

BankDirector

Really, What Is Franchise Value?

Fred Cannon



A Stifel Company

INTERNET PASSCODE:
growth15

ON DEMAND PASSCODE:
innovate

TWITTER HASHTAG:
#BDGrow15



A Stifel Company

KEEFE, BRUYETTE & WOODS
Specialists in Financial Services

North American Equity Research



Frederick Cannon, CFA
Executive Vice President,
Director of Research
(212) 887-3887
fcannon@kbw.com

**Bank Director
Growth & Innovation Conference**
April 28, 2015

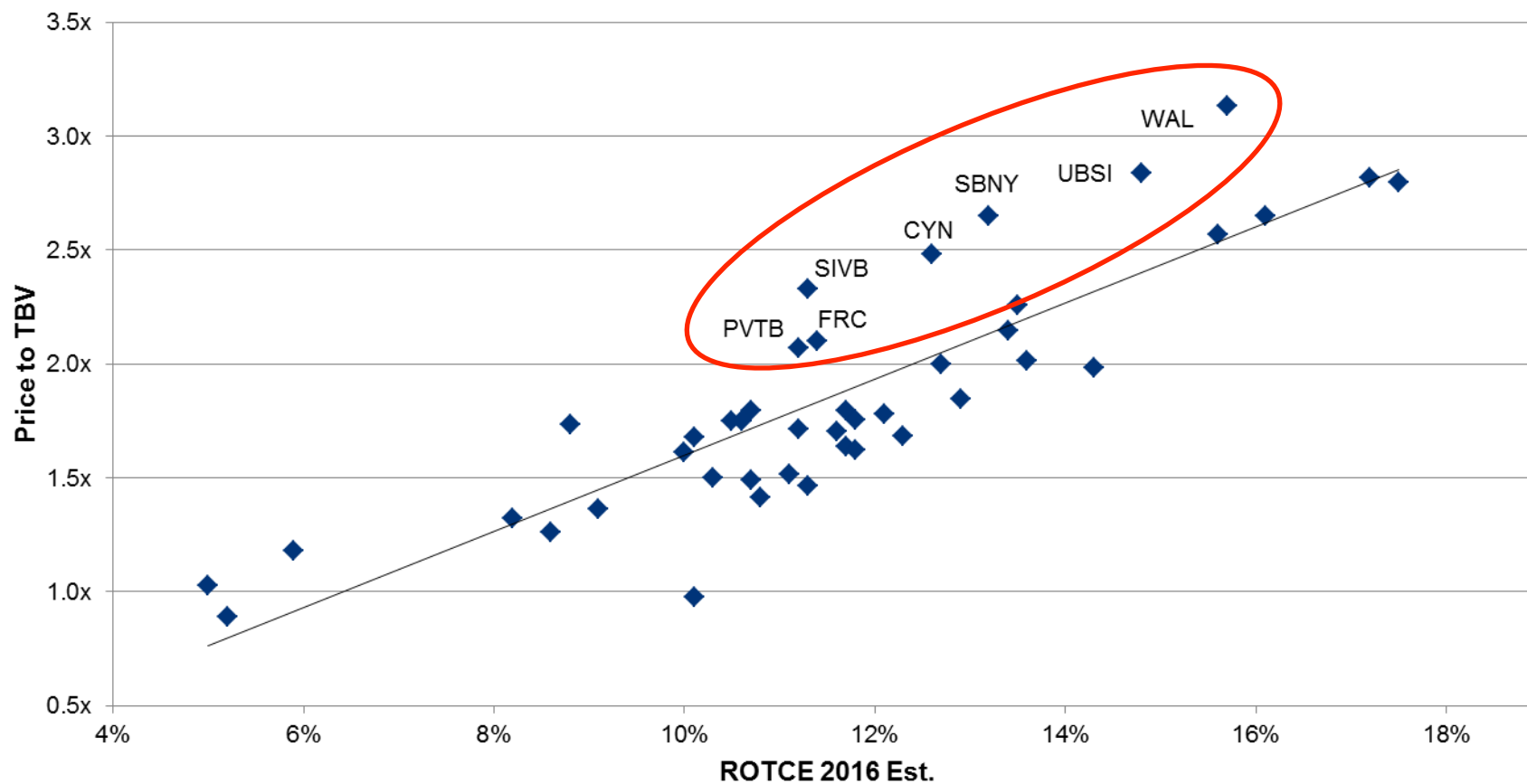
Really, What is Franchise Value?

