Donnelly Penman & Partners
INVESTMENT BANKING

Michigan Bankers Association

NETWORKING AT ITS BEST

BANKERS EDUCATION SUMMIT AND TRADE SHOW

How To Generate Prudent Loan Growth

April 25, 2013

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Confidential

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Data source utilized throughout presentation – SNL Securities, FDIC

Donnelly Penman & Partners

- Boutique investment banking firm based in Grosse Pointe, Michigan
- Established in 2000
- Specialize in merger advisory, raising capital, and valuation and strategic advisory services
- Industry concentration in the financial institution and automotive industries
- Owned by the employees of the firm

1. Where Have We Been?

Current Macro Issues Facing Community Banks

- Economic headwinds (domestic and global)
- Regulatory pressure – particularly compliance
- Legislative uncertainty (Dodd-Frank still being defined)
- Improving loan delinquencies and credit costs
- **Limited quality loan growth opportunities and aggressive pricing by nationals and regionals**

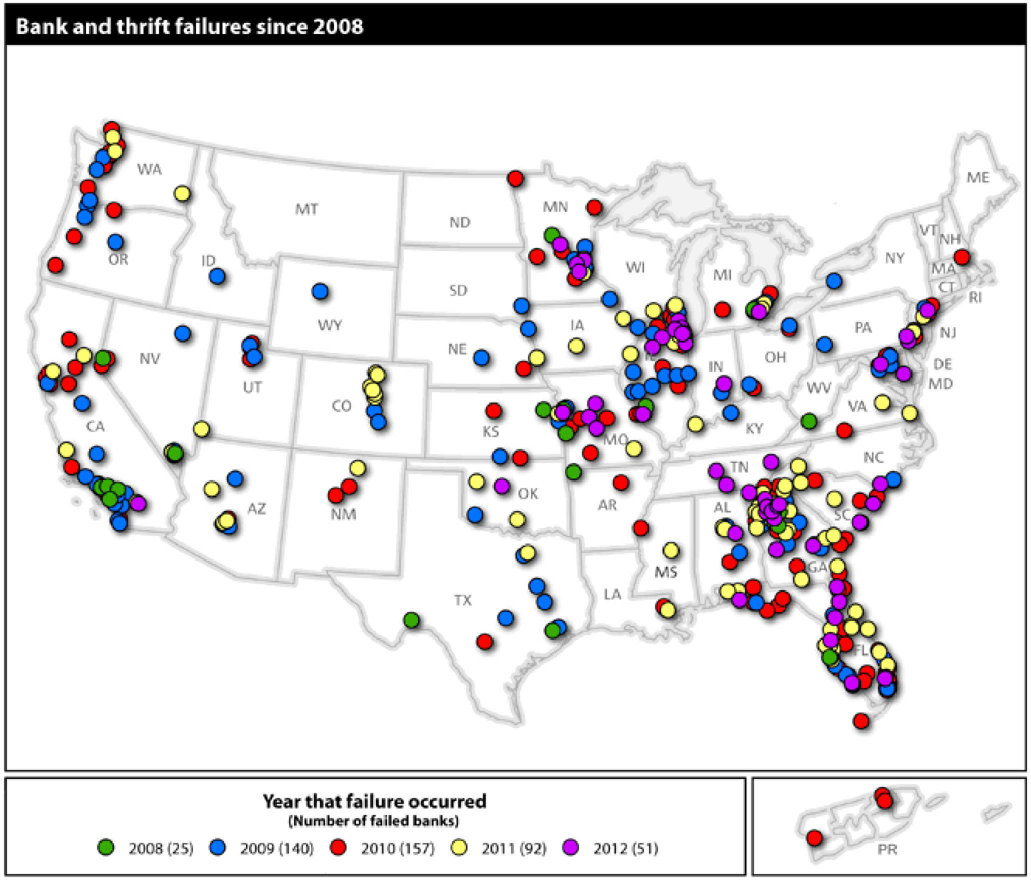
The latter point of loan growth has become a key gating item for community banks as we recover from the Credit Crisis

Backdrop to Current Lending Environment

- Record Low Interest Rates
- Low Loan Demand
- Excess Liquidity/Low Yields
- Fierce Pricing/Fixed Rates/Longer Maturities (10 years)
- Easing of Loan Covenants/Personal Guarantees
- **Limited quality loan growth opportunities and aggressive pricing by nationals and regionals**

Community Banks are at a critical juncture on where to seek prudent loan growth

Bank Failures Across the Nation

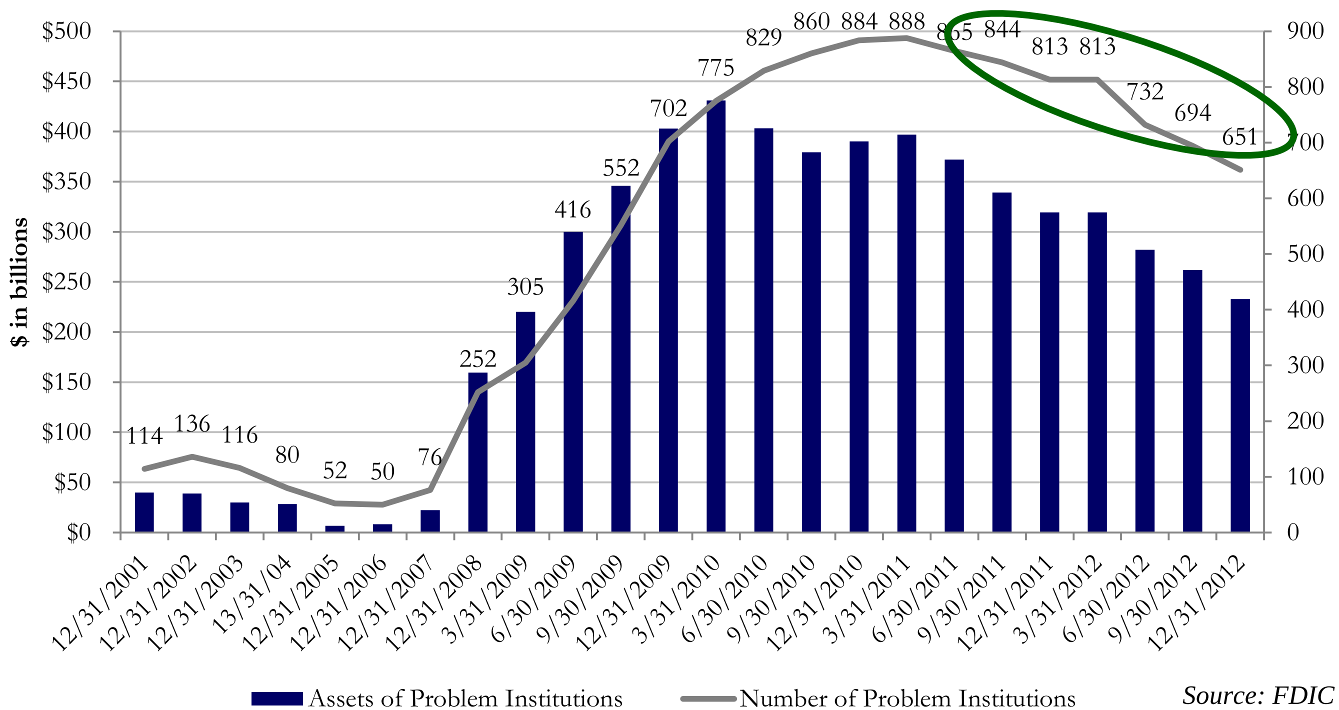


FDIC opportunities can offer buyers great opportunities to create shareholder value

FDIC Problem List Remains High

Despite continued bank failures, the FDIC Problem Institution List has begun to trend downward after not materially changing over the last 2 years, indicating bank failures should subside in 2013, as seen in 2012. However, this list indicates that nearly 10% of the nation's banks are constrained in their lending abilities.

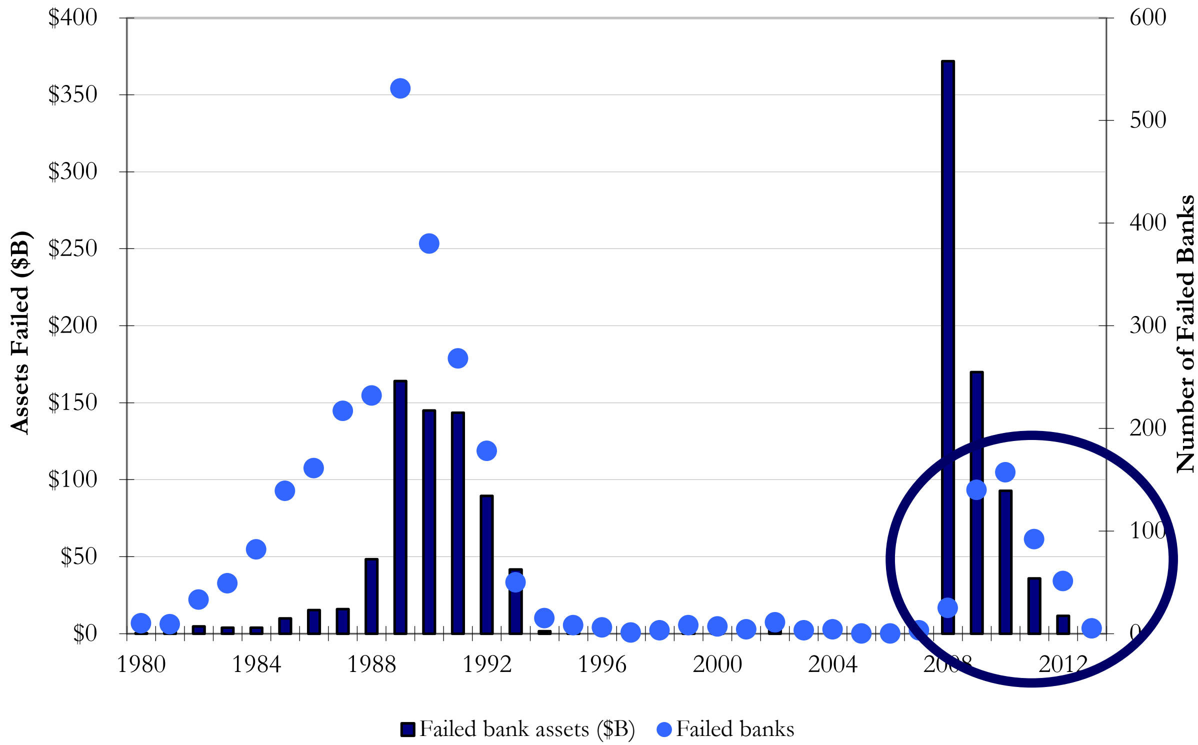
FDIC Problem Institution List



Source: FDIC

Historical Bank Failures

With more than 650 banks currently on the FDIC's Troubled List, we still expect significant number of failures (albeit at a slower pace) – many of which are small community banks



