Comparative Performance Analysis

Mutuals vs. Other Financial Institutions (1)

Financial Date: 12/31/2012 or Latest Available

#	Asset Size Class ($)	A	B	C	D	E	F	G	H	I	J	K	L	M	N	O	P	Q	R	
		Mutuals (2)			All Non-Mutuals (3)			MHCs			Stock Thrifts			Credit Unions			Commercial Banks			
		< 250m	250m < 750m	750m < 5b	< 250m	250m < 750m	750m < 5b	< 250m	250m < 750m	750m < 5b	< 250m	250m < 750m	750m < 5b	< 250m	250m < 750m	750m < 5b	< 250m	250m < 750m	750m < 5b	
	Number and Age	Number and Age																		
1	Number of Institutions	265	144	61	4,207	1,513	652	23	11	8	114	68	51	Data Not Available			2,306	710	276	
2	Average Charter Age (Years)	108	124	142	86	78	67	112	123	92	88	91	96				98	95	84	
	Bal Sheet/Capital (%)	Bal Sheet/Capital (%)																		Neutral Range:
3	Asset Growth Rate (LTM)	0.5	2.1	2.9	4.2	4.5	5.3	3.7	(1.8)	9.0	5.5	0.8	1.4	Data Not Available			4.9	4.5	5.2	+/- 1.00%
4	Liquidity Ratio (6)	34.4	24.5	22.5	31.8	24.4	21.2	22.5	18.7	35.2	23.8	26.4	18.3				31.9	22.6	18.4	+/- 5.00%
5	Loans/Deposits	76.5	83.2	86.4	68.5	75.2	78.2	85.8	83.6	67.2	84.2	82.6	89.1				68.8	76.0	79.1	+/- 5.00%
6	Tier 1 Leverage Ratio (4)	11.3	10.8	11.1	10.0	9.6	9.5	10.2	9.9	10.8	9.9	10.7	9.6				9.9	9.5	9.0	+/- 1.00%
7	Tier 1 RBC Ratio/RWA	22.4	17.8	16.7	15.9	14.2	13.5	19.1	16.8	19.2	16.3	18.0	14.4				15.4	13.4	12.6	+/- 1.00%
	Asset Quality (%)	Asset Quality (%)																		Neutral Range:
8	NPAs/Assets (Excluding TDRs)	1.6	1.6	1.4	1.3	2.0	1.9	2.4	2.9	2.2	1.9	2.3	1.8	Data Not Available			1.1	1.9	1.7	+/- 1.00%
9	ALLL/Loans	1.0	1.1	1.0	1.6	1.6	1.7	1.1	1.2	1.6	1.3	1.3	1.5				1.5	1.6	1.6	+/- 0.25%
10	Texas Ratio	13.3	14.4	13.4	12.3	18.6	18.7	27.3	25.5	22.2	18.2	18.8	18.7				10.6	17.7	17.7	+/- 5.00%
11	NCOs/Avg Loans (LTM)	0.0	0.2	0.1	0.1	0.3	0.4	0.2	0.2	0.3	0.2	0.4	0.3				0.1	0.3	0.4	+/- 0.25%
	Profitability (%)	Profitability (%)																		Neutral Range:
12	ROAA (LTM)	0.3	0.5	0.6	0.8	0.9	0.9	0.4	0.5	0.4	0.5	0.6	0.6	Data Not Available			0.9	0.9	1.0	+/- 0.10%
13	ROAE (LTM)	2.7	4.4	5.1	7.2	8.4	8.9	3.5	4.9	3.4	3.8	5.1	6.1				7.8	8.9	9.6	+/- 0.50%
14	Net Interest Margin (LTM)	3.2	3.2	3.1	3.8	3.7	3.7	3.4	3.3	3.0	3.6	3.3	3.3				3.7	3.6	3.6	+/- 0.20%
15	Non-Interest Income/AA (LTM)	0.3	0.6	0.6	0.5	0.7	0.9	0.3	0.5	0.4	0.5	0.7	0.8				0.5	0.7	1.0	+/- 0.10%
16	Non-Interest Expense/ AA (LTM)	2.8	2.8	2.8	3.0	2.9	3.0	2.9	2.5	2.5	3.4	2.9	2.8				2.8	2.8	2.9	+/- 0.30%
17	Efficiency Ratio (LTM)	81.5	76.3	74.8	73.2	67.4	66.1	76.2	74.2	77.5	79.1	76.2	73.3				70.7	64.8	64.7	+/- 5.00%
18	Assets/Emp ($)	4,567	4,841	5,807	3,948	4,315	4,698	4,968	4,495	5,873	3,823	4,266	5,727				4,104	4,390	4,585	+/- 500
	Loan & Deposit Mix (%) (5)	Loan & Deposit Mix (%)																		
19	1-4 Fam/Loans	80.5	63.8	60.6	26.3	25.2	23.9	76.3	70.7	49.8	60.3	53.0	43.7				26.1	25.0	23.5	
20	Non-Owner Occ CRE/Loans	2.4	8.5	11.3	8.1	14.3	17.2	3.7	6.0	14.3	5.2	12.6	16.9				6.4	12.5	16.9	
21	Const & Land Dev Lns/Loans	1.3	2.4	4.2	3.0	5.6	5.8	1.1	3.3	2.5	2.5	2.8	3.7				1.9	4.2	4.5	
22	Consumer Loans/Loans	1.2	0.5	0.6	4.7	2.4	1.9	1.0	0.5	0.4	1.7	1.2	0.4				4.5	2.2	2.1	
23	Retail Time Deps/Deposits	48.6	36.0	32.2	33.2	29.6	23.9	46.2	37.2	33.2	42.2	36.6	29.9				33.6	29.4	24.2	
24	Non-CD Deps/Deposits	52.9	41.7	37.8	38.1	34.8	29.3	52.6	41.5	38.1	48.9	40.4	34.6				37.7	33.9	28.4	
	Failures (Since 1998)	Failures (Since 1998)																		
25	Tot. Est. Cost to FDIC ($Mil.)	197	216	-	8,335	15,789	27,474	34	97	-	666	2,225	4,795				7,634	13,467	22,679	
26	Number of Failed Institutions	14	3	-	273	128	78	2	1	-	22	14	14				249	113	64	
27	Cost to FDIC per Inst. ($Mil.)	14	72	-	31	123	352	17	97	-	30	159	342				31	119	354	