Keefe, Bruyette & Woods, Inc. does and seeks to do business with companies covered in its research reports. As a result, investors should be aware that the firm may have a conflict of interest that could affect the objectivity of this report. Investors should consider this report as only a single factor in making their investment decision. **Please refer to important disclosures and analyst certification information on pages 18-21 of this report.**

Franchise Value = (ROE – Cost of Equity) × Market Premium

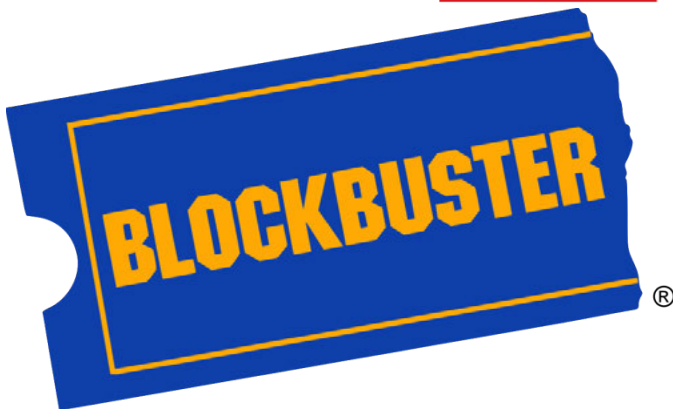
Franchise Value Creates Shareholder Value

Franchise Value Is Evident in the Market



Note: Banks with between \$10 billion and \$50 billion in assets as of 4/13/2015. Pricing data as of 04/13/2015.
Source: FactSet, and KBW Research.