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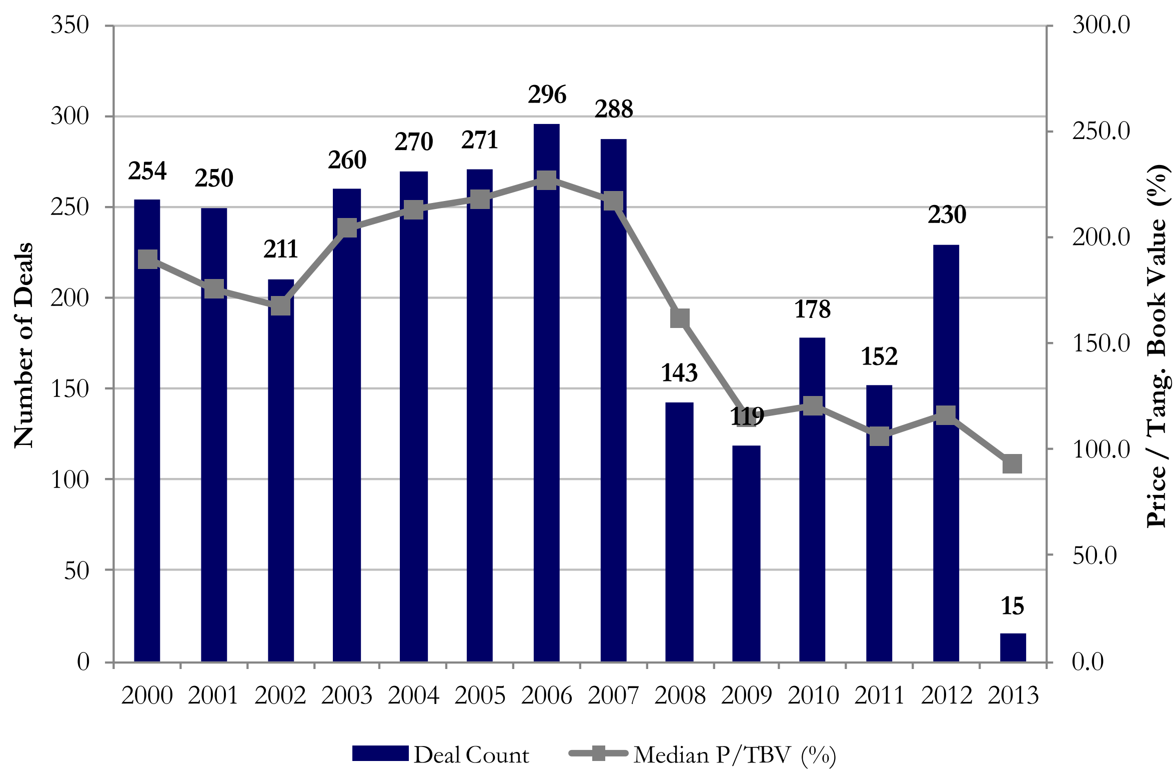
Unassisted Strategic M&A Rebounding

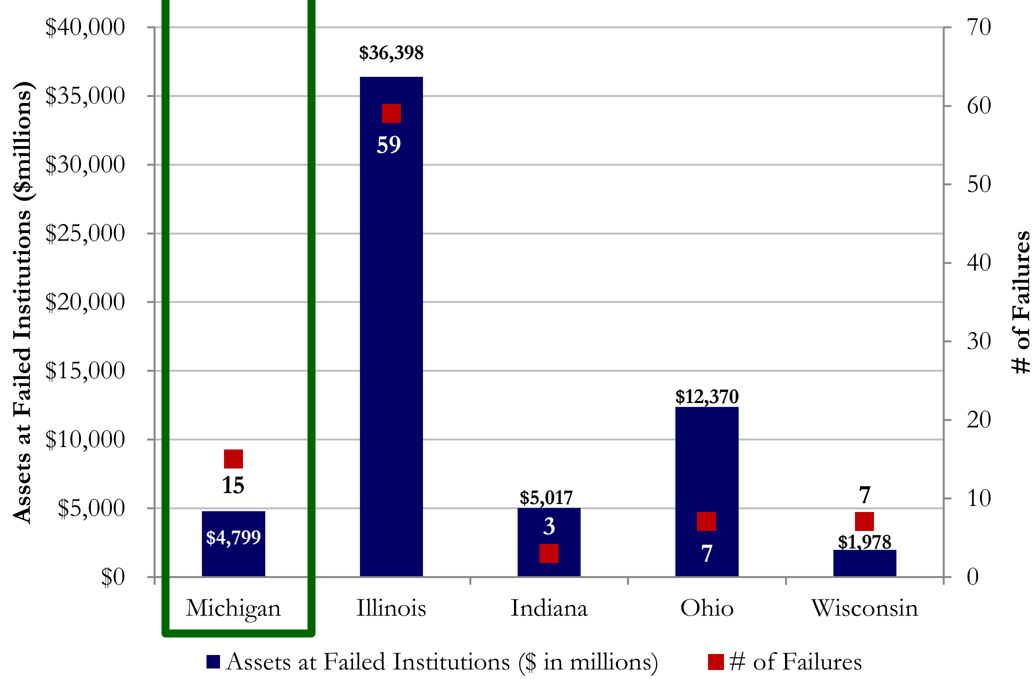
As the economy continues to improve and bank fundamentals and valuations strengthen, the level of failed bank opportunities will continue to decline and the likelihood of normal-course strategic M&A to increase is very high.



Great Lakes Bank Failures in This Cycle

Although Michigan has had the second most bank failures in the Great Lakes since the beginning of this credit cycle (and the highest percentage of bank failures), the last failure occurred in March 2012 and it appears that there may not be any additional failures. It should be noted that most of the bank failures in Michigan have occurred in Metro Detroit.

	Michigan	Illinois	Indiana	Ohio	Wisconsin	Total
# of Failures	15	59	3	7	7	76
Assets at Failed Institutions ($ in millions)	$4,799	$36,398	$5,017	$12,370	$1,978	$55,762



Distressed Banks and Bank Failures in Michigan

Source: SNL Financial, Data as of 12/31/2012

Stressed Banks in Michigan

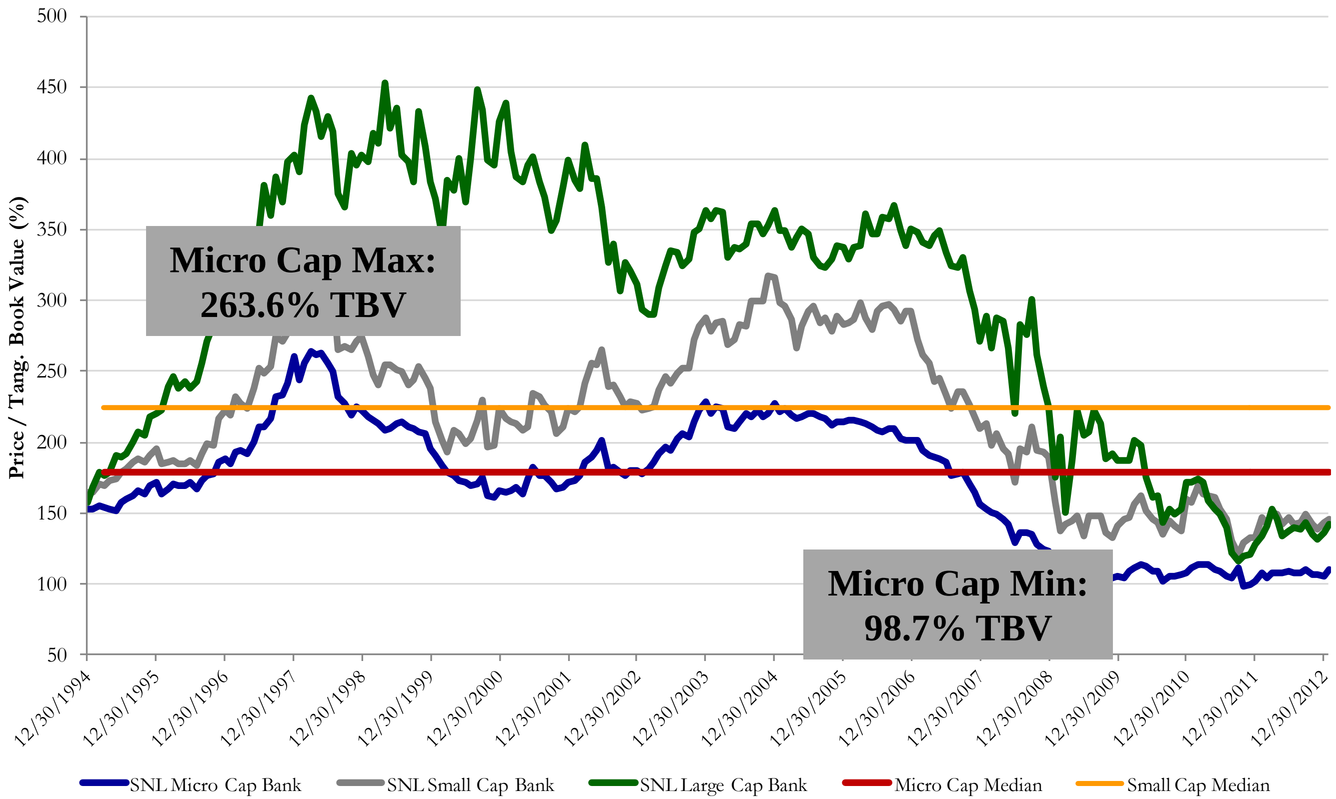
Bank	City	County	Branches	Assets ($000s)	Deposits ($000s)	Tier 1 Leverage Ratio	Nonaccrual + 90PD + OREO / Assets	Texas Ratio (NPAs + 90PD / Tang. Equity + LLR)
Michigan Commerce Bank	Ann Arbor	Washtenaw, MI	10	659,679	636,277	2.61%	18.39%	220.66%
Oxford Bank	Oxford	Oakland, MI	10	259,868	243,627	5.33%	14.64%	211.52%
Monarch Community Bank	Coldwater	Branch, MI	6	190,192	169,592	5.95%	12.06%	156.05%
Northpointe Bank	Grand Rapids	Kent, MI	1	315,751	273,145	7.25%	10.20%	125.47%
First National Bank in Howell	Howell	Livingston, MI	9	296,875	287,812	2.58%	7.65%	117.49%
Capitol National Bank	Lansing	Ingham, MI	2	144,742	133,280	7.28%	10.62%	115.11%
Community Shores Bank	Muskegon	Muskegon, MI	4	204,220	184,202	4.53%	6.99%	112.83%
Flagstar Bank, FSB	Troy	Oakland, MI	111	14,069,057	8,771,046	9.26%	11.48%	96.73%
Union Bank	Lake Odessa	Ionia, MI	7	174,595	155,473	8.60%	8.55%	86.53%
Monroe Bank & Trust	Monroe	Monroe, MI	24	1,267,977	1,049,042	6.38%	6.74%	85.29%
SSBBank	Stockbridge	Ingham, MI	3	62,662	55,948	7.70%	7.50%	80.41%
Independent Bank	Ionia	Ionia, MI	72	2,021,254	1,789,073	8.26%	8.87%	79.10%
Edgewater Bank	Saint Joseph	Berrien, MI	6	124,328	106,942	9.09%	7.89%	74.91%
		Total	265	19,791,200	13,855,459			

A number of banks in Michigan still have heightened credit problems and may not have ample capital to lend as actively as they once would inside the community

