

BankDirector.

## Breakout 2: M&A Diligence for Directors – Do You Know What to Ask?

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#BDAudit24



June 12, 2024

# M&A Diligence for Directors

*Do you know what to ask?*

**Gary L. Svec, CPA**

**Managing Director – Investment Banking**

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## **Important Information:**

*All charts/graphs are for illustrative purposes only. Past performance does not guarantee any results or that any trend will continue.*

*Certain assumptions have been made in connection with analysis presented and changes in market conditions or assumptions may have had material impact on results. There is no guarantee any strategy will be successful.*

**THESIS / BIAS:**  
We believe M&A  
(different from 2008-09)  
is a tremendous opportunity  
to play offense

# Thoughts for Board Review of M&A

## Generic M&A Assumptions

- Credit marks & credit stress
- Growth assumptions
- Cost saves assumptions & timing

## Current Environment Key Assumptions

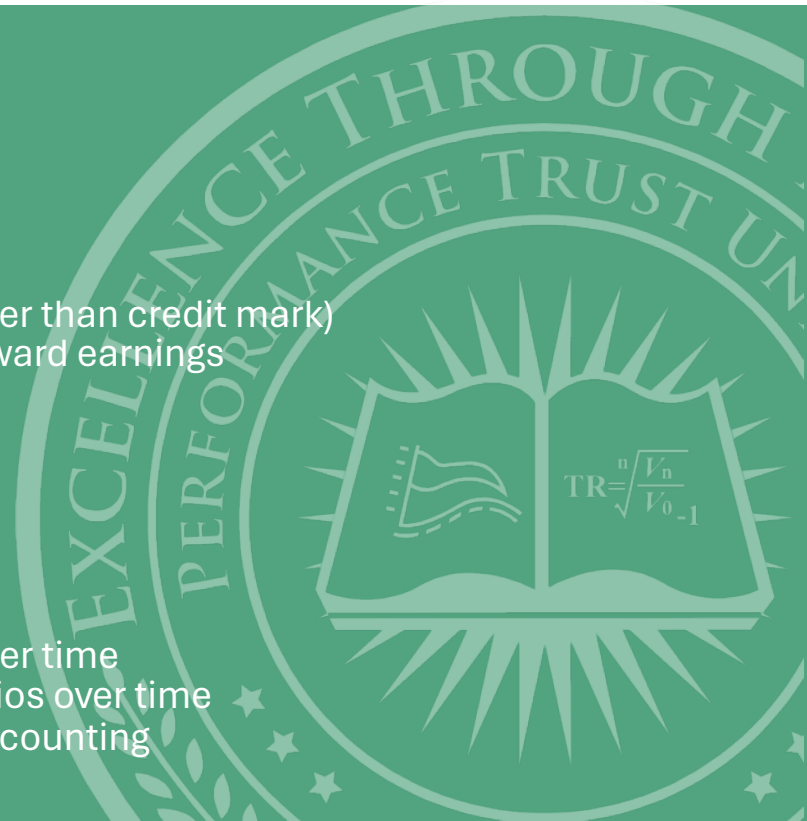
- Cash flow analysis of low-interest-rate borrowers
- INTEREST RATE MARK on loan portfolio (may be higher than credit mark)
- COST OF FUNDS assumptions in forecasting go-forward earnings

## Stress (Multi-Result) Analysis

- Credit mark (standard)
- Cost saves (standard)
- Cost of funds (new)

## Multi-interest-rate Scenario Analysis

- Your risk-reward profile in different rate scenarios over time
- The target risk-reward profile in different rate scenarios over time
- Your combined risk-reward profile after purchase accounting





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# Generic M&A Assumptions

# M&A Credit Mark Sensitivity

Illustrative table based on a real transaction

## TBV DILUTION AT CLOSE

Deal Value (\$000s)	Price / TBV (%)	Gross Loan Credit Mark, Pre-Tax (% / \$000s)						
		0.75%	1.00%	1.25%	1.50%	1.75%	2.00%	2.25%
\$60,000	174%	\$3,708	\$4,944	\$6,180	\$7,416	\$8,652	\$9,888	\$11,124
\$58,000	167%							
\$56,000	160%							
\$54,000	153%							
\$52,000	145%							
\$50,000	138%				(15.2%)			
\$48,000	131%							
\$46,000	124%							
\$44,000	117%							
\$42,000	109%							
\$40,000	102%							