A Logo Does Not Create Franchise Value, but a Brand Does



Brand Value and Franchise Value Are Not Always Stable Over Time

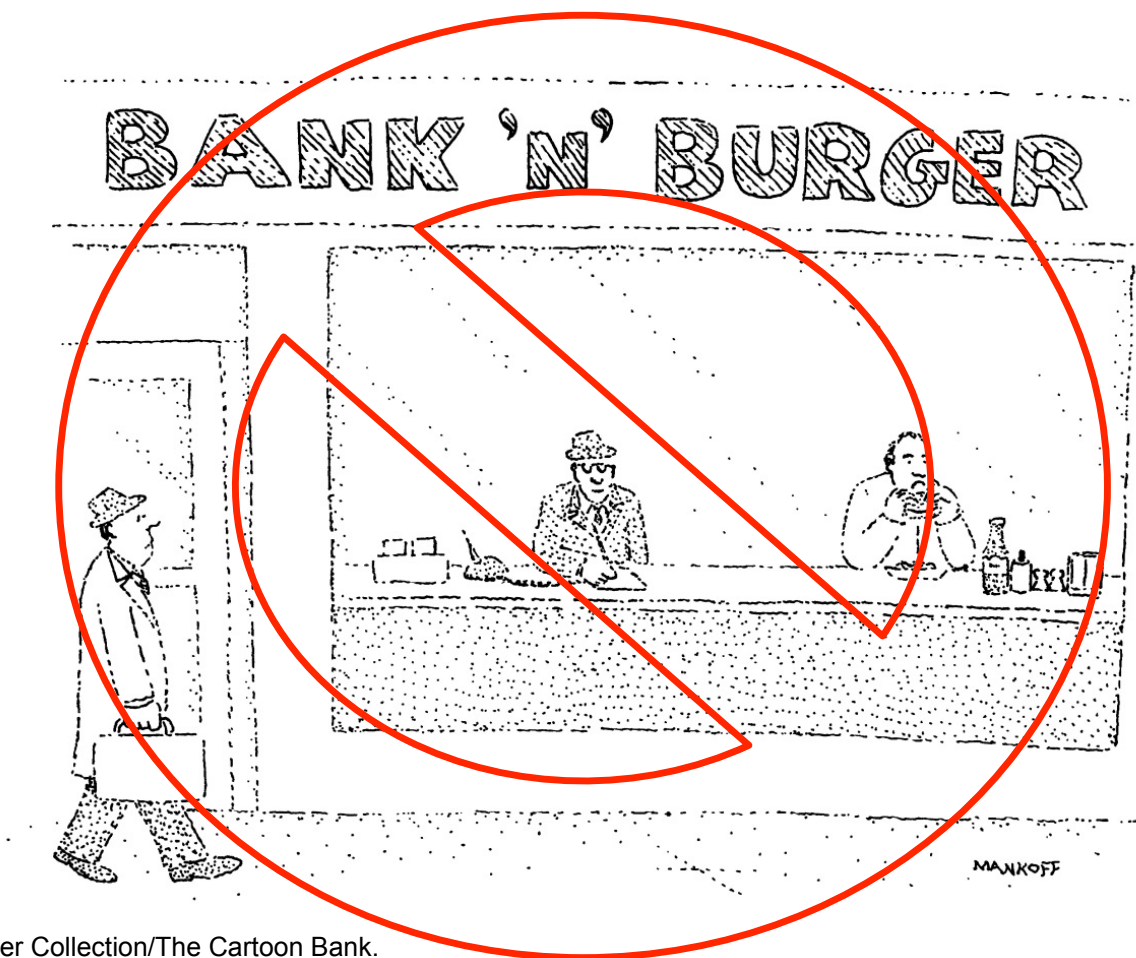
Building Franchise Value

It is contextual

- Industry
- Technology
- Clients

