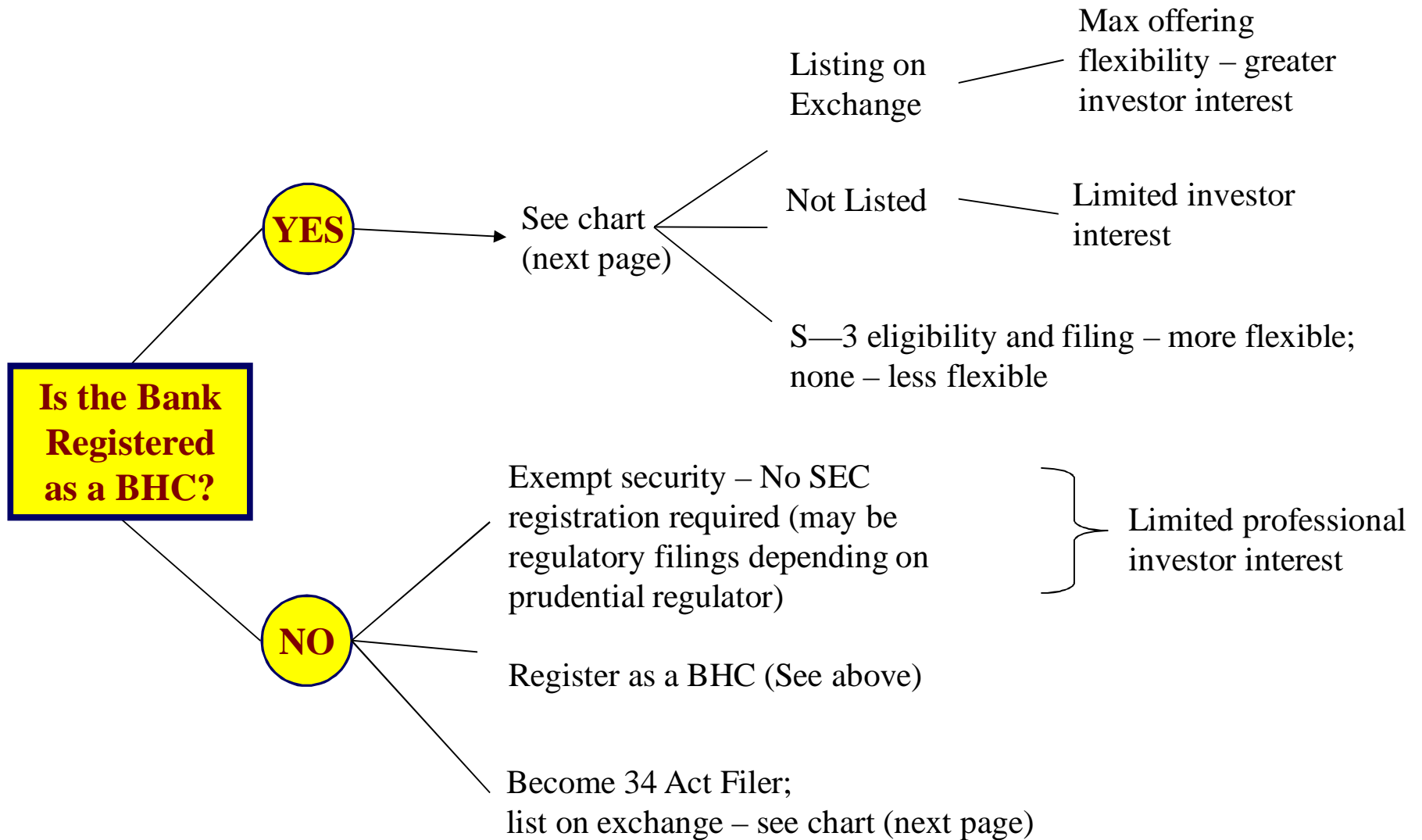
Costs

- Effort to complete the initial application to the Federal Reserve
 - Usually approved within 60 days
- Future applications required in the event of proposed acquisitions or new lines of business besides banking
- Ongoing reporting requirements to and supervision by the Federal Reserve
 - Becoming a “state member bank” can consolidate the federal regulatory relationships to be with the Fed at both holding company and bank levels
- Potential for required registration with the SEC and associated reporting costs
 - Lessened by the JOBS Act