Notes

(1) Only Mutuals, MHCs, Stock Thrifts, Credit Unions, and Commercial Banks in the Mid-Atlantic, New England, or Midwest regions are considered for comparability purposes. Does not apply to "All Non-Mutuals".
(2) Includes Mutuals, Co-Ops, and Non-Stock MHCs. Non-Stock MHCs are excluded from the MHC category.
(3) Includes all non-credit union US financial institutions from all regions of US; credit unions excluded due to reporting differences.
(4) For credit unions, the ratio shown here is Equity to Assets.
(5) Only major loan categories are shown. Totals may not add to 100%.
(6) Liquidity ratio = (Cash & Balances Due + Securities + Fed Funds Sold & Repos)/ Total Liabilities

Regional Institutions: by Classification (1)

Mutuals	MHCs	Stock Thrifts	Credit Unions	Comm. Banks	Regional Total
470	42	233	NA	3,292	4,037

Key: Performance Assessment Relative to Mutuals Average

- *Outperforming Mutuals of Similar Asset Size*
- *Comparable to Mutuals of Similar Asset Size*
- *Lagging Mutuals of Similar Asset Size*

Regional Institutions: by Assets (1)

< 250m	250m < 750m	750m < 5b
2,708	933	396

Totals

Regional Total	All US Mutuals	All US Fin. Institutions
4,037	555	13,656

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Advisory | Planning | Valuation

February 14, 2013

Douglas P. Faucette, Esq.
Locke Lord Bissell & Liddell, LLP
701 8th Street, N.W.
Suite 700
Washington, DC 20001