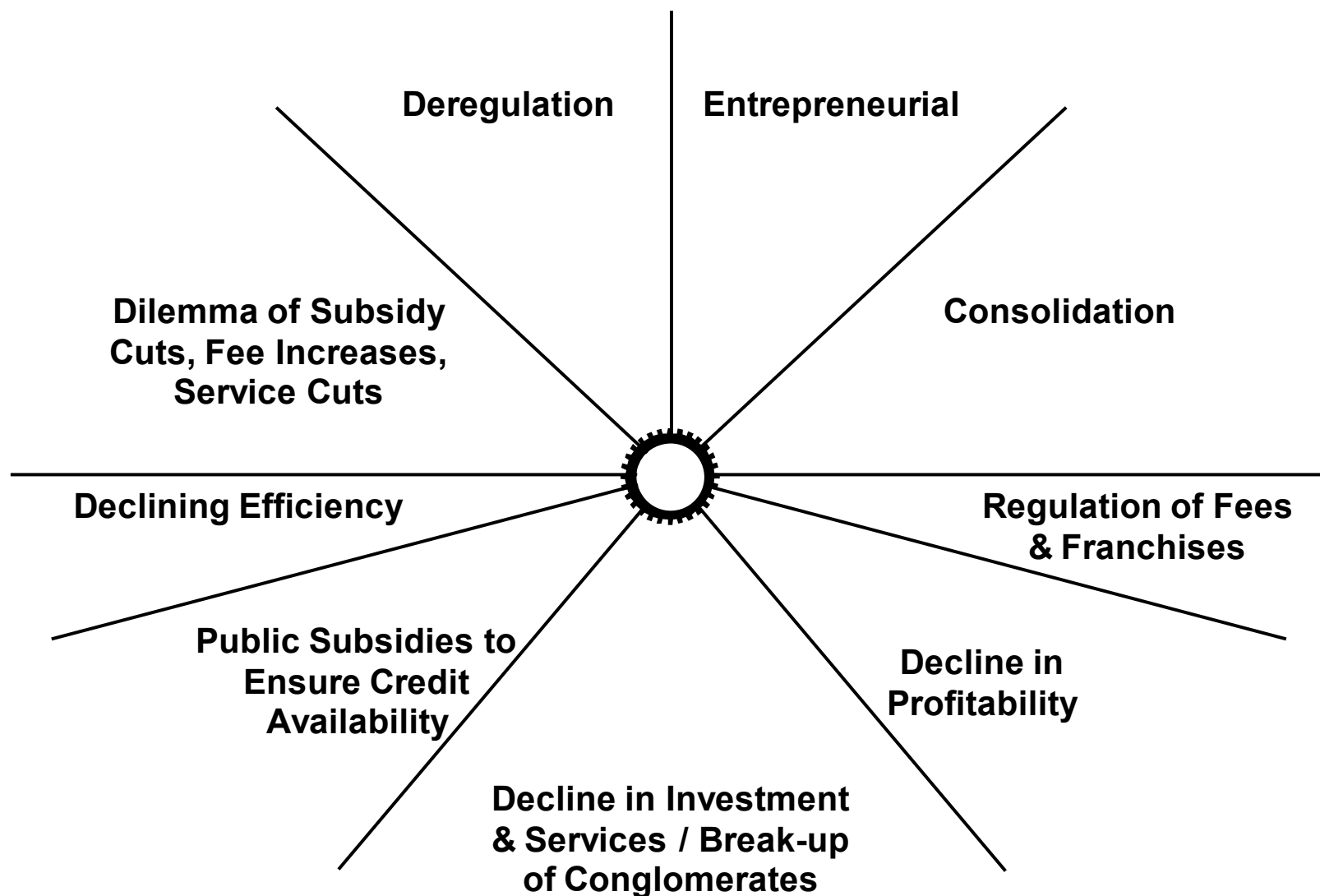
It takes focus

- “The universal banking model is dead” – Chairman of Barclays
- Small banks can’t be all things to all people



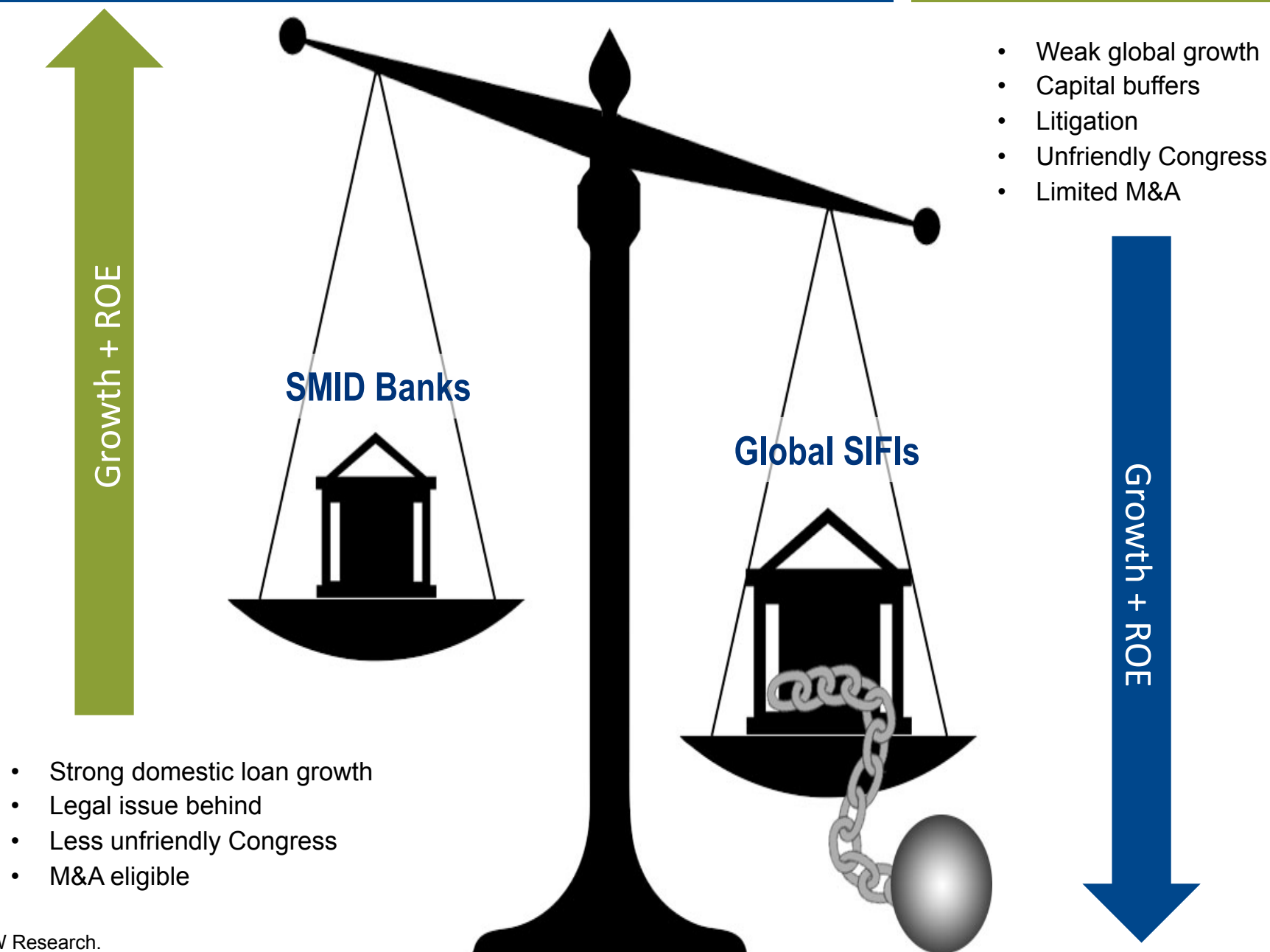
Source: Robert Mankoff/The New Yorker Collection/The Cartoon Bank.