Failed Banks in Michigan

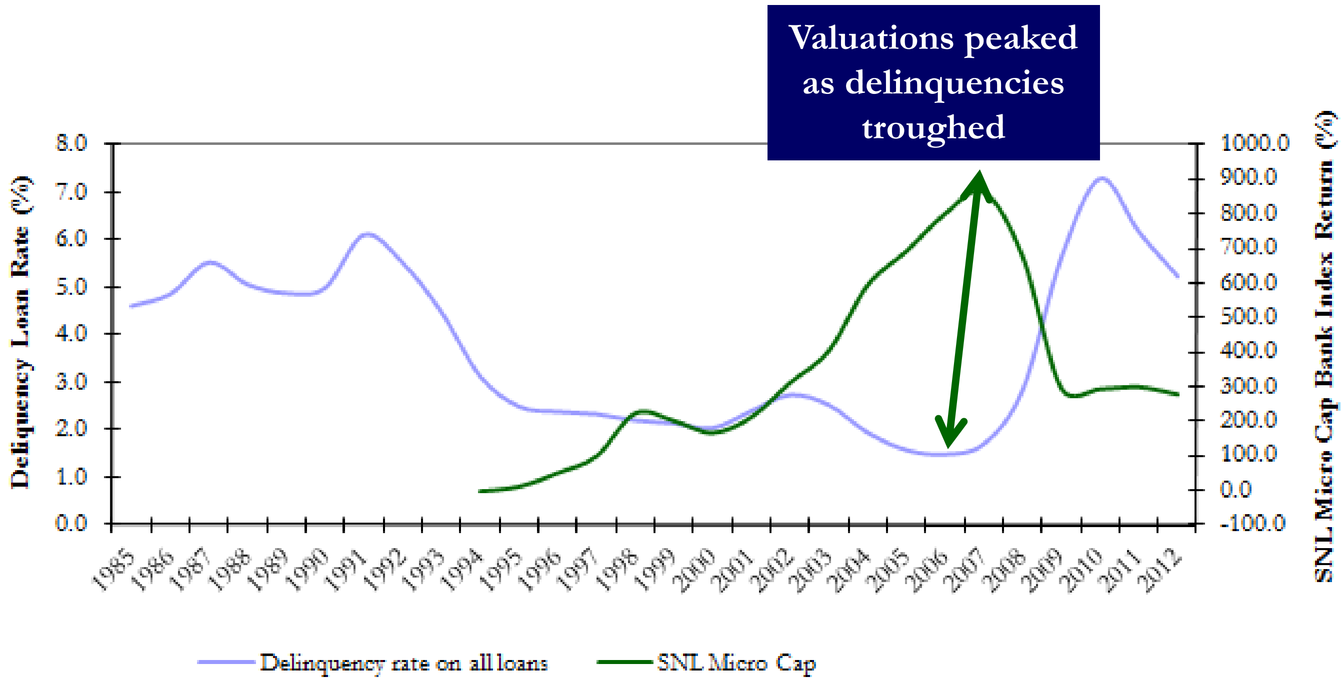
Bank	City	County	Branches	Assets ($000s)	Deposits ($000s)	Tier 1 Leverage Ratio	Nonaccrual + 90PD + OREO / Assets	Texas Ratio (NPAs + 90PD / Tang. Equity + LLR)	Date of Failure	Acquirer
Fidelity Bank	Dearborn	Wayne, MI	15	818,237	747,640	2.30%	18.89%	261.42%	3/30/2012	Huntington National Bank
Community Central Bank	Mt. Clemens	Macomb, MI	4	476,334	385,350	0.16%	12.28%	303.83%	4/29/2011	First Michigan Bank
Peoples State Bank	Hamtramck	Wayne, MI	10	390,524	389,868	-0.25%	15.49%	592.24%	2/11/2011	First Michigan Bank
Paramount Bank	Farmington Hills	Oakland, MI	4	252,744	213,550	0.98%	8.99%	275.01%	12/10/2010	Level One Bank
MainStreet Savings Bank, FSB (MHC)	Hastings	Barry, MI	2	93,701	62,374	1.34%	8.13%	312.75%	7/16/2010	Commercial National
New Liberty Bank	Plymouth	Wayne, MI	1	111,239	101,884	0.10%	12.95%	638.08%	5/14/2010	Bank of Ann Arbor
CF Bancorp	Port Huron	St. Clair, MI	22	1,599,122	1,418,445	-4.89%	7.89%	1042.75%	4/30/2010	First Michigan Bank
Lakeside Community Bank	Sterling Heights	Macomb, MI	1	49,173	48,622	0.73%	12.29%	288.57%	4/16/2010	None
Citizens State Bank	New Baltimore	Macomb, MI	7	168,551	157,149	1.23%	13.73%	432.44%	12/18/2009	None
Home Federal Savings Bank	Detroit	Wayne, MI	2	12,994	12,730	0.75%	14.48%	582.66%	11/6/2009	Liberty Bank and Trust Company
Warren Bank	Warren	Macomb, MI	6	504,816	467,767	1.09%	19.29%	514.99%	10/2/2009	Huntington - Deposits Only
Michigan Heritage Bank	Farmington Hills	Oakland, MI	4	167,710	149,065	1.39%	10.81%	183.35%	4/24/2009	Level One Bank - Deposits Only
Main Street Bank	Northville	Wayne, MI	2	112,368	98,934	2.28%	9.49%	236.29%	10/10/2008	Monroe Bank & Trust
		Total	80	4,757,513	4,253,378					

Historical Valuation Multiples of Bank Stocks



"Micro Cap" bank stocks are being valued near the lowest levels they have been in over 15 years

Improving Credit Should = Improving Valuations



Note: Delinquent loans are those past due thirty days or more and still accruing interest as well as those in nonaccrual status.

There is a high historical correlation between the value of bank stocks and credit quality, however, the small community bank stock prices have not rebounded back this cycle to the extent of the larger banks

2. Where Has This Left Us?

Shareholder Objectives vs. Regulator Objectives

Shareholder Objectives		Regulator Objectives
Maximize Earnings	⟷	Conservative Lending
Maximize ROE	⟷	Well-Capitalized
Pay Cash Dividends	⟷	Preserve Capital
Grow Earning Assets	⟷	Reduce C&D and CRE Lending
Maximize Shareholder Value	⟷	Safety and Soundness

The current regulatory environment will put pressure on bank business strategies and profitability

Federal Reserve Beige Book Loan Data – Midwest Market

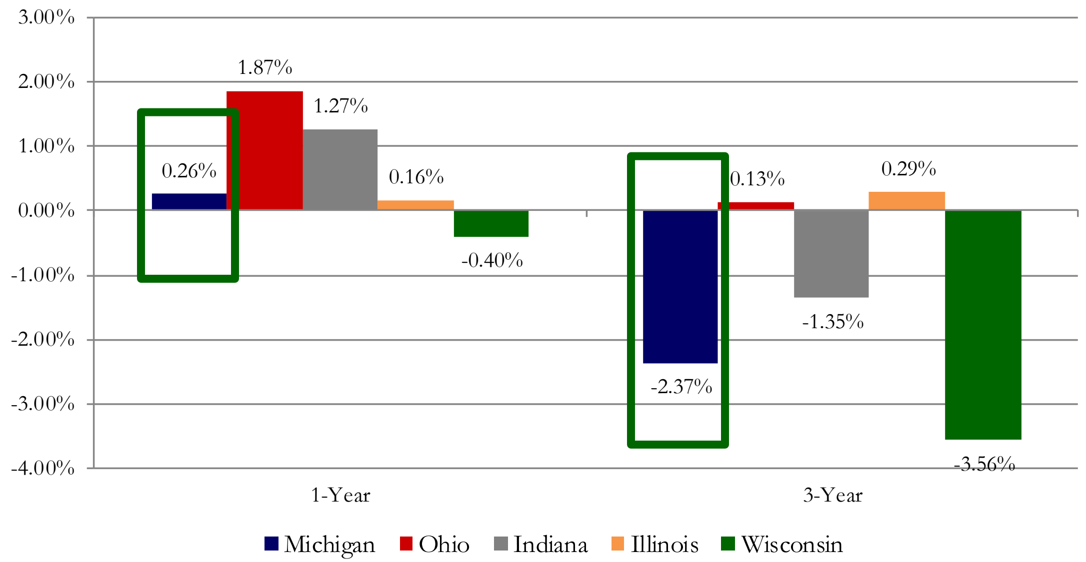
- Demand for business credit flat
- Demand for CRE loans rising again
- Credit card balances coming down, HELOC and auto lending are up
- Lower delinquencies
- Core deposits are growing
- Net interest margins shrinking
- Cost controls (layoffs) coming

Tepid Midwest/Michigan Loan Growth

Loan growth has been negligible in the past year (and negative the past 3 years), particularly in Michigan, as local economies have been hurt, real estate values have significantly declined, and regulatory pressures (FDIC, state, Federal Reserve, Dodd-Frank, Basel III, etc…) are forcing banks to hold more capital – which in turn limits lending ability

Michigan has the highest population per banking institution in the Great Lakes, and with many regional and national banks pulling back their lending efforts in the state during this credit cycle, Michigan would appear to be underbanked when compared to its neighbors

Median Loan Growth by State



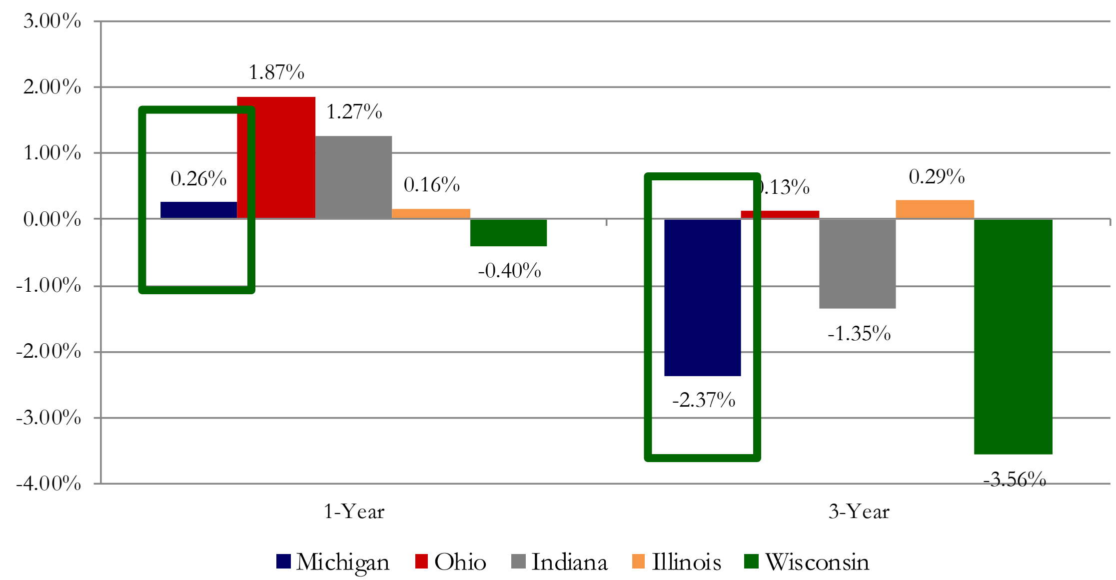
Percentage of Banks with Positive Loan Growth

	Michigan	Ohio	Indiana	Illinois	Wisconsin
1-Year	52.31%	58.72%	61.27%	52.68%	50.55%
3-Year	46.15%	51.91%	47.89%	53.20%	42.44%
Total Banks	130	235	142	579	271
Population per Bank	77,728	49,383	45,633	22,607	21,187

Tepid Midwest/Michigan Loan Growth to Continue?

As of December 31, 2012, 86 banks in the five states listed below are carrying a Tier 1 Leverage Ratio below 7%, and 105 banks have a Texas Ratio greater than 75%, with Illinois leading in both categories. Both of these figures suggest a good portion of the banking institutions in the Great Lakes states will be limited in their lending abilities going forward without additional capital.