Re: Fair Valuation Services for Mergers of Mutual Thrifts and Credit Unions

Dear Doug:

I am writing to provide you with a copy of our most recent presentation pertaining to our fair valuation services, particularly with regard to mutual mergers. We have a robust valuation practice for banking companies that includes: (1) fair valuation services for merger transactions of stock banking companies, as well as mutual thrifts and credit unions; (2) impairment testing for goodwill and other intangible assets; (3) valuation for initial, and secondary and private offerings; (4) valuation for stock plans of non-public banking; (5) financial advisory services; (6) stress testing for risk management and capital planning; and, (7) a variety of other purposes.

Given the increased cost of regulation, and its pronounced impact on smaller banking companies, we have observed an increased interest in mergers. This has been particularly the case with those mutual thrifts that face management and board succession issues, have weakened financial performance, are located in more rural or highly competitive markets, and perceive limited market interest in their stock which may be offered through a stock conversion.

The valuation for mutual thrift and credit union mergers is complicated by the fact that there are no shareholders and no cash or stock consideration paid. We have developed a specialty in the fair valuation services for mergers of mutual thrifts and credit unions, which have been vetted by the Federal banking agencies as well as by accounting firms. The enclosed presentation sets forth some considerations and methodologies for such valuations.

If you are advising mutual thrifts or credit unions in merger transactions, we can more fully discuss the valuation matters with you so the transaction can be properly accounted for in the initial regulatory application and at the time of the closing of the merger. Please feel free to call if you have any questions.

Sincerely,

Ronald S. Riggins
Ronald S. Riggins
President and Managing Director

Enclosure

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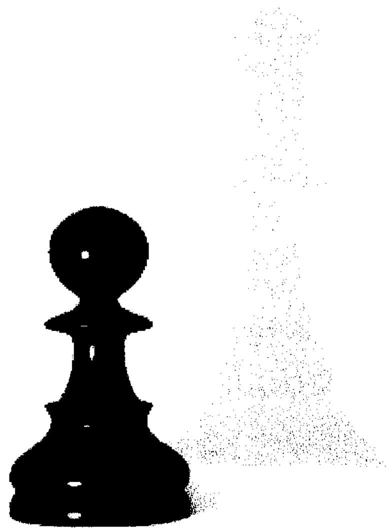
APPRAISAL & ACCOUNTING CONSIDERATIONS IN MUTUAL THRIFT COMBINATIONS



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-

Recent regulatory changes and the external environment has led to an increased number of mergers among mutual thrifts

MUTUAL MERGER OVERVIEW

Mutual Merger Market Overview

Mutual Merger Activity

- Increased merger activity involving mutual thrifts and thrifts in mutual holding company (MHC) form seeking mergers with other mutual thrifts to strengthen their financial condition and increase size to diminish the increased cost of regulation with a larger balance sheet
  - 4 announcements in 2011 with target assets of $0.7 billion
  - 6 announcements in 2012 with target assets of $2.2 billion

Characteristics of Mutual Targets

- Recent mutual thrifts acquisitions have had some or all of the following characteristics –
  - Operating losses or low profitability
  - Elevated non-performing assets
  - Small assets facing reduced profitability to address the increased cost of regulation
  - Concerns on ability to access the capital markets through a conversion transaction, and, if successful, ability to generate attractive shareholder returns

Fair Value Accounting

- Acquirer must be able to absorb the fair value balance sheet of the target mutual thrift

Gradual evolution of merger accounting has eliminated "Pooling of Interests" accounting for mutual-mutual mergers, and all such mergers are now accounted for using the "Acquisition Method"

EVOLUTION OF MERGER ACCOUNTING

Evolution of Merger Accounting for Mutual Mergers: Pooling Gradually Phased Out in Favor to Acquisition Accounting