We Are Moving to an Era of Concern About Credit Availability



Source: World Bank and KBW Research.

Big Isn't Beautiful in Banking



Source: KBW Research.

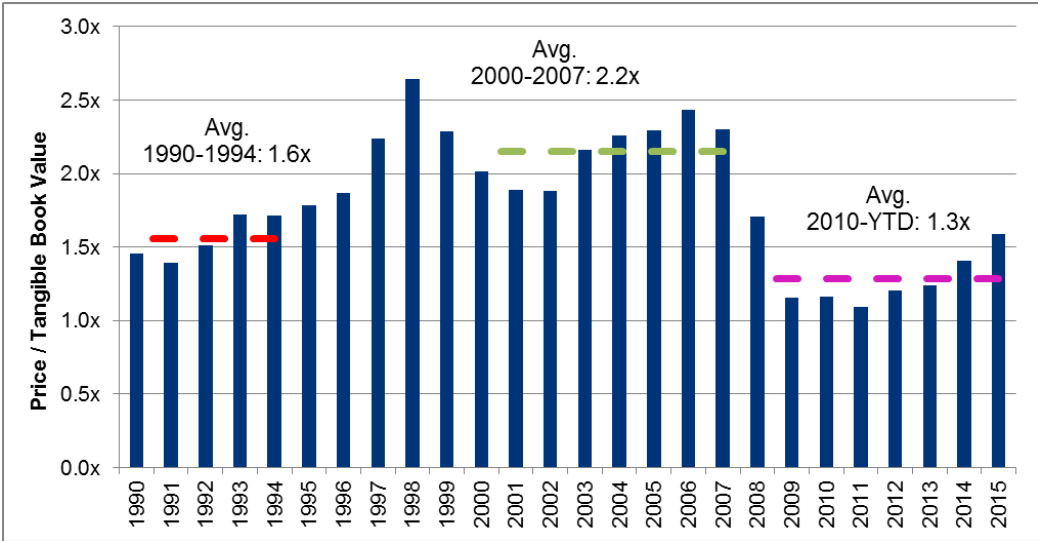
A Branch Is Not a Franchise

<u>INPUTS</u>	Branch Economics		
	2006 Rates and Fees	Current Rates and Fees	Normalized Rates/ Current Fees
Leasehold Improvements	\$1,000,000	\$1,000,000	\$1,000,000
Operating Costs Per Month	\$50,000	\$50,000	\$50,000
Average Total Deposits	\$50,000,000	\$50,000,000	\$50,000,000
Deposit Mix:			
Checking (non-interest bearing)	30%	30%	30%
Savings/Money Markets	40%	40%	40%
Time Deposits	30%	30%	30%
Deposit Fees/Checking Deposits	3.0%	1.5%	1.5%
Loan/Deposits	30%	30%	30%
1-year Treasury Rate	5.00%	0.50%	5.00%
Yield on Investments	5.50%	1.00%	5.50%
Yield on Loans	7.50%	3.50%	7.50%
<u>OUTPUTS</u>			
Net Interest Income	\$1,675,000	\$735,000	\$1,675,000
Non-Interest Income	\$450,000	\$225,000	\$225,000
Expenses	<u>\$800,000</u>	<u>\$800,000</u>	<u>\$800,000</u>
Net Pre-Tax Pre-Provision Income	\$1,325,000	\$160,000	\$1,100,000
ROA*	1.67%	0.16%	1.38%