Median Loan Growth by State



Percentage of Banks with Capital or Credit Quality Problems

	Michigan	Ohio	Indiana	Illinois	Wisconsin
< 7% Tier 1	7.69%	2.98%	2.82%	8.98%	4.80%
> 75% Texas Ratio	10.00%	3.83%	2.82%	10.02%	7.75%

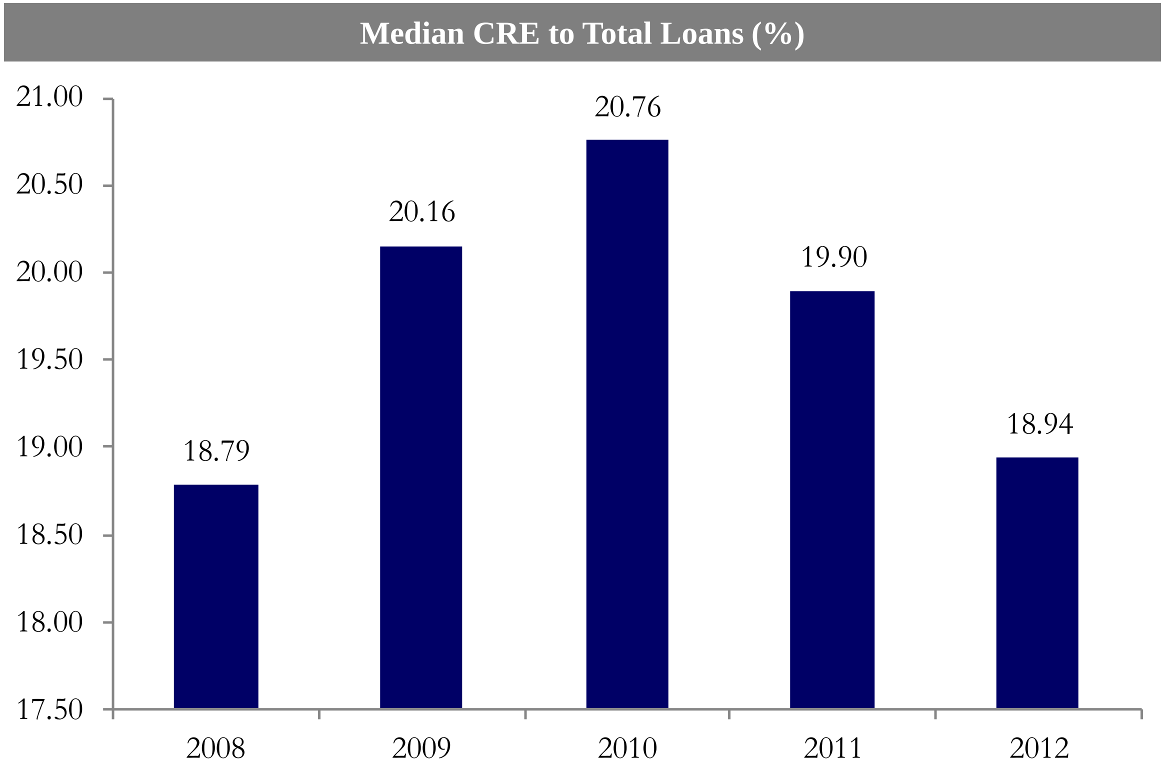
Michigan Public Peer Group

(In $000s, except per share data)

							Valuation Summary:				
Company	**Ticker**	**Stock Price (as of 4/16/2013)**	**Avg. Daily Volume (One-Year)**	**One-Year Return**	**Assets**	**Tangible Common Equity**	**Core Deposit Trading Premium**	**P / BV**	**P / TBV**	**P / LTM EPS**	**P / LTM Core EPS**
Birmingham Bloomfield Bancshares, Inc.	BBBI	$4.95	400	52.8%	$152,773	$12,383	-3.79%	72.94%	72.94%	8.84x	8.84x
Capital Directions, Inc.	CTDN	$47.55	0	0.0%	$127,606	NA	NA	207.47%	207.47%	NM	NA
Century Financial Corporation	CYFL	$12.30	281	74.9%	$266,001	$28,634	-2.21%	84.35%	84.35%	11.18x	11.18x
Chemical Financial Corporation	CHFC	$24.11	40,009	14.9%	$5,990,528	$473,174	NA	109.76%	140.29%	12.82x	12.25x
ChoiceOne Financial Services, Inc.	COFS	$15.25	1,244	17.2%	$508,913	$45,054	1.47%	83.13%	111.63%	11.82x	11.77x
CNB Corporation	CNBZ	$10.50	74	56.5%	$260,898	$18,716	-2.79%	68.00%	68.00%	9.13x	10.48x
Commercial National Financial Corporation	CEFC	$7.90	254	-3.3%	$364,729	NA	NA	119.16%	126.51%	12.54x	NA
County Bank Corp	CBNC	$18.00	938	16.8%	$301,808	$30,892	-4.60%	62.98%	62.98%	10.40x	18.29x
CSB Bancorp, Inc.	CBMI	$135.00	0	2.2%	$237,584	$27,078	-5.58%	60.83%	60.83%	6.06x	6.10x
Eastern Michigan Financial Corp	EFIN	$13.60	42	11.6%	$270,472	$26,617	-4.95%	57.82%	57.82%	8.25x	8.25x
Fentura Financial, Inc.	FETM	$5.60	2,260	106.0%	$310,722	$16,203	-0.98%	84.52%	84.52%	10.78x	10.91x
First Federal of Northern Michigan Bancorp,	FFNM	$4.54	1,722	14.6%	$213,834	$24,277	-8.45%	53.59%	53.93%	NM	NA
Firstbank Corporation	FBMI	$12.50	8,390	33.9%	$1,498,762	$93,672	0.62%	76.85%	106.78%	10.78x	10.06x
HCB Financial Corporation	HCBN	$14.55	31	23.5%	$258,779	$25,251	-4.60%	61.42%	61.42%	11.73x	11.73x
Independent Bank Corporation	IBCP	$8.44	104,918	257.6%	$2,023,867	$46,796	2.01%	151.17%	164.01%	10.55x	12.11x
Isabella Bank Corporation	ISBA	$25.30	966	9.8%	$1,430,639	$117,957	9.75%	117.92%	164.44%	16.22x	16.73x
Macatawa Bank Corporation	MCBC	$5.79	145,446	67.3%	$1,560,718	$97,343	4.94%	161.81%	161.81%	4.42x	4.39x
Mackinac Financial Corporation	MFNC	$8.95	3,846	41.3%	$545,980	$61,448	-2.85%	80.98%	80.98%	5.93x	5.93x
MBT Financial Corp.	MBTF	$4.09	34,451	101.5%	$1,268,595	$83,564	-1.09%	85.13%	85.14%	8.35x	9.22x
Mercantile Bank Corporation	MBWM	$17.35	12,850	17.2%	$1,385,355	$149,692	NA	100.90%	100.90%	11.49x	11.49x
Southern Michigan Bancorp, Inc.	SOMC	$17.53	1,037	44.1%	$528,860	$39,872	0.51%	76.23%	104.46%	9.53x	9.09x
Sturgis Bancorp, Inc.	STBI	$7.75	495	39.6%	$317,045	$21,735	-2.73%	58.67%	72.68%	8.42x	8.41x
United Bancorp, Inc.	UBMI	$5.30	9,674	53.6%	$907,741	$76,921	-1.35%	87.55%	87.55%	20.38x	19.27x
University Bancorp, Inc.	UNIB	$2.17	372	66.9%	$133,604	NA	NA	132.07%	132.02%	9.03x	NA
West Shore Bank Corporation	WSSH	$20.85	137	45.4%	$368,414	$32,493	-1.97%	85.21%	85.64%	12.42x	12.58x
Wolverine Bancorp, Inc.	WBKC	$18.88	704	27.2%	$285,281	$62,447	-13.18%	74.35%	74.35%	29.97x	29.97x
High			145,446	257.6%	5,990,528	473,174	9.75%	207.47%	207.47%	29.97x	29.97x
Mean			14,252	45.9%	827,673	70,096	-1.99%	92.88%	100.52%	11.29x	11.78x
Median			**952**	**36.8%**	**340,887**	**39,872**	**-2.21%**	**83.74%**	**85.39%**	**10.66x**	**11.05x**
Low			0	-3.3%	127,606	12,383	-13.18%	53.59%	53.93%	4.42x	4.39x

Michigan Public Peer Group – *CRE/Total Loans*

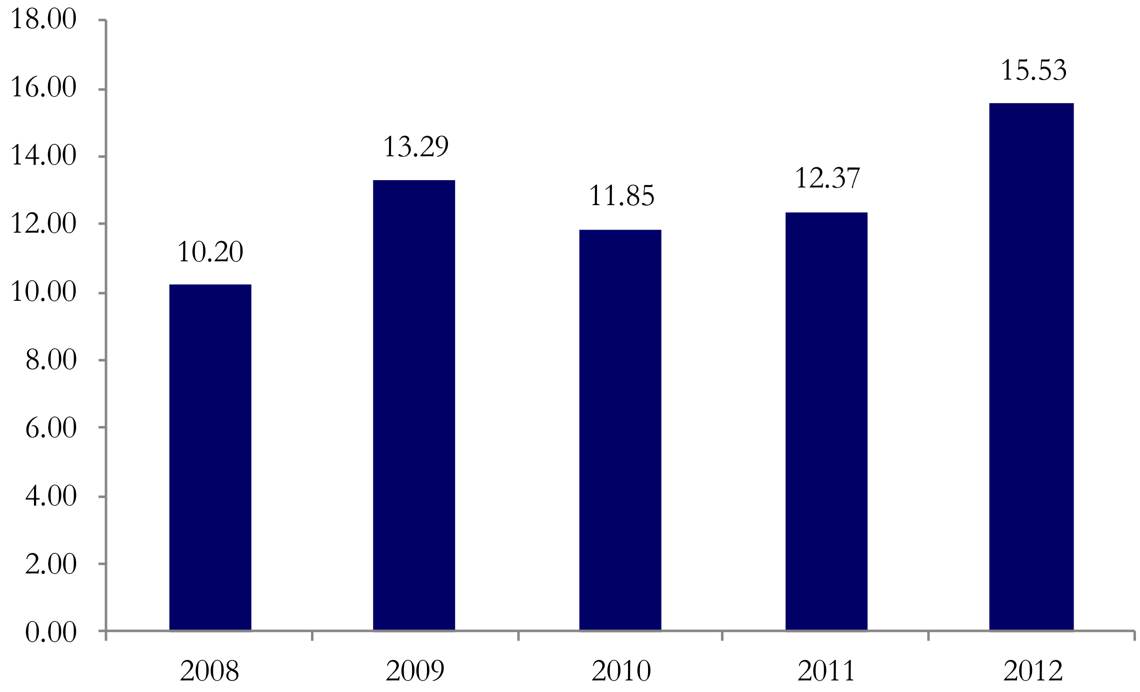
Michigan banks saw a spike in commercial real estate as a percentage of total loans in 2010, with many banks not having an immediate exit strategy for its CRE concentrations in the state. Over the last few years, we have seen that exposure come down to pre-crisis levels.



Michigan Public Peer Group – *Non-Owner Occupied/Total Loans*

Non-owner occupied CRE has actually risen post Credit Crisis. This is predominantly due to fewer quality C&I credit opportunities in the market and the need to put unencumbered capital to use. We foresee this trend continuing as competition for loans is strong in Michigan.