## TBV EARNBACK

Deal Value (\$000s)	Price / TBV (%)	Gross Loan Credit Mark, Pre-Tax (% / \$000s)						
		0.75%	1.00%	1.25%	1.50%	1.75%	2.00%	2.25%
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\$58,000	167%							
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\$52,000	145%							
\$50,000	138%						2.8 yrs	
\$48,000	131%							
\$46,000	124%							
\$44,000	117%							
\$42,000	109%							
\$40,000	102%							

Source: Performance Trust Investment Banking

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# M&A Cost Savings Sensitivity

Illustrative table based on a real transaction

## 2026 EPS ACCRETION (DILUTION)

Deal Value (\$000s)	Price / TBV (%)	Cost Savings, Pre-Tax (% / \$000s)						
		10.0%	12.5%	15.0%	17.5%	20.0%	22.5%	25.0%
\$60,000	174%	\$1,958	\$2,322	\$2,786	\$3,251	\$3,715	\$4,180	\$4,644
\$58,000	167%							
\$56,000	160%							
\$54,000	153%							
\$52,000	145%							
\$50,000	138%				36.1%			
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# M&A Assumptions for *Today's* Environment

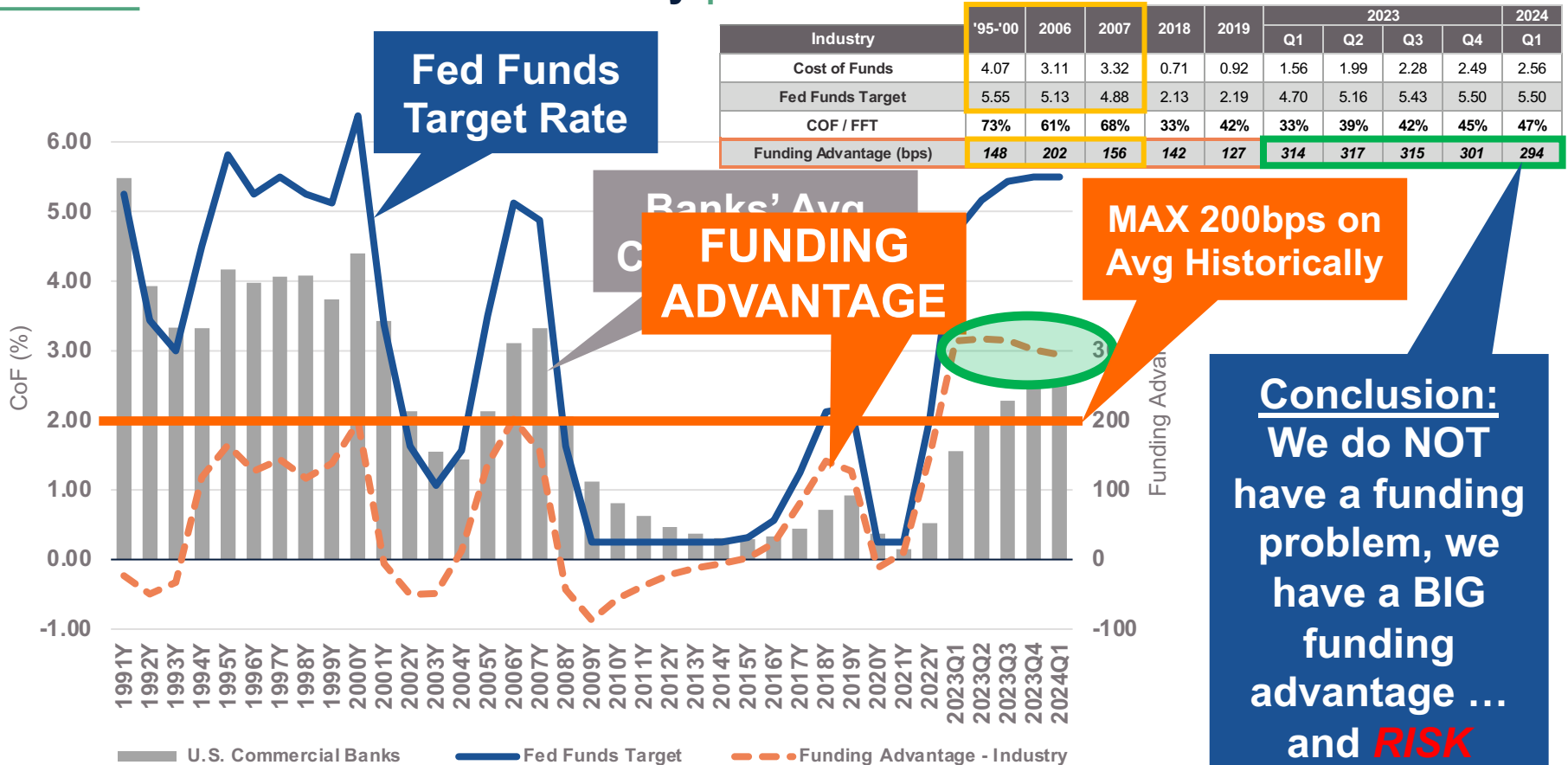


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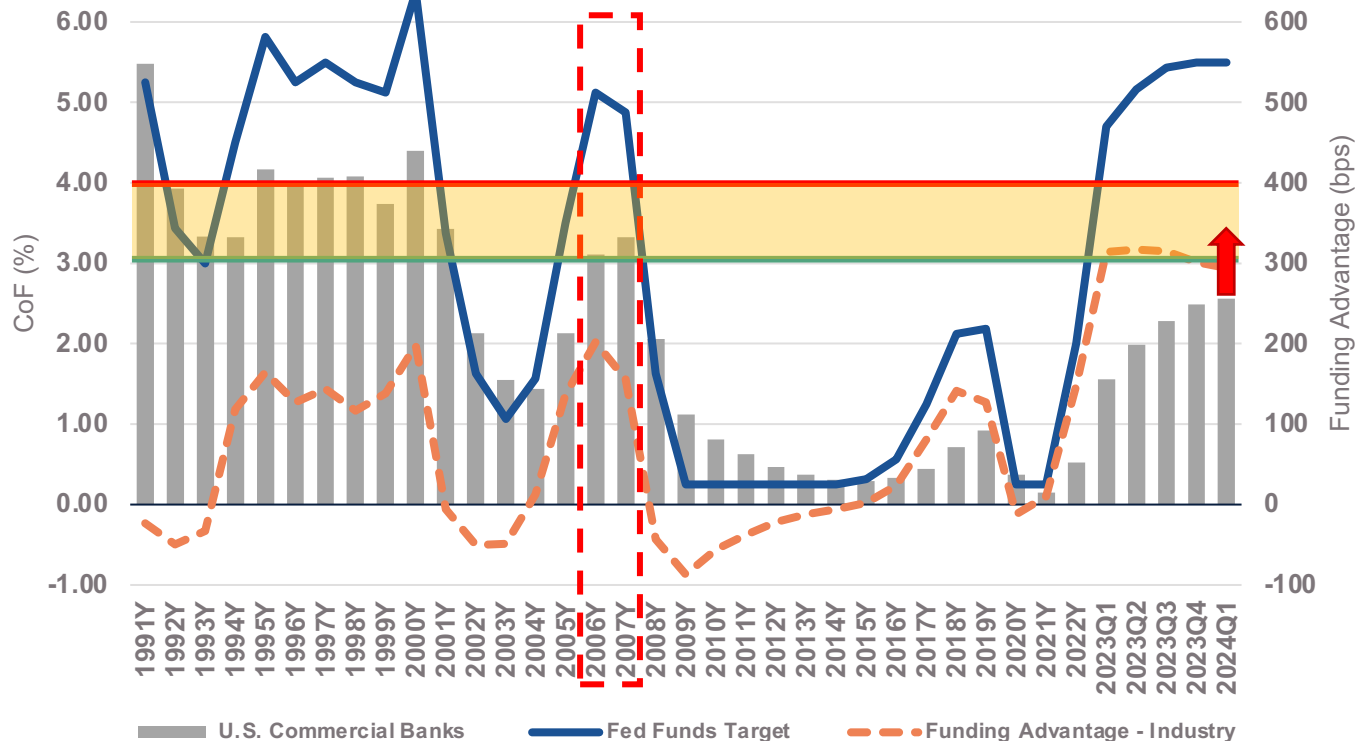
The Industry *Problem*....??