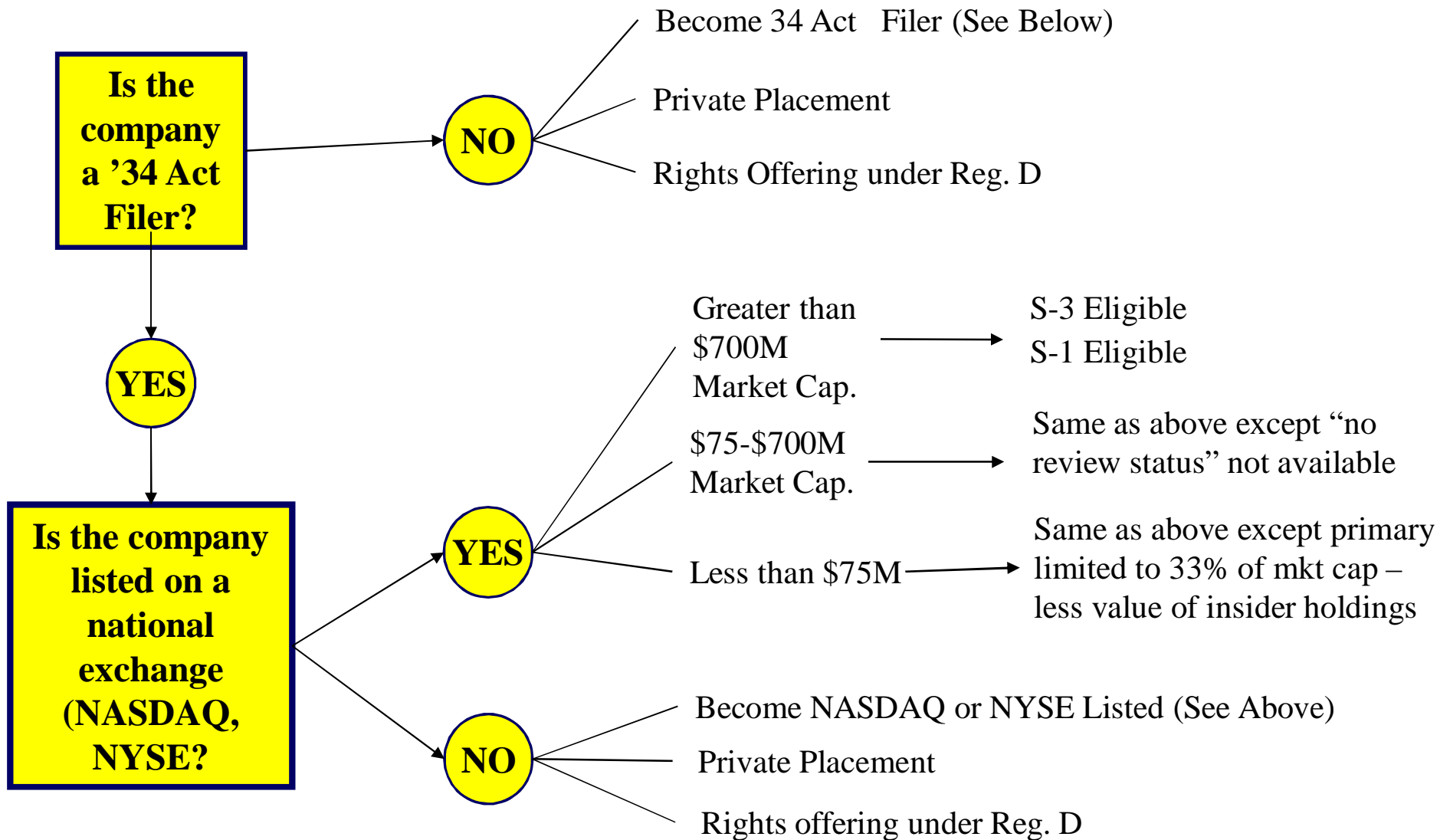
Benefits

- Significantly expanded capital planning and leverage opportunities
 - Expanded access to debt and capital
 - Reporting is not just a cost; it provides investors with transparency, which encourages investment
- Significantly expanded business flexibility
 - BHCs can merge one bank into an existing subsidiary bank
 - BHCs can operate with multiple banking subsidiaries
 - BHCs can acquire nonbanking companies
- Additional investment flexibility
 - Ability to invest in non-bank eligible investment (like debt or equities of other banks)
 - Ability to participate in non-bank permitted businesses

Flow Chart of Capital Raising Alternatives: Bank Only



Flow Chart Of Capital Raising Alternatives For BHC's



ESOPs for Banks



Outline

- The Concept
- Mechanics of an ESOP
- Benefits to the Bank
- Other Considerations
- Banks with ESOPs
- Banks without ESOPs
- Summary