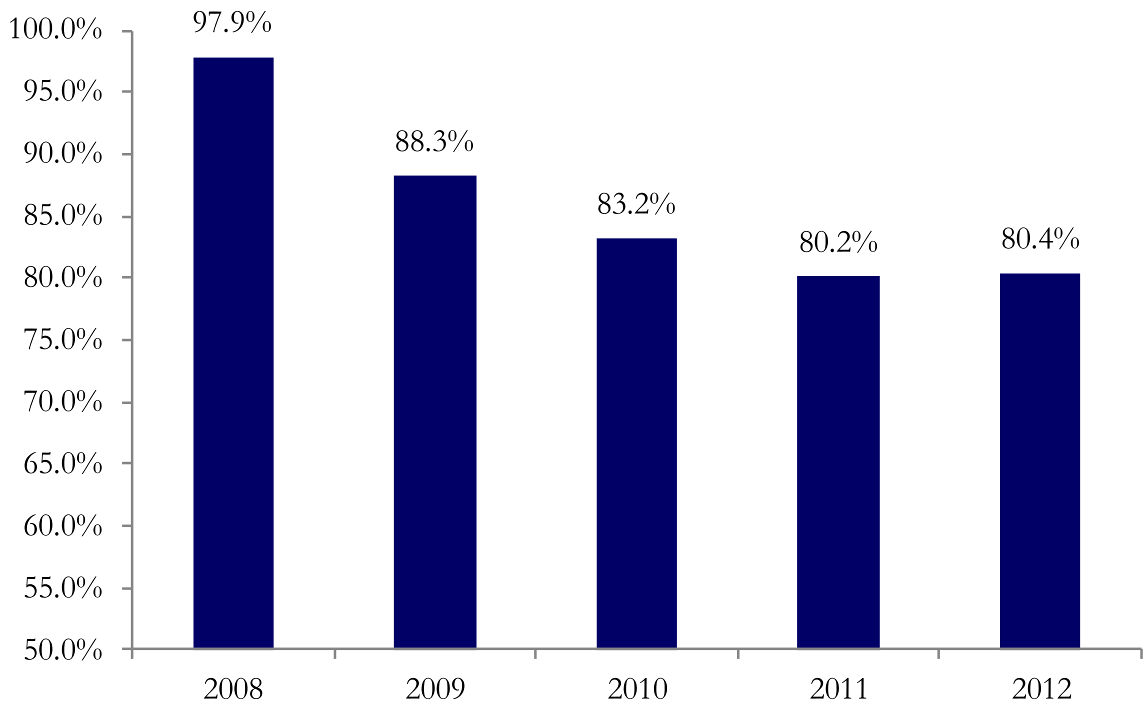
Median Non-owner Occupied CRE to Total Loans (%)



Michigan Public Peer Group – *Loan to Deposit Ratio*

Loan to deposit ratio for the peer group has been gradually declining over the past several years, as loan portfolio growth is challenged and the deposit base is steadily increasing year over year, reaching a median of $248.5 million in 2012 for the peer group – a 3.72% CAGR from 2008.

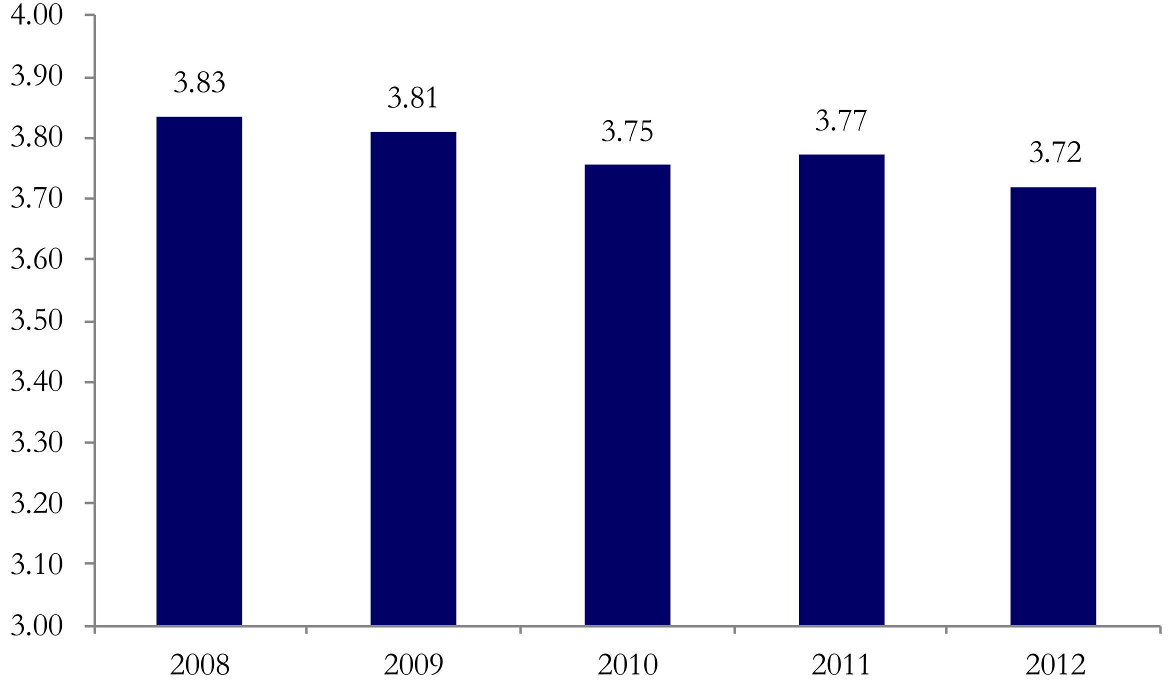
Median Loan to Deposit Ratio (%)



Michigan Public Peer Group – *Net Interest Margin*

Banks have seen increasing pressures on net interest margins over the past 5 years. In 2012, we saw NIM reach a low point of 3.72%, 11 basis points lower than 2008. With competition for new loans being very high, we anticipate this declining trend will continue in 2013.

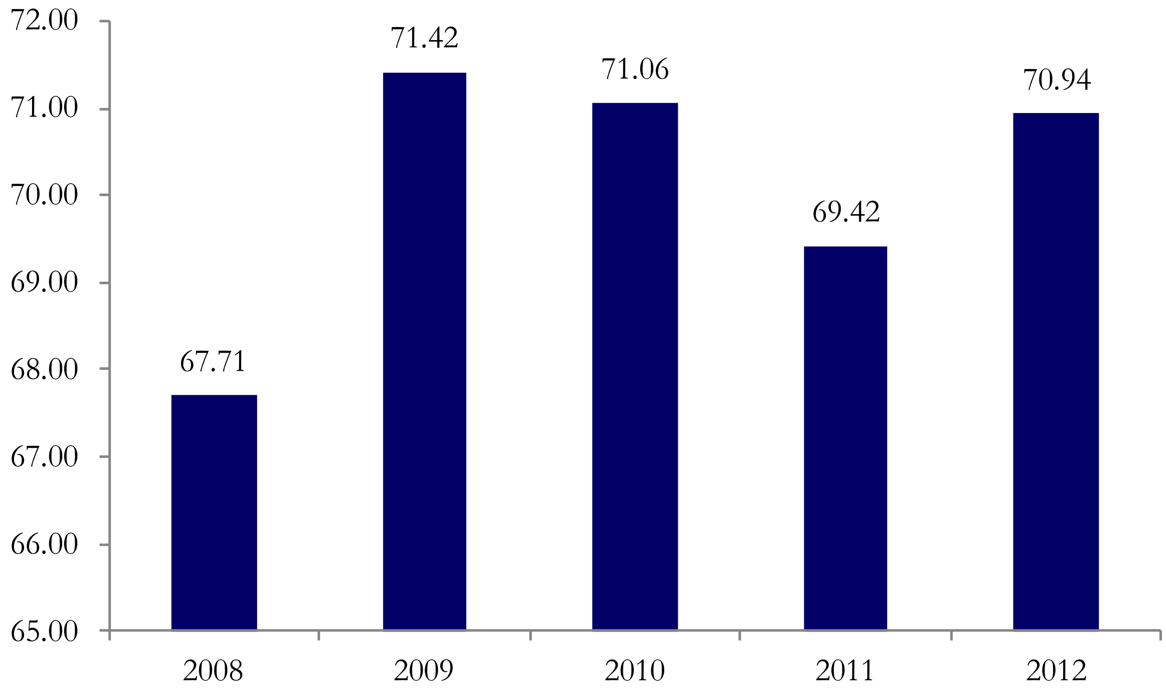
Median Net Interest Margin (%)



Michigan Public Peer Group – *Efficiency Ratio*

The Efficiency Ratio has risen since 2008. We anticipate this trend will continue in 2013, as rates remain flat.

Median Efficiency Ratio (%)



Financial Performance Trends

- Lower Net Interest Margins +
- Higher Operating Costs (= higher efficiency ratio) +
- Lower Fee Income (interchange, overdraft) +
- Higher Credit Costs = Lower Profitability = **Lower Stock Price**

There appears to be a permanent "squeeze" on the bank profitability model which is reflected in lower earnings and soft stock prices

3. Who Do We Admire?

Midwest Public Peer Group

This Midwest peer group consists of public companies located in IL, IN, and OH with total assets greater than $125 million and net interest margins above 4.0%. The median price to tangible book value for this Midwest peer group is nearly 110%, which represents a significant premium over the median Michigan peer group at 85.4%

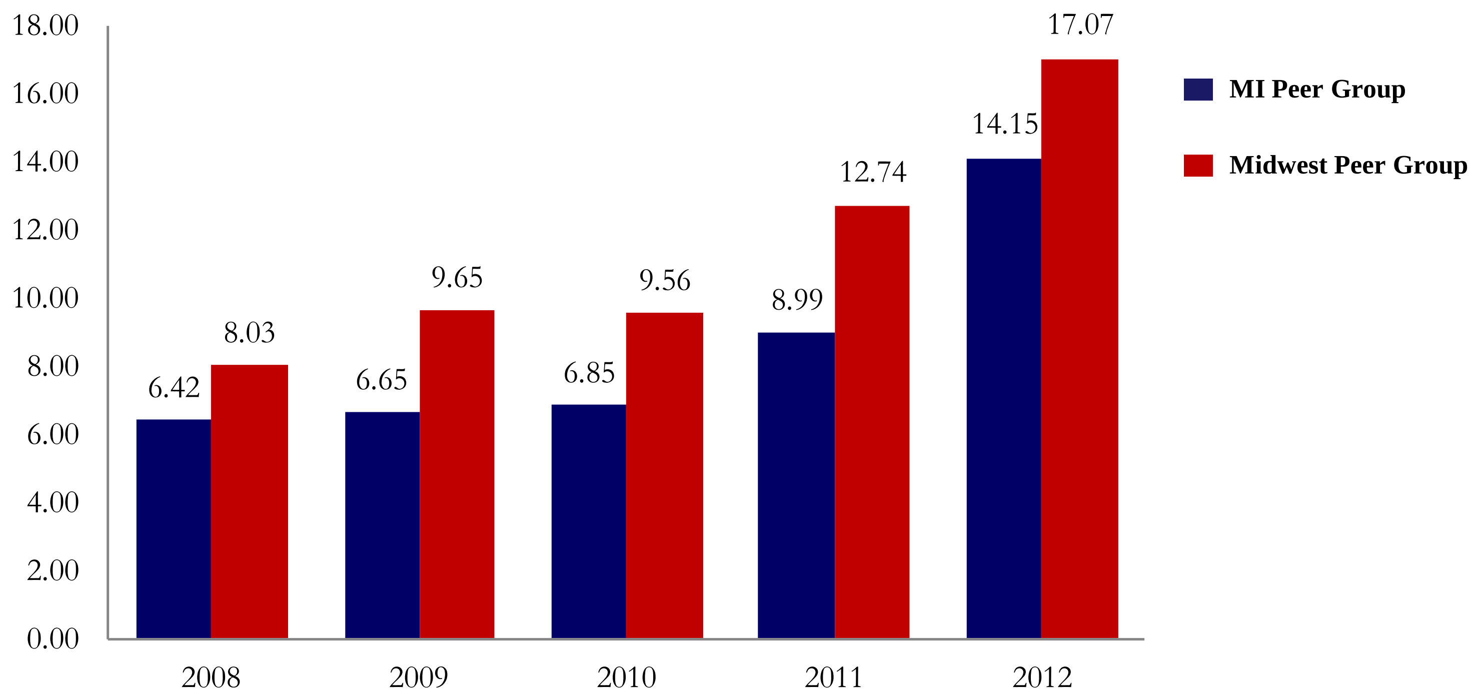
(In $000s, except per share data)