**Cost of Funds**

# Cost of Funds for the Industry | **FUNDING ADVANTAGE**



# Historical COF & Funding Advantage | Last Time FF @ 5%



**2007Q2, U.S. Banks (Fed Funds @ 5.25%)**

Percentile Rank	Cost of Funds (%)	Funding Advantage
10%	2.30	295
20%	2.70	255
25%	2.83	242
30%	2.94	231
40%	3.12	213
50%	3.29	196
60%	3.44	181
70%	3.63	162
75%	3.73	152
80%	3.83	142
90%	4.16	109

**THESIS / BIAS:**  
We believe cost of funds will  
**continue to rise,**  
even in rates unchanged  
AND rates down moderate

*(We believe rates **UP** will be a **DISASTER** for the industry)*

# Cost of Funds Impact on M&A

*Illustrative table based on a example transaction*

Target's Cost of Funds (%):	1.75	
TBV Earnbank (Years):		
2025E EPS Accretion (Dilution) (%):		
2026E EPS Accretion (Dilution) (%):		

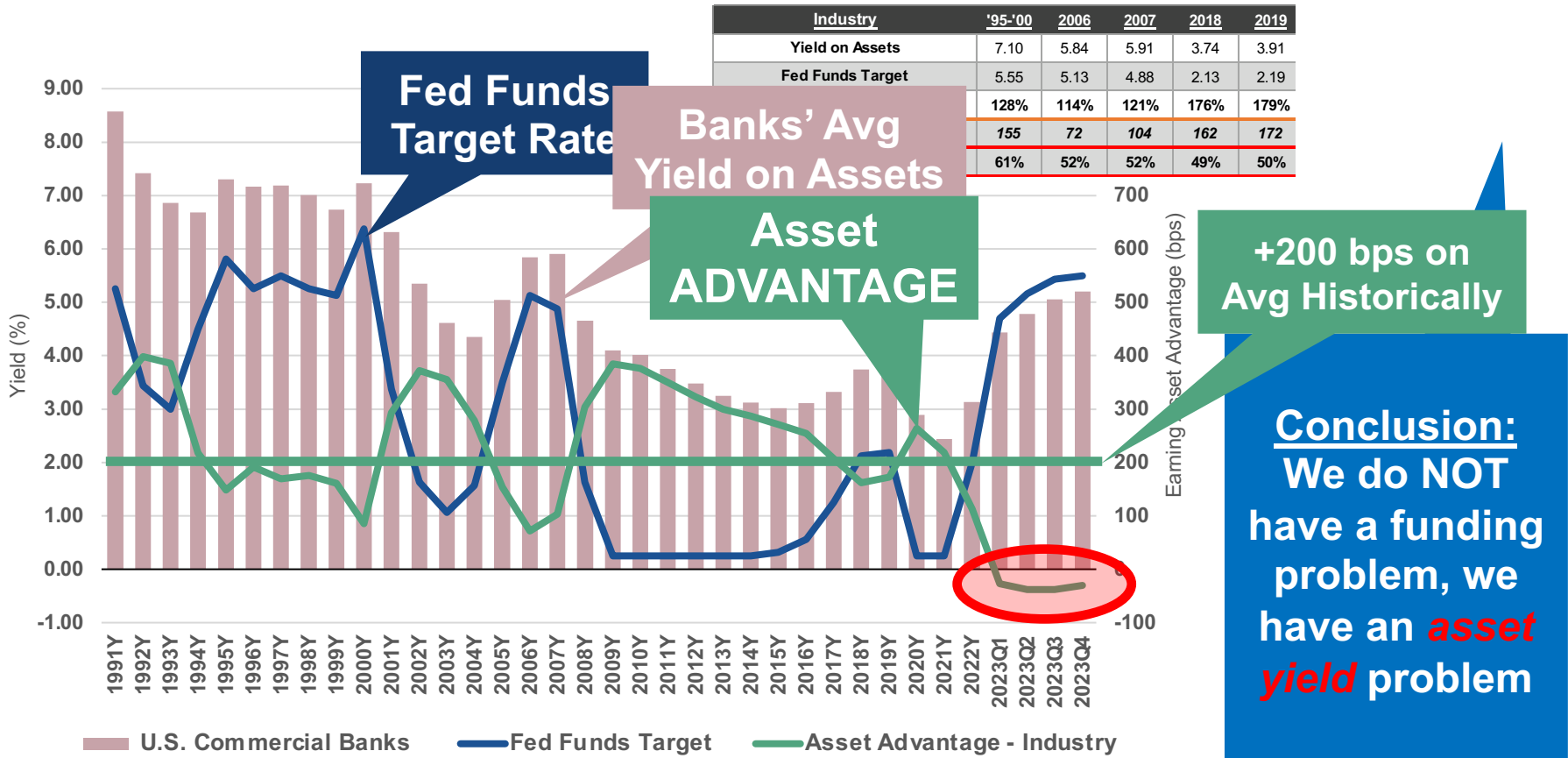




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# The Industry *REAL* Problem **Asset Yields & Duration**

# Yield on Assets for the Industry | *Asset ADVANTAGE*





What *interest rate* do  
you use to mark the  
loan portfolio to  
market?



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# What if *(When)* Rates Change?