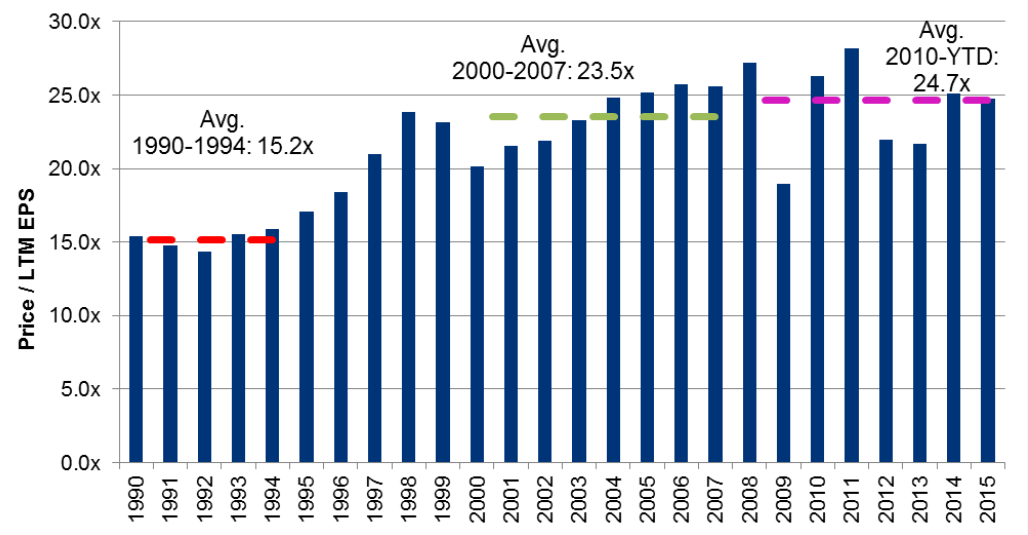
*Assumes 25 bps credit costs and 35% tax rate.
Source: FDIC and KBW Research.

Deposits Are Generating Less Value/Earnings Are Maintaining Values

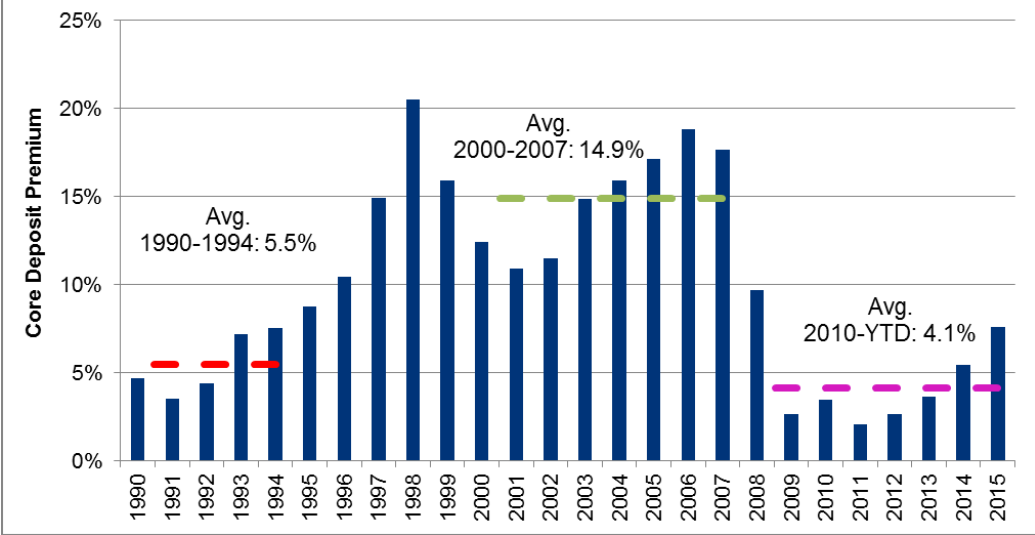
Median Takeout Price/TBV



Median Takeout Price/LTM EPS



Median Takeout Core Deposit Premiums



Source: SNL Financial and KBW Research.