Company	State	Ticker	Stock Price (as of 4/16/2013)	Avg. Daily Volume (One-Year)	One-Year Return	Assets	Tangible Common Equity	Core Deposit Trading Premium	P / BV	P / TBV	P / LTM EPS	P / LTM Core EPS
								Valuation Summary:				
Allied First Bancorp, Inc.	IL	AFBA	$1.25	36	594.4%	$126,240	$1,079	-0.74%	52.48%	59.24%	1.84x	NA
Commercial Bancshares, Inc.	OH	CMOH	$20.45	281	-4.6%	$301,564	$29,388	-2.23%	81.40%	81.40%	8.21x	8.21x
Community Bank Shares of Indiana, Inc.	IN	CBIN	$15.33	1,646	15.7%	$819,500	$57,804	-1.07%	88.43%	89.40%	7.44x	9.12x
Community First Bank of Indiana	IN	CFHW	$9.00	0	1.2%	$194,311	$19,471	-5.08%	59.38%	59.38%	7.01x	7.01x
F.S. Bancorp	IN	FXLG	$43.10	151	3.7%	$493,945	$43,900	1.11%	100.84%	109.69%	9.29x	NA
First Financial Bancorp.	OH	FFBC	$15.39	188,830	-1.5%	$6,497,048	$608,015	6.12%	125.75%	146.93%	13.50x	13.79x
First Financial Corporation	IN	THFF	$29.45	23,820	-0.7%	$2,895,408	$330,617	2.97%	105.16%	118.36%	11.88x	11.61x
First Merchants Corporation	IN	FRME	$14.61	56,907	23.8%	$4,304,821	$311,799	3.65%	90.87%	134.45%	10.36x	12.24x
First Savings Financial Group, Inc.	IN	FSFG	$21.82	2,280	27.9%	$652,634	$56,119	NA	76.19%	90.12%	11.61x	NA
Home Loan Financial Corporation	OH	HLFN	$19.00	889	62.8%	$167,238	$20,683	5.32%	128.29%	128.29%	9.69x	9.69x
Horizon Bancorp	IN	HBNC	$19.53	13,063	65.4%	$1,848,227	$122,672	4.13%	114.91%	137.19%	8.49x	7.93x
MainSource Financial Group, Inc.	IN	MSFG	$13.68	27,486	21.6%	$2,769,288	$237,893	1.97%	89.94%	116.76%	10.52x	9.85x
Ohio Valley Banc Corp.	OH	OVBC	$19.44	2,095	13.5%	$769,223	$74,549	0.80%	104.15%	105.93%	11.11x	11.10x
Old National Bancorp	IN	ONB	$12.77	401,031	3.7%	$9,543,623	$826,525	6.71%	108.16%	156.32%	13.44x	12.70x
United Bancorp, Inc.	OH	UBCP	$7.28	3,570	-21.1%	$438,354	$36,321	0.85%	106.79%	107.69%	15.17x	14.68x
High				401,031	594.4%	9,543,623	826,525	6.71%	128.29%	156.32%	15.17x	14.68x
Mean				48,139	53.7%	2,121,428	185,122	1.75%	95.52%	109.41%	9.97x	10.66x
Median				**2,280**	**13.5%**	**769,223**	**57,804**	**1.54%**	**100.84%**	**109.69%**	**10.36x**	**10.47x**
Low				0	-21.1%	126,240	1,079	-5.08%	52.48%	59.24%	1.84x	7.01x

Midwest Public Peer Group – *DDA/Total Deposits*

Both peer groups have experienced similar upward trends in demand deposits as a percentage of total deposits over the past five years. In 2012, both groups saw a dramatic increase in DDAs as interest rates were low and remain flat.

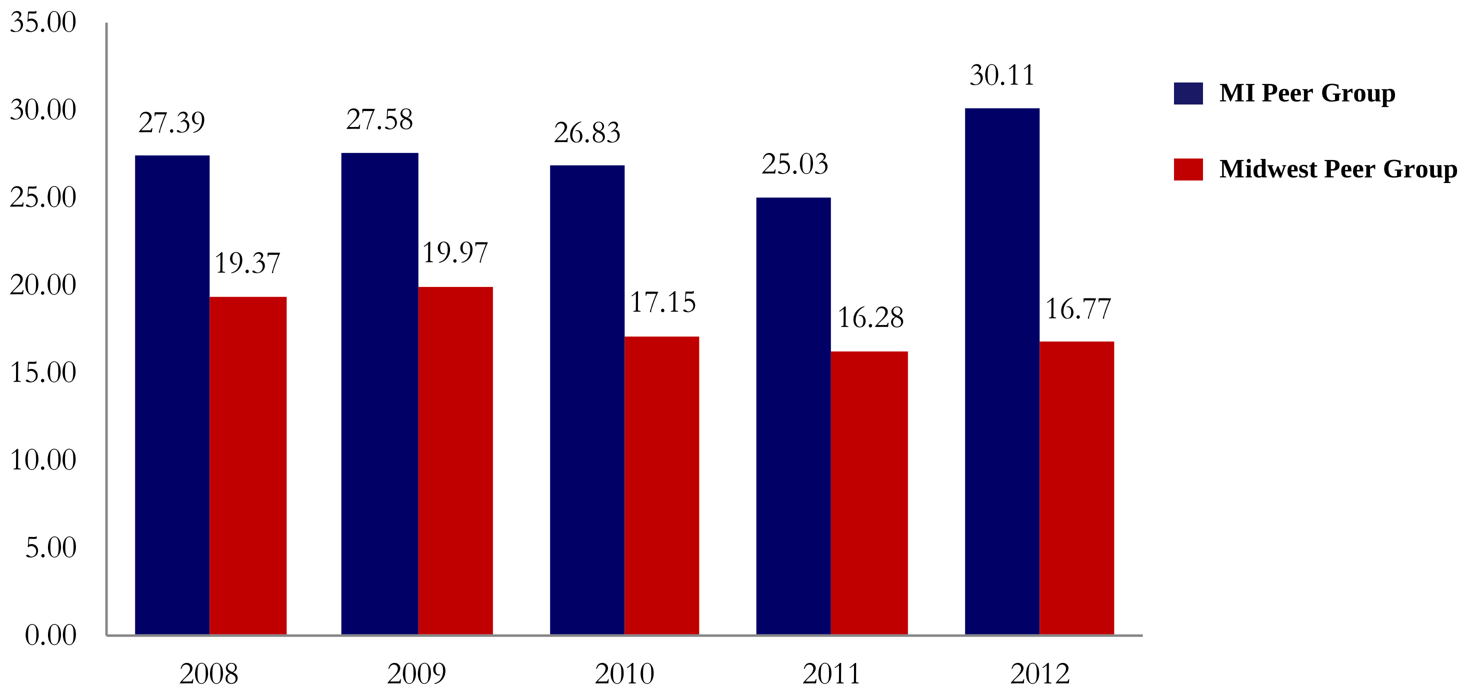
Median DDA/Total Deposits (%)



Midwest Public Peer Group – *Noninterest Income*

The Michigan peer group has historically generated more income from non-portfolio operations than its Midwest counterparts. Over the past five years, however, we have seen the gap between the two groups grow, as Michigan banks have increased their noninterest income activities as a percentage of total income while Midwest banks have decreased.

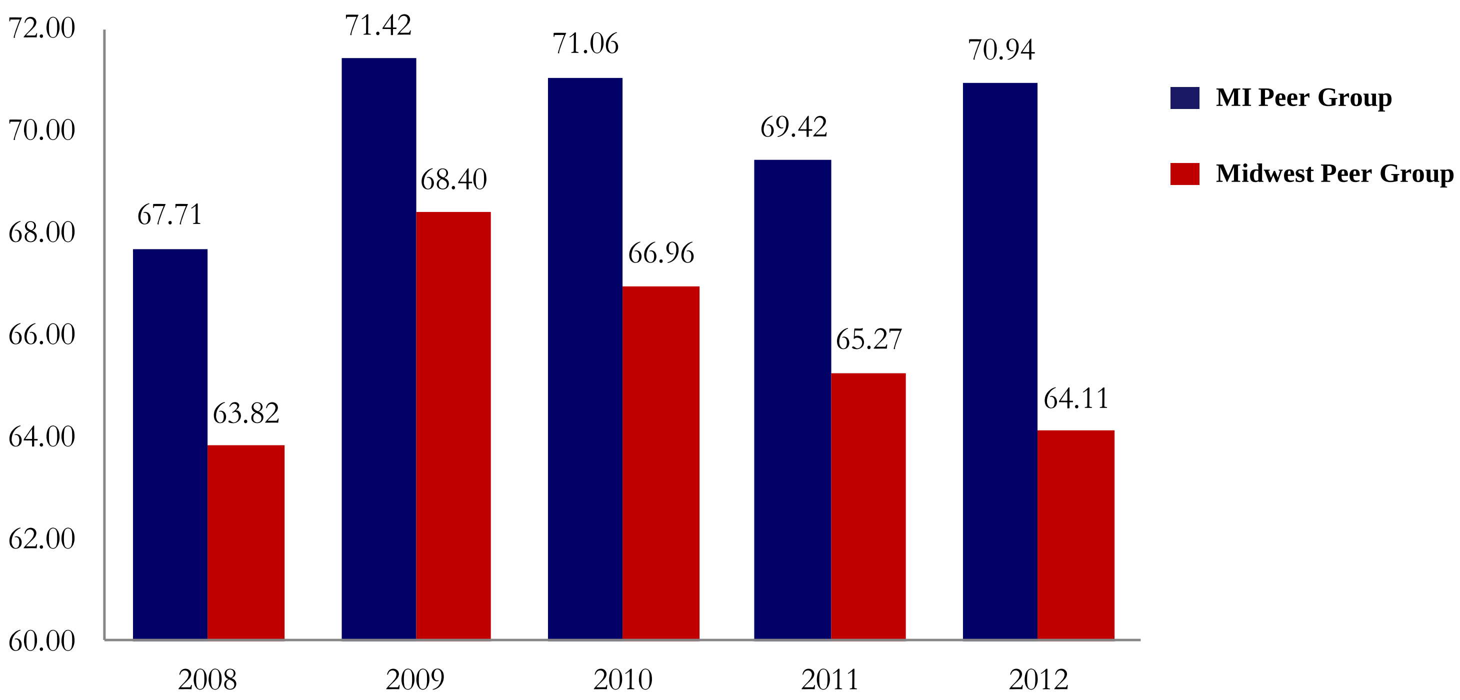
Median Noninterest Income as percentage of Total Income (%)