**A Better Way**  
**...to M&A**

# First: Standalone Enterprise Shape to Determine Baseline

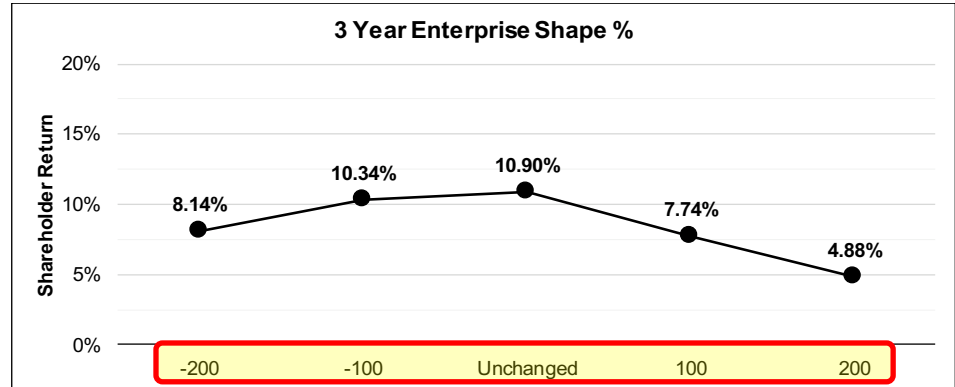
## EXAMPLE

1 Start with the Value of YOUR Equity Today

2 COUNT Growth of Tangible Book Value & Dividends over TIME

3 ARRIVE at a Horizon Value of Equity

1+ Shareholder Value  
2+ Created Over Multiple  
3 = Scenarios

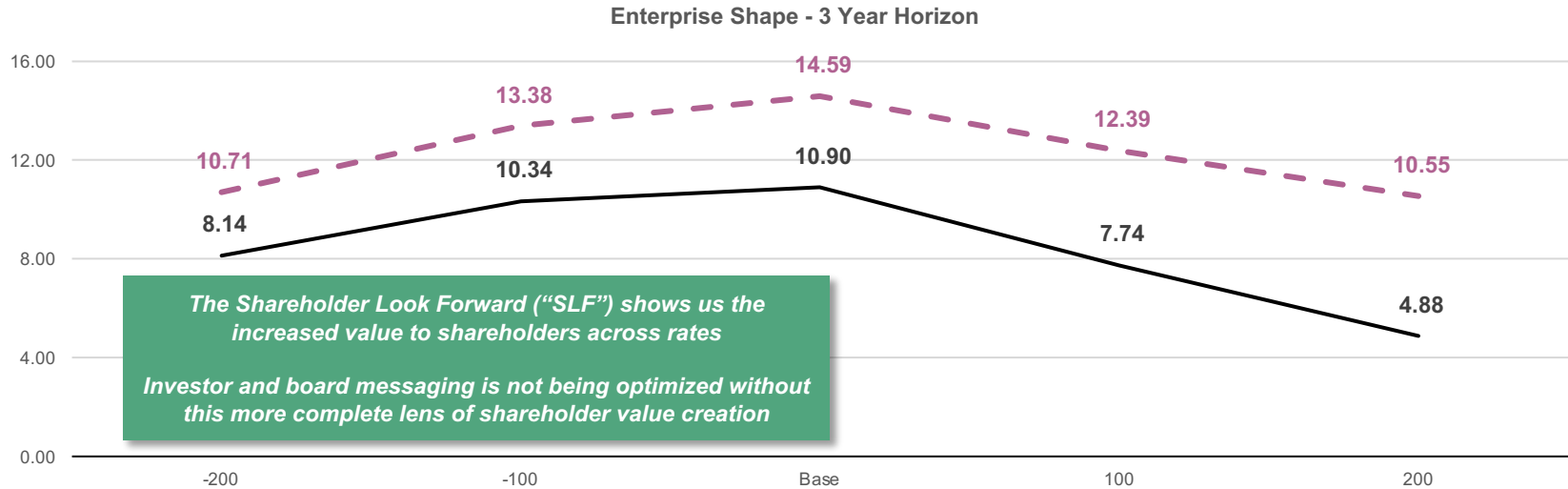


Walk	-200	-100	Unchanged	+100	+200
<b>A</b>	<b>Beginning Tangible Book</b>	\$ 153,859	\$ 153,859	\$ 153,859	\$ 153,859
<b>B</b>	<b>Beginning Valuation</b>	\$ 184,631	\$ 184,631	\$ 184,631	\$ 184,631
<b>C</b>	<b>Common Dividends</b>	\$ 19,413	\$ 19,413	\$ 19,413	\$ 19,413
<b>D</b>	<b>Retained Earnings</b>	\$ 40,577	\$ 38,236	\$ 34,964	\$ 29,329
<b>E</b>	<b>Change in AOCI</b>	\$ 13,370	\$ 9,289	\$ 4,868	\$ (1,941)
<b>F = A + D + E</b>	<b>Horizon Tangible Book</b>	\$ 207,806	\$ 201,384	\$ 193,691	\$ 181,247
<b>G</b>	<i>Price / TBV</i>	103%	114%	120%	117%
	<i>Horizon ROTCE</i>	8.57%	9.50%	10.09%	9.82%
<b>H = F x G</b>	<b>Horizon Valuation</b>	\$ 214,076	\$ 228,612	\$ 232,429	\$ 211,519
<b>J = (H - B) + C</b>	<b>Value Creation \$</b>	\$ 48,858	\$ 63,394	\$ 67,211	\$ 46,301
<b>Ann. Value Creation (J)</b>	<b>Annualized Shareholder Return</b>	8.14%	10.34%	10.90%	7.74%