APB 16 (1970)
Pooling if 12 criteria met, otherwise purchase method

SFAS 141 (2001)
Eliminated pooling method except for mutual-mutual mergers

SFAS 141R (2008)
Eliminated pooling for all business combinations

ASC 805 (2009)
Financial Accounting Standards Board introduced Accounting Standards Codification (ASC) – no substantive change to requirements of SFAS 141R

Accounting for Mutual-Mutual Mergers – Once Pooling … Now the Acquisition Method

Pooling Method

- Combine the balance sheets
- No consolidation adjustments
- Retained earnings of both mutual thrifts before and after merger are the same
- *No longer applicable once SFAS 141R became effective in 2008 (now ASC 805)*

Acquisition Method: ASC 805, Business Combinations

- Determine fair value of:
  - Target mutual thrift
  - Fair value of assets & liabilities
  - Fair value of identifiable intangible assets (e.g., core deposit intangible, mortgage servicing rights, wealth management accounts)
- Determine resulting goodwill
- Target thrift's equity replaced by appraised fair value

Current Acquisition Accounting – Implementation

Step 1
Fair Value of Target

- Determine fair value of target entity
- Consideration (purchase price) = establishes fair value
- **Appraised Value** establishes purchase price in mutual mergers

Step 2
Fair Value of Balance Sheet

- Determine fair value of assets & liabilities
- Determine fair value of identifiable intangible assets
- Determine remaining **Net Assets** resulting from such fair values

Step 3
Determine Goodwill

- Calculate goodwill as follows:
- **Goodwill = Appraised Value – Net Assets**

GOODWILL results if …

- Appraised Value > Fair Value of Net Assets

NEGATIVE GOODWILL results if …

- Appraised Value < Fair Value of Net Assets
- Post-closing recognition of negative goodwill into earnings

Implications for Mergers of Mutual Thrifts

INTRODUCTION TO ASC 805 BUSINESS COMBINATIONS

ASC 805 Business Combinations – Requires Transaction-Related & Post-Transaction Valuations

Transaction Related Valuations – Preliminary and at Closing

- Fair value
  - Including consideration exchanged in stock deals
- Net assets acquired
- Contingent assets & liabilities
  - Contractual – such as mortgage servicing rights
  - Non-contractual – such as lawsuits, with more than 50% probability

Post-Transaction – Typically on an Annual Basis

- Intangible assets impairment valuation (at least annually)
  - Goodwill
  - Core deposit intangible ("CDI")
  - Mortgage servicing rights ("MSRs")
  - Assets under management ("AUM")
  - Employment agreements
  - Non-compete agreements

Identifying & Recognizing Intangibles For Mutual Mergers –
Accounting for Acquisition, Merger Consideration & Transaction Fees

Item	Previously (SFAS 141)	Currently (ASC 805)
ACCOUNTING FOR ACQUISITION	**Cost accumulation approach** **Cost of acquisition is allocated to acquired assets & liabilities based on estimated fair value** **Any excess after allocation is recognized as goodwill**	**Assets acquired, liabilities assumed and non-controlling interests are recognized at fair value** **Goodwill is the excess of total value of the Target over the fair value of identifiable net assets**
MERGER CONSIDERATION	**Marketable equity securities issued by Acquirer are measured at announcement – all other consideration measured at closing**	**Measure at fair value at closing date – if consideration involves public stock, change in market price is built in**
TRANSACTION FEES	**Added to the purchase price**	**Expensed as incurred** ***(Costs related to issuing equity or debt securities to finance the transaction are recognized in accordance with other applicable GAAP rules)***

Identifying & Recognizing Intangibles For Mutual Mergers –
Loss Allowances, Contingency Merger Consideration Payment & Contingent Assets & Liabilities, Bargain Purchase Prices & Restructuring