Midwest Public Peer Group – *Efficiency Ratio*

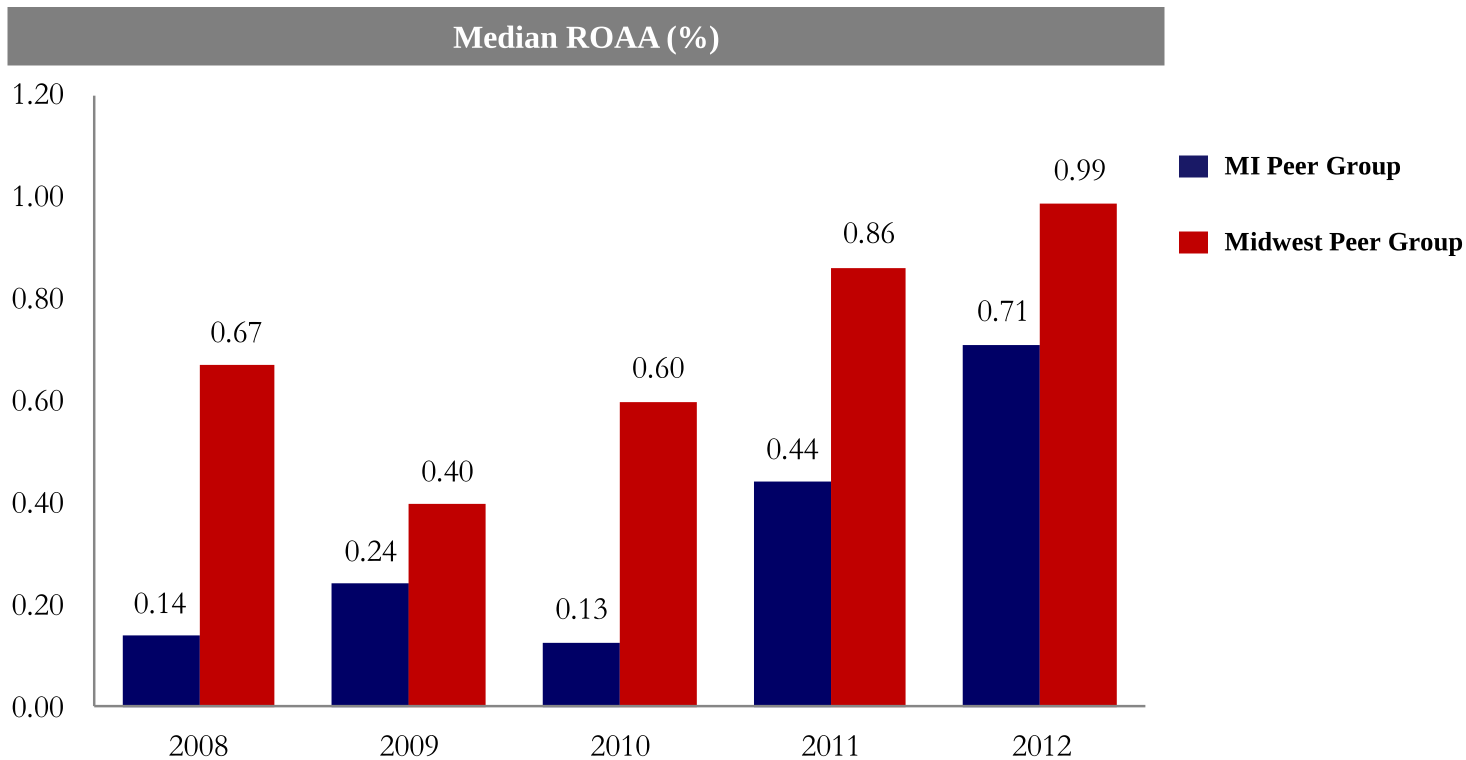
The Michigan peer group has higher efficiency ratios than its Midwest counterparts, and historically has. The gap continues to widen as the Michigan peer group is not making much headway in improving its ratio, whereas the Midwest peer group has consistently lowered its since 2009. In order to combat top line income pressure, banks will have to focus on managing costs.

Median Efficiency Ratio (%)



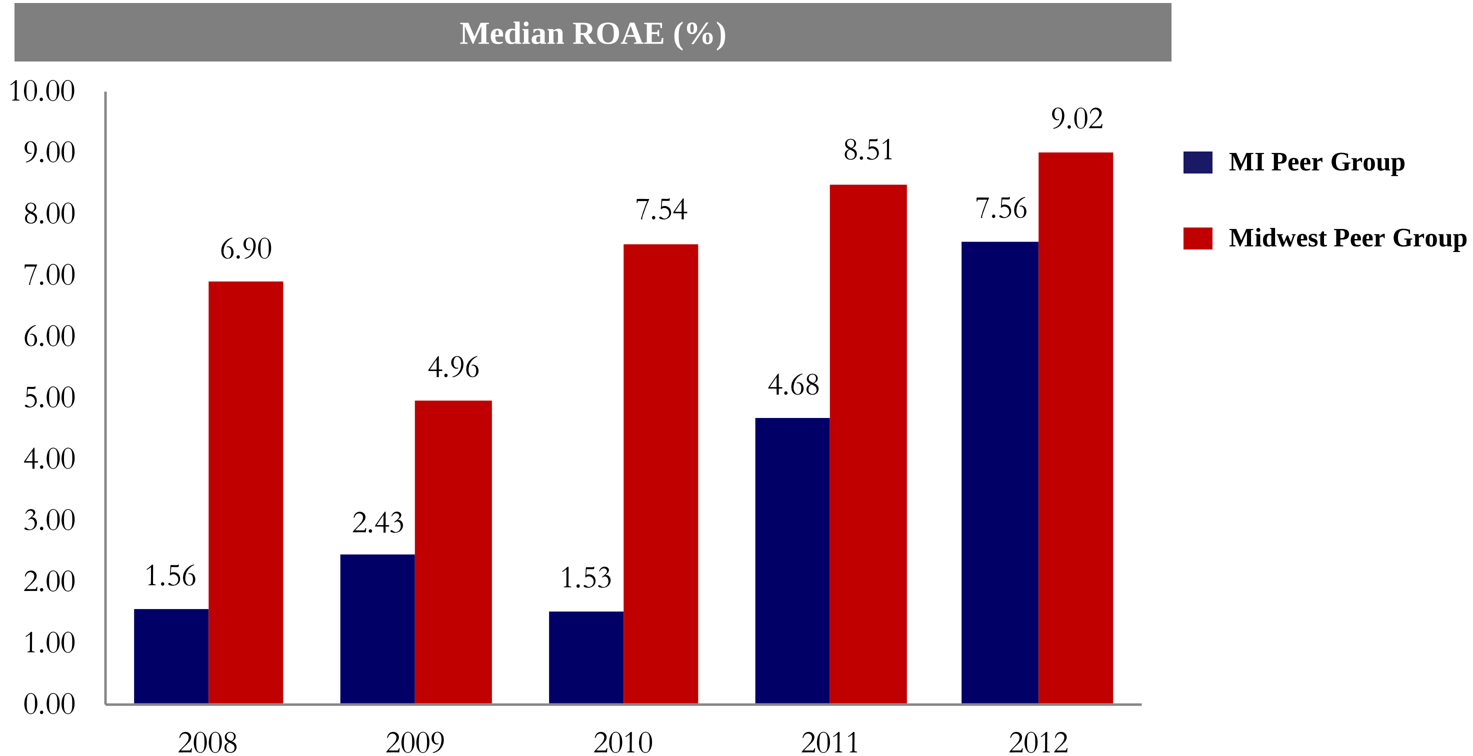
Midwest Public Peer Group – *ROAA*

The Michigan peer group is trending upwards nicely from a ROAA standpoint but still lags the Midwest peer group. The Midwest peer group is approaching a level that historically is well accepted in the investor community – how much higher will the Michigan peer group be able to go?



Midwest Public Peer Group – *ROAE*

Similar to the trends we see in the ROAA calculation, the Midwest peer group has historically achieved higher returns than the Michigan peer group.



4. Techniques to Generate Prudent Loan Growth

SBA Lending

- Established in 1953; Enhanced under Jobs Act of 2010
- 7(a) (variable rate) and 504 (fixed rate) lending most common
- Opens opportunity for lending opportunities due to 75% federal loan guaranty
- Opportunity for Fee Income selling guaranteed portion in secondary market

Community Banks can distinguish themselves with a robust SBA effort

SBA Lending – Case Study – Metro Phoenix Bank (AZ)

- Total Assets of $73.9 million; SBA "Certified" lender status; Seeking "Preferred" lender status
- Total SBA dedicated lenders: 4
- Total SBA support staff: 4
- 2012 Net Interest Income (pre-provision) - $2,146,000
- 2012 Noninterest Income – $2,810,000 (SBA Gains – $1.8 million; avg. premium 13-15%)
- Avg. Loan Size - $850,000
- 2012 Noninterest Income/Total Income = 43.3%
- 2012 ROAA – 1.99%; ROAE – 15.84%

Metro Phoenix has distinguished itself in the SBA market and generated above average returns on assets and equity

Mortgage Banking

- Credit Crisis arose due to mortgage debacle
- Increased Regulatory requirements ensued (Dodd-Frank, S.A.F.E. Act)

But….

- Low interest rates
- Improving economy
- Shrinking number of competitors
- Government guarantees

Means….

- Increasing mortgage lending volume for community banks

Some community banks are going from a "passive" to a "dedicated" effort in mortgage banking

Mortgage Banking – Case Study – Bank of Manhattan (CA)

- 7 year old de novo bank based in LA area
- Embarked on mortgage banking division 2 years ago
- Specialized mortgage banking talent hired
- Complements community banking

Dedicated Mortgage Loan officers:	40
Mortgage Support Staff:	60
Total Bank Assets:	$464 million
Net Interest Income (pre=provision):	$15,675,000
Noninterest Income:	$18,551,000
Mortgage Origination (volume):	$1.5 billion
Originations/Total Bank Assets:	3.2x

The disproportionate mortgage banking revenue creates significant operating leverage for Bank of Manhattan while still staying true to its community banking roots

Vendor Finance

- Opportunity to finance the product line of a major Manufacturer/Franchisor
- Deal directly with Manufacturer/Franchisor or through a seasoned broker specializing in the paper
- Allows you to turn spigot "on" or "off" depending on liquidity
- Paper is usually 36 to 48 month full payout
- Borrower financials provided
- Some credits are credit scored (larger borrowers)

While "backyard" lending is still the hallmark of community banking, a well developed vendor/franchise lending operation can generate much needed loan volume

Vendor Finance – Case Study – Bank of Cape Cod, MA

- 7 year old de novo staffed by ex BankBoston (now BofA) lenders with 20+ years of Vendor Finance/Franchise lending backgrounds
- Major program with a national computer company (they are only community bank on approved list)
- Major Franchise Finance program with Dunkin Donuts
- Deals are brought through a broker
- Financials, D&B, LexisNexis due diligence
- Average pricing 50 - 200 basis points over tradition local portfolio
- Remarketing arrangements with vendors mitigates risk

Hiring bankers with specialty skill sets can differentiate a community bank against its competition

Loan Participations

- Loans participations still a viable source of loan growth
- Allows community bank to purchase loans from banks with excess loan demand or legal limit issues
- Sources include:
  - <u>Local</u> community banks
  - <u>Regional</u> correspondent banks (i.e. Great Lakes or United Bankers Bank)
  - <u>National</u> correspondent banks (i.e. Pacific Coast Bankers Bank, BancAlliance)
- While re-underwritten locally, much of the up-front work is done by the correspondent bank

Many banks facing a liquidity surplus have turned to a "limited" amount of participation lending

Case Study - BancAlliance

- The BancAlliance (BA) network is a shared corporate and specialty lending platform
- BA identifies, evaluates and refers loan and lease opportunities to community banks
- Banks join BA with a pay-as-you-go fee structure
- Members evaluate asset opportunities but are not obligated to acquire any particular loan opportunity
- Members are supported by a sophisticated technology platform (portal) for asset selection, evaluation, and monitoring with loan servicing performed for BancAlliance
- Individual credit files are maintained at a high documentation standard to facilitate ongoing monitoring and examiner reviews
- BA receives a portion of the loan yield as compensation

United Bank of Michigan (Grand Rapids) is a member of the BancAlliance program

Toehold Investment in Another Community Bank

- Post Credit Crisis, many community banks are raising capital

- One source of capital is selling stock to a regional community bank up to 9.9%

- Investing bank has three motivations:
  - ✓ Make a good return on the investment
  - ✓ Generate two-way loan participations
  - ✓ Have a "seat at the table" if the bank decides to sell

- Allows sponsoring bank to enter a new market and generate loan volume

Several Michigan banks including Firstbank, Fentura Financial and Isabella Bank Corporation have deployed this tactic

Case Study – German American Bancorp

- In 2004, GABC made a 9.9% investment in American Community Bancorp, Inc. (ACBI) (Predecessor)
- Chairman of GABC goes on ACBI board
- Chairman sits on ACBI Loan Committee
- Loan participation shared both ways
- In January, 2011 GABC acquires ACBI