The Concept

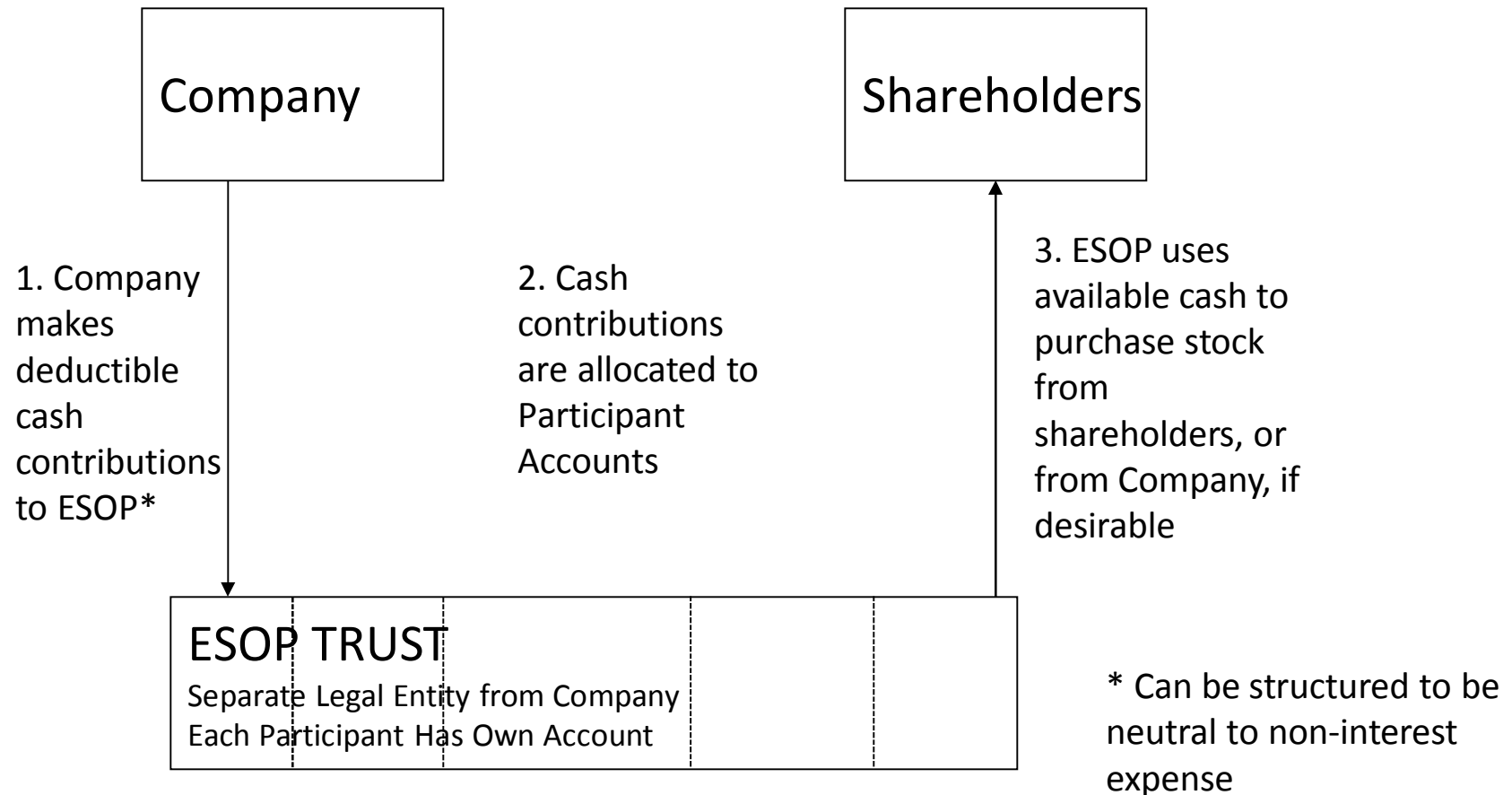
- ESOP = “Employee Stock Ownership Plan”
- ESOP = tax-qualified retirement plan that invests primarily in employer securities
- Tool of Corporate Finance
 - Creates market for shares – mechanism to create shareholder liquidity or buy-side interest in stock
 - Shares end up in “friendly” hands
 - Can be structured so no adverse P&L consequence or hit to capital
 - Bank gets to deduct contribution

The Concept (cont'd)

- Two general types
 - Non-leveraged, deductible employer contributions are made in cash, which is then used to purchase employer stock (can also be made directly in stock)
 - Leveraged, deductible employer contributions are made in cash, which contributions are then used by the ESOP to repay a loan used to purchase employer stock
- In many cases, no impact on earnings since ESOP replaces bank's contribution to 401(k) or profit sharing plan