Item	Previously (SFAS 141)	Currently (ASC 805)
ALLOWANCE FOR LOAN & LEASE LOSSES	Target's ALLL generally carried over to Acquirer	None of Target's ALLL is carried over to Acquirer as each acquired loan is recorded at fair value
CONTINGENT MERGER CONSIDERATION PAYMENT	Not recorded until earned	Recorded at fair value at the acquisition date – any subsequent adjustments must be classified as a liability & recognized through earnings
CONTINGENT ASSETS & LIABILITIES	Generally not recorded unless SFAS 5 threshold is triggered	Contractual contingencies recorded at fair value Non-contractual contingencies recorded at fair value if realization exceeds 50% probability
BARGAIN PURCHASE PRICES	Negative goodwill allocated as a pro rata reduction of certain acquired assets (such as fixed assets), with excess recognized as extraordinary income	Negative goodwill recognized by Acquirer as a gain ("bargain purchase") – not an extraordinary item
RESTRUCTURING ACTIVITIES	Restructuring plans of Acquirer related to Target generally incorporated into the business combination accounting	Acquirer's restructuring plan accounted for separate from the business combination accounting

Illustration Shows Impact of Key Components of ASC 805

HYPOTHETICAL MERGER OF MUTUAL THRIFTS

Hypothetical Merger of Mutual Thrifts Pursuant to ASC 805 – Assets

	Mutual Target								
		Purchase Accounting Adjustments							
	Current Target	Debt		Credit	Fair Value Target	(A) Goodwill	Adjusted Target	Mutual Acquirer	Combined Pro Forma
ASSETS									
Cash & Due	3,000	-		-	3,000		3,000	10,000	13,000
Investments:									
Bonds	20,000	1,000	(1)		21,000		21,000	78,000	99,000
ASC 320 Adjustment - Bonds	1,000		(1)	1,000	-		-	2,000	2,000
Equities	3,500	500	(1)		4,000		4,000	-	4,000
ASC 320 Adjustment - Equities	500		(1)	500	-		-	-	-
Total Investments	25,000	1,500		1,500	25,000		25,000	80,000	105,000
Gross Loans	70,000	1,400	(2)	-	71,400		71,400	250,000	321,400
Allowance for Loan Losses	(600)	600	(3)	-	-		-	(3,000)	(3,000)
Net Loans	69,400	2,000		-	71,400		71,400	247,000	318,400
Fixed Assets	1,500	150	(4)	-	1,650		1,650	6,000	7,650
Core Deposit Intangible (CDI)	-	1,700	(5)	-	1,700		1,700	-	1,700
Other Intangible Assets (MSRs)	-	250	(6)	-	250		250	-	250
Goodwill (Negative Goodwill)	-	-		-	-	980	980	-	980
Other Assets	1,100	(50)	(7)	-	1,050	-	1,050	7,000	8,050
Total Assets	100,000	5,550		1,500	104,050	980	105,030	350,000	455,030

See notes on page 16

Hypothetical Merger of Mutual Thrifts Pursuant to ASC 805 – Liabilities + Equity

	Mutual Target								
		Purchase Accounting Adjustments							
	Current Target	Debt		Credit	Fair Value Target	(A) Goodwill	Adjusted Target	Mutual Acquirer	Combined Pro Forma
LIABILITIES									
Non-Interest Bearing Deposits	10,000	-		-	10,000		10,000	25,000	35,000
Interest-Bearing Deposits:									
Checking & Savings	12,000	-		-	12,000		12,000	50,000	62,000
Certificates of Deposits (CDs)	35,000	-	(8)	700	35,700		35,700	125,000	160,700
Money Market Accounts (MMAs)	28,000	-	(9)	280	28,280		28,280	75,000	103,280
Total Interest-Bearing Deposits	75,000	-		980	75,980		75,980	250,000	325,980
Total Deposits	85,000	-		980	85,980		85,980	275,000	360,980
Borrowings	5,000	-	(10)	250	5,250		5,250	40,000	45,250
Other Liabilities	3,000	-	(11)	300	3,300		3,300	10,000	13,300
Total Liabilities	93,000	-		1,530	94,530		94,530	325,000	419,530
EQUITY									
Retained Earnings	6,100	-		3,420	9,520	980	10,500	23,800	34,300
Acc. Other Comprehensive Income (ASC 320)	900	900	(1)	-	-	-	-	1,200	1,200
Total Equity	7,000	900		3,420	9,520		10,500 (A)	25,000	35,500
Total Liabilities & Equity	100,000	900		4,950	104,050	980	105,030	350,000	455,030