This situation was a "Win-Win" for both organizations

Be an Industry Specialist

- Being an industry specialist allows for the following:
  - ✓ Value-add when meeting with prospects
  - ✓ Best practices when structuring loan terms/covenants
  - ✓ More efficient knowledge base (less steep learning curve)
  - ✓ Referrals from others in the industry
  - ✓ Geographic diversification
  - ✓ More customer loyalty

Community Banks should strategize as to whether specialization will enhance loan growth opportunities

Case Studies – Industry Specialization

- JP Morgan (NY) – Automotive Lending
- Wells Fargo (MN) –Finance Companies
- Texas Capital (TX) – Mortgage Warehousing
- Comerica (TX) – Entertainment Lending
- IBERIABANK (LA) – Oil & Gas Lending
- Pacific Continental Bank (OR) – Dental Practice Groups
- First Tennessee – Commercial Banks

These banks have established strong reputations in their specific area of expertise

Hire a Team of Bankers

- A lending team brings a "turn key" operation
- A "book of business" usually follows
- New loan and fee income generates early ROI
- Each community banker can bring $15-$20 million of business or more

Many banks have found this to be a very effective tool in growing assets

How to Hire a Team

- Word of mouth networking
- Print, radio or social media (i.e.. LinkedIn)
- Utilize a recruiting firm to:
  - ✓ Retain confidentiality
  - ✓ Identify the candidate
  - ✓ Pre-qualify the candidate
  - ✓ Assist in salary/benefit negotiations

Recruiting firms such as Angott Search Group and others are retained by a number of community banks for this purpose

5. Loan Growth Through M&A

Strategic Transaction Alternatives

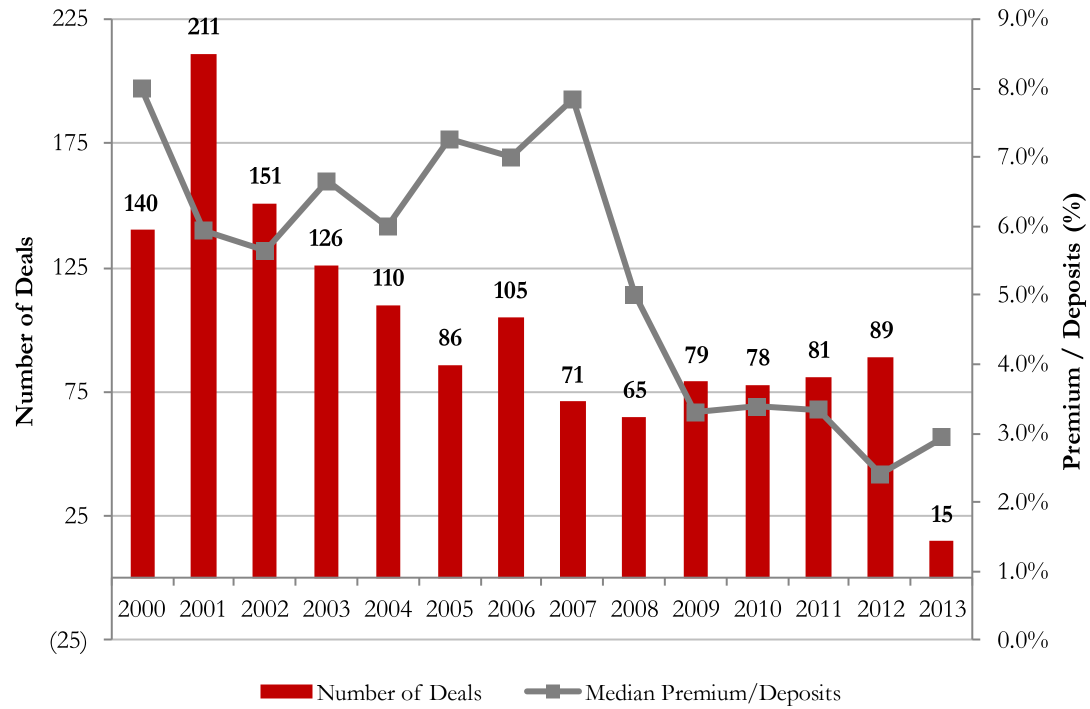
	Positives	Negatives
Whole-Bank Acquisition	✓ Acquire going concern ✓ Favorable valuations ✓ May add Equity ✓ May acquire more human capital / talent than other alternatives ✓ Gain scale	o Fair value accounting issues o Disconnect on valuation expectations? Are there willing sellers? o Cultural integration issues? o Risk of regulatory approval o Possible dilution to current shareholders
Merger of Equals	✓ Gain scale to combat "costs of banking" ✓ "Book to Book" valuation structure ✓ Generally, better for employees of the bank ✓ Ability to choose your partner	o Social issues / culture issues o Fair value accounting issues / capital issues o No immediate liquidity created for shareholders o Costs to terminate certain contracts
Sell the Bank to a Larger Competitor	✓ More product offerings ✓ Higher legal lending limit ✓ More capital to lend	o Possible employee treatment o Possible negative in-market reaction o Possible loss of identity o Culture issues

Strategic Acquisition Alternatives

	Positives	Negatives
Branch Acquisition	✓ May be able to pick which loans to purchase ✓ Core deposit premiums at historical lows ✓ Less integration risk than whole-bank acquisitions ✓ No contracts to cancel / buyout	o Potential customer retention problem as selling franchise still operating o Unlikely to achieve same scale as whole-bank acquisition o Must have capital to support transaction o Risk of regulatory approval
FDIC-Assisted Acquisition	✓ Loss-share guarantee on acquired loans ✓ Can be accretive to book value immediately if deal is priced correctly ✓ Less risk than whole-bank acquisition, and potentially even branch acquisition	o Pricing becoming more competitive, o 10-year relationship with the FDIC if enter into loss-sharing arrangement o Lack of FDIC-assisted opportunities in market

Branch Transactions Gaining Popularity

Historical Branch M&A Activity (Bank & Thrift)



As capital market options remain limited for most community banks, branch transactions have gained popularity as a means to raise capital/divest non-core operations for sellers; and present an opportunity to enter new markets and leverage excess capital into quality loan "growth" for buyers, at historically low premiums (less than 2.0% deposit premium for most small transactions)

6. Summary

Summary

- Bankers are still "smarting" from the Credit Crisis
- Competition is fierce for quality loan opportunities
- Credit and underwriting should not be relaxed to "reach" for opportunities
- Bankers should think "out of the box" as it relates to the type of lending to do
- Strategic planning should consider options to access to new markets via mergers and acquisitions to augment organic loan growth

Institutions in Michigan should consider incorporating many of these concepts into their strategic planning processes.

Summary

Questions?

7. Donnelly Penman Bios

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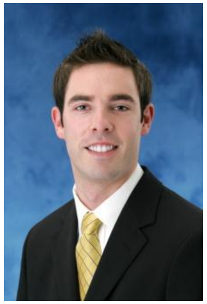

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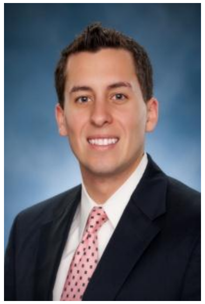

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Financial Institutions - Investment Banking Team

John C. Donnelly - Managing Director

Mr. Donnelly is a Managing Director for Donnelly Penman & Partners (DP&P). DP&P is an investment banking firm specializing in raising capital and advising on mergers and acquisitions in the banking industry. Mr. Donnelly is also the founder and Managing Member of the Donnelly Penman Financial Services Fund, LP (the “Fund”) which invests in community banks throughout the country. Prior to co-founding DP&P in 2000, Mr. Donnelly was a Managing Director in the investment banking department of Raymond James & Associates, Inc. where he focused on the financial services industries. Mr. Donnelly joined Raymond James in 1999 effective with its acquisition of Roney & Co., a Midwest based investment banking and brokerage firm. Mr. Donnelly joined Roney in 1993 where he held the positions of Managing Director and head of the Financial Institutions group and also served on the Executive Committee. From 1983 to 1993, Mr. Donnelly held the positions of Senior Vice President and Director of Corporate Finance at First of Michigan Corporation (now Oppenheimer). Prior to that, he was employed in various credit and lending positions at both Manufacturer's National Bank (now Comerica, Inc.) and Michigan National Bank (now Bank of America).

Mr. Donnelly graduated from Georgetown University and holds a M.B.A. degree from the University of Detroit Mercy. Mr. Donnelly also has Series 7, 24, 27, 55 and 63 licenses with FINRA.

Andrew C. Christians, CFA – Vice President

Joining DP&P in 2006, Mr. Christians specializes in mergers and acquisitions (buy side and sell side), business valuations, financial advisory, strategic analysis, and raising capital for financial institutions. Mr. Christians has also rendered sell-side and valuation services for the automotive, manufacturing, and service industries. Additionally, Mr. Christians has been the Portfolio Manager for the Donnelly Penman Financial Services Fund ($28 million private equity fund dedicated to investing in community bank equities across the nation) since March 2009, in addition to managing accounting, investor relation, and administrative activities. He also sits on the Advisory Board and Investment Committee for the Fund. Prior to joining DP&P, Mr. Christians was an Analyst in Stout Risius Ross' Transaction Advisory Group. At Stout Risius Ross, he specialized in performing financial opinions and consulting services primarily related to mergers and acquisitions, goodwill impairment analyses, and corporate strategic planning. Mr. Christians has earned the right to use the Chartered Financial Analyst (CFA) designation and graduated from the University of Michigan's Ross School of Business with a B.B.A. degree with concentrations in Finance and Accounting.

Financial Institutions - Investment Banking Team

John D. Lewis - Managing Director
Mr. Lewis also serves as an advisor to the Donnelly Penman Financial Services Fund ("the Fund"). He serves as the Chairman of the Fund's investment committee and oversees the governance, portfolio management and fund raising of the Fund. Mr. Lewis will play a similar role with the anticipated second financial services fund and will assist in capital raising. Mr. Lewis has an extensive banking background with a 36-year career at Comerica.

Currently, Mr. Lewis is the non-executive Vice Chairman of Flagstar Bancorp, located in Troy, MI. Prior to Flagstar, Mr. Lewis was Vice Chairman of Comerica through 2006. During his tenure, Mr. Lewis served as a Director of Comerica Incorporated and Comerica Bank, and a member of Comerica's Management Policy Committee and Management Council. Mr. Lewis was instrumental in building and expanding Comerica's presence in Michigan, Florida, California and Texas. As Director of Corporate Planning and Development in the early 1980s, he led the corporate development efforts to identify and successfully negotiate five acquisitions in Michigan, expanding Comerica's presence beyond the Detroit metropolitan area. Later, through the mid-1990s, as Director of Affiliate Banking, he led the team that completed more than 30 mergers and acquisitions, establishing Comerica's footprint in the high growth markets of Florida, Texas and California. Mr. Lewis holds a Bachelor of Science degree from the University of Dayton, and a M.B.A. from the University of Detroit Mercy. He also attended the University of Michigan Graduate School of Banking.

Gregory H. Cunningham – Associate
Mr. Cunningham joined DP&P in 2011. At DP&P, Mr. Cunningham specializes in merger and acquisition transactions, valuations, financial advisory, fairness opinions, and due diligence services for the automotive, manufacturing, distribution, and service industries. Additionally, he provides financial advisory and strategic analysis for financial institutions. Prior to joining DP&P, Mr. Cunningham was a Turnaround Consultant at Kenneth J. Dalto & Associates, where he provided advisory services to middle market companies requiring debt restructuring and refinancing, as well as corporate finance. Mr. Cunningham graduated from Western Michigan University's Haworth College of Business with a B.B.A. degree with a major in Finance and minor in Accounting. Additionally, Mr. Cunningham is pursuing an M.B.A. from the University of Detroit Mercy.