Mechanics of an ESOP

- Non-Leveraged ESOP

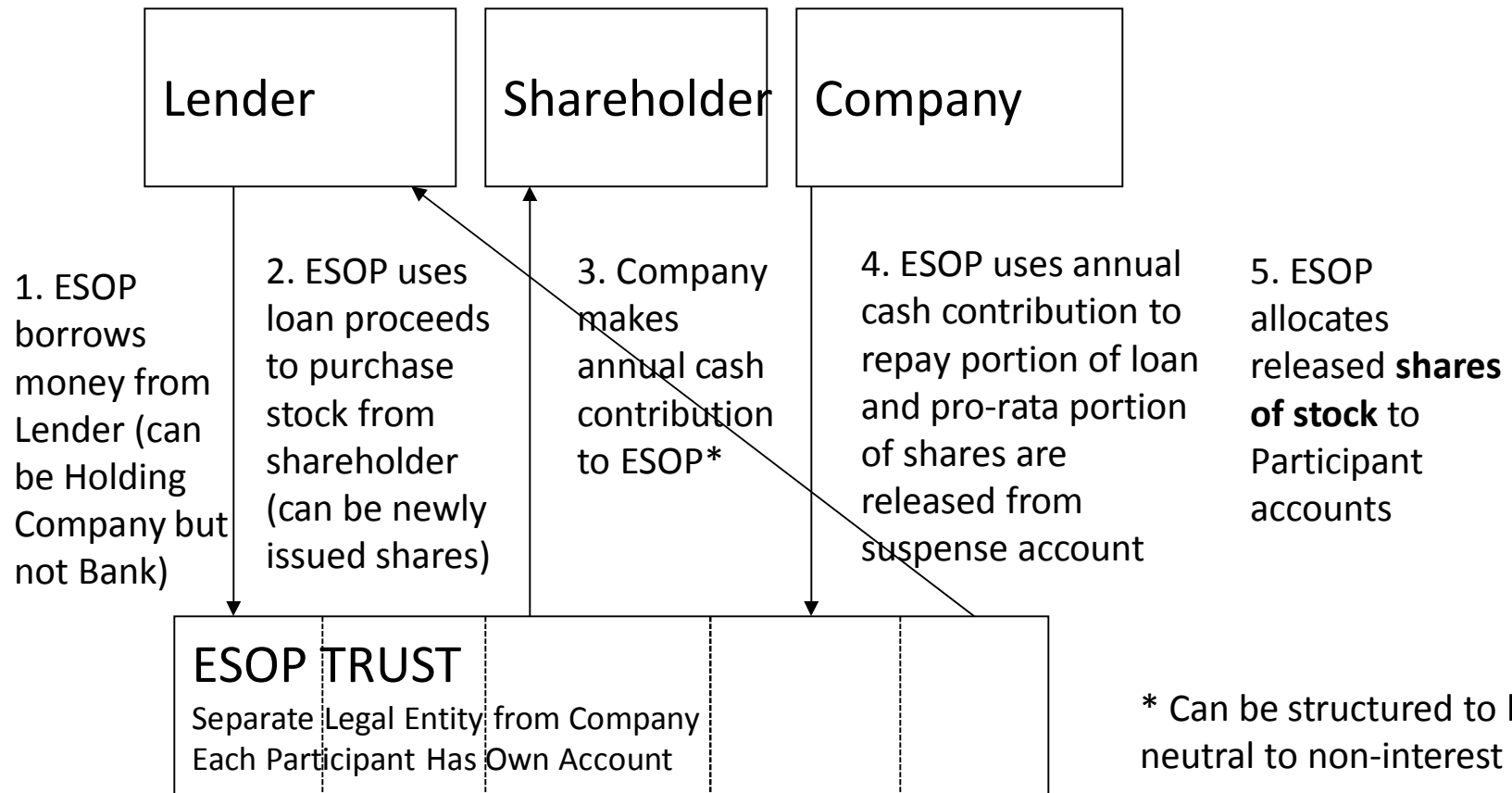


Mechanics of an ESOP (cont'd)

- Non-Leveraged ESOP
 - Bank makes deductible cash contribution to ESOP (could be made in stock)
 - No incremental cost to bank – replaces bank's contribution to 401(k) or profit sharing plan
 - ESOP uses cash to buy shares thereby creating a market for shares
 - Contribution is typically allocated proportionately based on eligible compensation

Mechanics of an ESOP (cont'd)

- Leveraged ESOP



Mechanics of an ESOP (cont'd)