Source: Performance Trust Investment Banking

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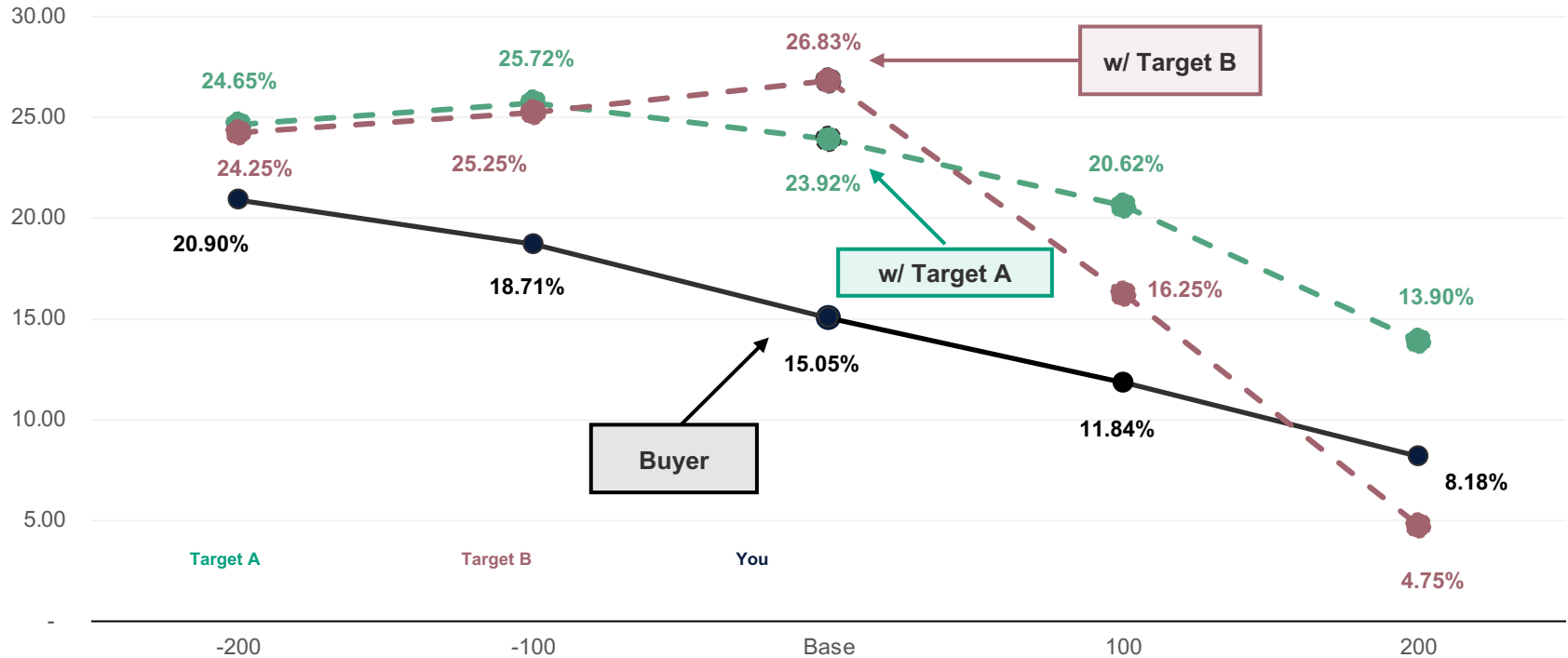
## Second: Factor in Impact on Enterprise After the Acquisition



	-200	-100	Base	100	200	Walk
Starting Value	\$ 184,631	\$ 184,631	\$ 184,631	\$ 184,631	\$ 184,631	A
Pro Forma Terminal Value	\$ 262,064	\$ 282,943	\$ 292,685	\$ 275,066	\$ 260,842	B
Pro Forma Change in Value	\$ 77,434	\$ 98,312	\$ 108,054	\$ 90,435	\$ 76,211	C = B - A
Deal Costs & Consideration	\$ (30,266)	\$ (32,524)	\$ (33,578)	\$ (31,672)	\$ (30,134)	D
Pro Forma Dividends	\$ 18,713	\$ 18,713	\$ 18,713	\$ 18,713	\$ 18,713	E
Pro Forma Shareholder Value Creation	\$ 65,881	\$ 84,501	\$ 93,189	\$ 77,476	\$ 64,790	F = C + D + E
Pro Forma Annualized Shareholder Return %	10.71	13.38	14.59	12.39	10.55	Ann. Value Creation (F)