See notes on page 16

Hypothetical Merger of Mutual Thrifts Pursuant to ASC 805 – Footnotes

ASSUMPTIONS - FOOTNOTES

Explanation Key

Documentation of fair value of individual assets & liabilities (required under ASC 805)

(A) Assumed acquisition value multiplier: 1.50 x book value to determine amount of goodwill

Purchase accounting adjustments (excludes acquisition costs expensed under the standard)

(1) Adjustment to previous changes in fair value under ASC 320 out of accumulated other comprehensive income (AOCI)

(2) Adjustment to fair value for acquired loans — Adjustment = 2.00% of acquired loans

(3) ASC 805 eliminates ALLL on acquired loans & requires loans to be recorded at fair value; Acquirer may need to establish additional provisions for such loans

(4) Adjustment to fair value for acquired fixed assets — Adjustment = 10.00% of acquired fixed assets

(5) Adjustment to fair value for core deposits — Adjustment = 2.00% of total deposits

(6) Adjustment to fair value for MSRs — Adjustment = 250

(7) Adjustment to fair value for real estate owned (REO) — Adjustment = (50)

(8) Adjustment to fair value for CDs — Adjustment = 2.00% of CDs

(9) Adjustment to fair value for MMAs — Adjustment = 1.00% of MMAs

(10) Adjustment to fair value for borrowings — Adjustment = 5.00% of borrowings

(11) Adjustment to fair value for SERP: increase of $100 and unrecorded litigation accrual: increase of $200

The valuation approaches used are consistent with the determination of acquisition values for stock banking companies

VALUATION APPROACHES FOR MUTUAL THRIFTS

Standard of Fair Value: ASC 820 *(formerly FAS 157)*

LEVEL 1 INPUTS

- Quoted prices for identical assets or liabilities in active markets
- Very liquid market, listed in the *Wall Street Journal* or online sources
- Highly reliable

LEVEL 2 INPUTS

- Quoted prices for similar assets or liabilities in active markets
- May require adjustment to account for certain factors

LEVEL 3 INPUTS

- Inputs that are unobservable & significant to the fair value measurement
- May require assumptions, thus less reliable

In the absence of Level 1 Inputs – the valuation of mutual thrifts is determined through standard valuation methodologies

Approaches for Determining Merger Values of Mutual Thrifts

Valuation Approach 1
Market Approach:
Comparable Merger Transactions Approach

- Level 2 Inputs
- Value based on merger pricing ratios paid in mergers of similar banks/thrifts
- Key pricing ratios include value relative to earnings, equity, assets & core deposits

Market Approach:
Control Premium Approach

- Level 2 Inputs
- Value based on control premiums paid over value determined hypothetical "trading price"
- Level 2 input – stock price of Target, based on peer group comparison of similar public banking companies
- Level 2 input – control premium paid for similar banks/thrifts

Valuation Approach 3
Discounted Cash Flow (DCF) Approach

- Level 2 & 3 Inputs
- Value based on present value of interim cash flows + terminal value at end of year 5 based on merger pricing for similar banks/thrifts
- Based on many assumptions for 5 year business plan

Most weight given to Market Approach as DCF Approach has many unobservable assumptions

Factors Impacting Merger Pricing for Market Approaches 1 & 2: **Comparable Transactions & Control Premium**

Adjustments in value in the following areas are based on fundamental differences between the Target thrift and the valuation peer groups

Risk Profile + A/L & Equity + ROA / ROE + Size / Growth + Market Area = Total Value Adjust-ments

<u>Variance in Market Pricing</u>

But those that command higher pricing are generally – larger, stronger, more diversified, lower risk, operate in more dynamic market areas