- Leveraged ESOP

- Holding Company loans directly to ESOP or guarantees loan from a third party (bank cannot)
- ESOP uses loan proceeds to purchase large block of shares
- Purchased shares are held in "Suspense Account" as collateral for ESOP loan
- With each loan payment, tranche of shares are released from the suspense account and allocated to participant accounts
- Allocation to participants is typically proportional based on eligible compensation

Benefits to the Bank

- Creates market for shares – mechanism to create shareholder liquidity or buy-side interest in stock
- Shares end up in “friendly” hands
- Can be structured so no adverse P&L consequence or hit to capital
- Bank gets to deduct contribution
- Share repurchases are fully tax-deductible
- EPS bump if leveraged

Benefits to the Bank (cont'd)

- A Case Study – Non-Leveraged
 - Current Situation
 - Stock Price - \$8.00/share
 - \$125,000 annual matching contribution
 - 7 million shares outstanding
 - No market for shares
 - Bank forms ESOP and contributes \$125,000 annually instead of 401(k) match
 - ESOP can buy 15,625 shares/year - ~0.22% of outstanding shares each year
 - No incremental cash cost to bank – only shifting benefit from 401(k) to ESOP
 - If appetite to contribute more, can do so

Benefits to the Bank (cont'd)

- A Case Study – Leveraged

- Current Situation

- Stock Price - \$8.00/share
 - \$125,000 annual 401(k) matching contribution
 - 7 million shares outstanding
 - \$5 million in net income - \$0.71 EPS

- Bank forms ESOP and ESOP borrows \$1.75 million with 20 year amortization schedule and 3.93% interest

- ESOP buys 218,750 shares (~3.12% of outstanding shares) and places them in the suspense account – cautionary note – may need to spread purchases over time depending upon trading volume
 - EPS increases to \$0.73 on day 1 because suspense shares are not outstanding for EPS purposes
 - Annual contribution will only be \$125,000 – so no incremental cash cost to bank – only shifting benefit from match to ESOP
 - ~10,930 shares are allocated to participants annually

Other Considerations

- Deduction Limits
 - Aggregate limit: cannot exceed 25% of eligible comp
 - Individual limit: cannot exceed the lesser of (i) \$52,000 (in 2014) or (ii) 100% of a participant's compensation (capped at \$260,000 in 2014)
 - This limit applies to the total of all plans, including 401(k)
- Compensation limit of \$260,000 (in 2014, adjusts for inflation each year)
- Dividends are generally not considered contributions
- Dividends can be deducted in certain cases

Other Considerations (cont'd)

- Accounting is complex, and often counterintuitive
 - Controlled by ACS 718-40 (formerly SOP 93-6)
 - Direct loan made by third-party to ESOP is considered Company liability
 - If leveraged, can be mismatch between comp expense and contribution deduction - comp expense is value of the shares released not amount contributed
 - Shares held in suspense account are not considered outstanding for capital or EPS purposes

Other Considerations (cont'd)

- Unique fiduciary issues
 - The implementation of the ESOP (e.g., the price at which shares are sold and the choice of trustees and service providers) is fiduciary in nature
 - Trustee is generally responsible for decisions, such as voting and determining FMV
 - Internal vs. external trustee
 - External trustee advisable in conflict situations
 - Primary fiduciary is responsible for assuring that the ESOP does not pay more than fair market value for employer securities
 - Fiduciaries have an obligation to monitor and/or attempt to influence management if such activity is likely to enhance the value of the ESOP's investment in the company

Other Considerations (cont'd)

- Unique fiduciary issues (cont'd)
 - Potential personal liability
 - Indemnification and fiduciary liability insurance provides fiduciaries with protection
 - Fiduciary liability is not covered under E&O policy- requires separate policy
 - Diversification – Participant right to elect to diversify out of employer stock
 - Not publicly traded – age 55 and 10 years of service
 - Publicly traded – 3 years of service

Other Considerations (cont'd)

- Adequate Consideration
 - Purchase must be for “adequate consideration”
 - Based on a good faith determination of fair market value, which requires written documentation of value
 - If traded on NASDAQ or NYSE, value is determined by most recent trade
 - If not traded on NASDAQ or NYSE, value must be determined by an independent appraiser
- Put – if not NYSE or NASDAQ, participant has right to require holding company to repurchase distributed shares at fair market value (not bank)

Other Considerations (cont'd)

- Voting
 - NYSE or NASDAQ - participants can direct trustee on all matters for which shareholders are permitted to vote
 - If not NYSE or NASDAQ, trustee votes shares in its discretion unless it involves merger, consolidation, recap, etc.

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