# Application Example, Comparing Two Merger Partners

## Standalone and Pro Forma Enterprise Shapes (3 Year Annualized)



# Multi-Interest Rate Scenario Summary Analysis

	INTEREST RATE SCENARIO				
	-200	-100	UNCH	+100	+200
<b>Merger Impacts</b>					
2025 EPS Accretion (Dilution)	14.7%	25.9%	35.4%	44.4%	54.5%
2026 EPS Accretion (Dilution)	17.0%	27.2%	35.4%	42.1%	49.6%
Initial TBV Accretion (Dilution) @ Close	(6.6%)	(11.7%)	(17.3%)	(23.8%)	(31.0%)
TBV Earnback (TBVPS Crossover)	3.1 yrs	3.5 yrs	3.8 yrs	5.1 yrs	11.1 yrs
Fully-diluted Pro Forma Ownership	100.0%	100.0%	100.0%	100.0%	100.0%
<b>Pro Forma Balance Sheet</b>					
Total Assets (\$mm)	\$1,419	\$1,415	\$1,411	\$1,406	\$1,401
Cash & Securities (\$mm)	\$76	\$77	\$105	\$80	\$81
Total Gross Loans (\$mm)	\$1,069	\$1,064	\$1,060	\$1,055	\$1,050
Total Deposits (\$mm)	\$1,204	\$1,204	\$1,204	\$1,204	\$1,204
Tangible Common Equity (\$mm)	\$109.0	\$99.8	\$90.0	\$79.0	\$68.0
<b>Pro Forma Income Statement</b>					
2025 ROAA	0.84%	0.95%	1.06%	1.10%	1.14%
2025 ROATCE	10.59%	12.92%	15.61%	18.07%	21.26%
2025 Efficiency Ratio	69.7%	69.2%	68.9%	70.1%	71.3%
2026 ROAA	0.93%	1.04%	1.15%	1.19%	1.24%
2026 ROATCE	10.99%	13.03%	15.20%	17.13%	19.51%
2026 Efficiency Ratio	68.0%	67.4%	67.0%	68.0%	68.9%
<b>Pro Forma Regulatory Capital</b>					
Consolidated: TCE/TA @ Close	7.71%	7.11%	6.46%	5.71%	4.96%
Bank: Tier 1 Leverage Ratio @ Close	9.52%	9.15%	8.69%	8.35%	7.94%
Bank: Tier 1 Risk-based Ratio @ Close	11.41%	10.97%	10.52%	10.03%	9.54%
Bank: Total Risk-based Ratio @ Close	12.66%	12.22%	11.77%	11.28%	10.79%

# Important Questions to Ask

## Generic M&A Assumptions

- What are the credit marks & credit stress assumptions?
- What are your growth assumptions for the target?
- What are the cost saves assumptions & timing?

## Current Environment Key Assumptions

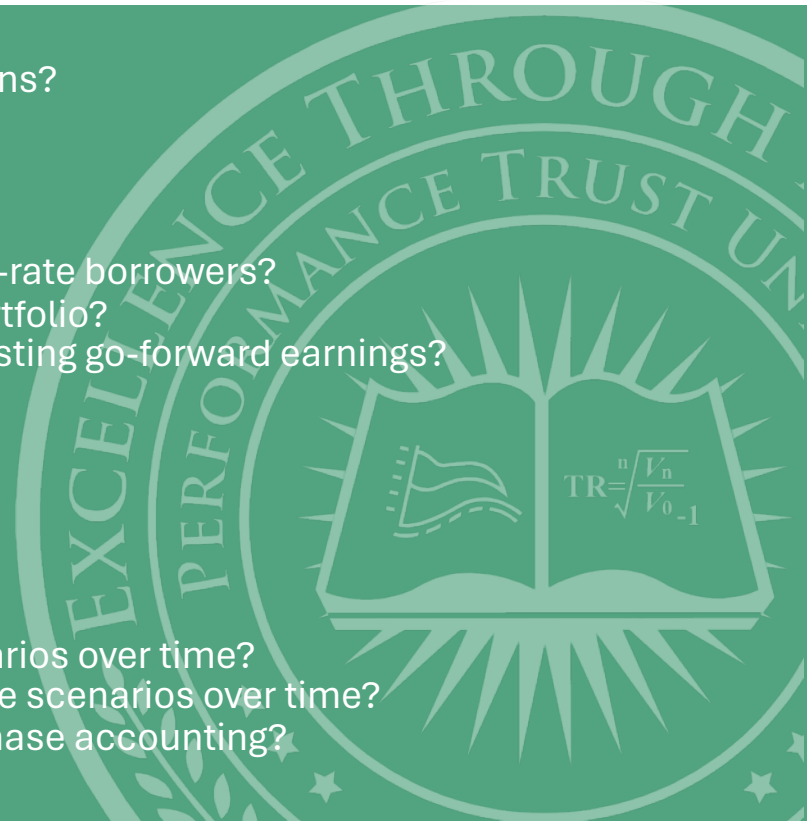
- Do we have cash flow risk upon reset of low-interest-rate borrowers?
- What interest rate(s) did we use to mark the loan portfolio?
- What cost of funds assumption did we use in forecasting go-forward earnings?

## Stress (Multi-Result) Analysis

- Credit mark (standard)
- Cost saves (standard)
- Cost of funds (new)

## Multi-interest-rate Scenario Analysis

- What is our risk-reward profile in different rate scenarios over time?
- What is the targets risk-reward profile in different rate scenarios over time?
- What is our combined risk-reward profile after purchase accounting?





**Q & A**



# Would you like a copy of the presentation?

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