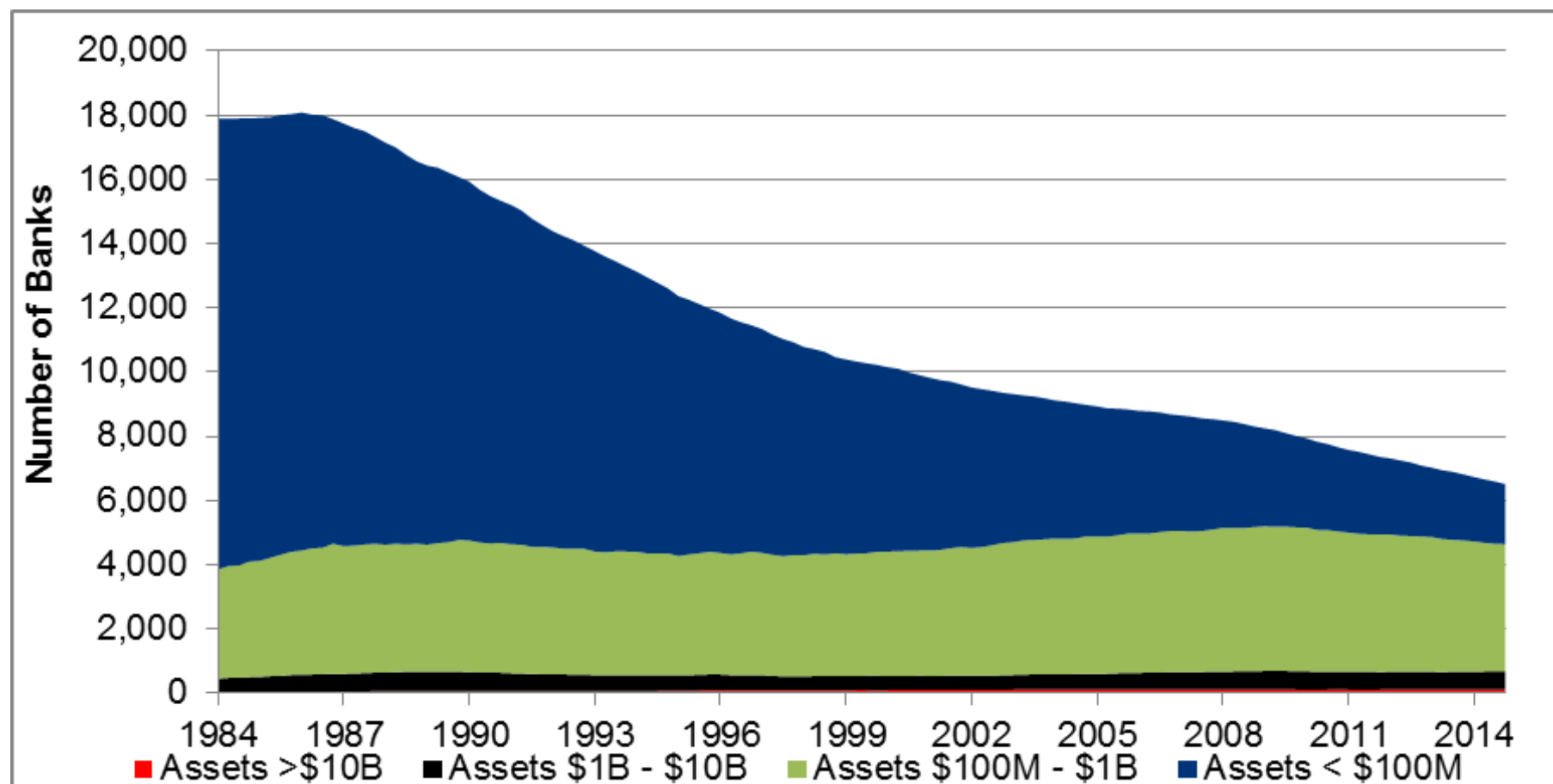
Non-Bank Banking Is Proliferating



"There's money in there that could be used for other purposes."

Source: Frank Cotham/The New Yorker Collection/The Cartoon Bank.

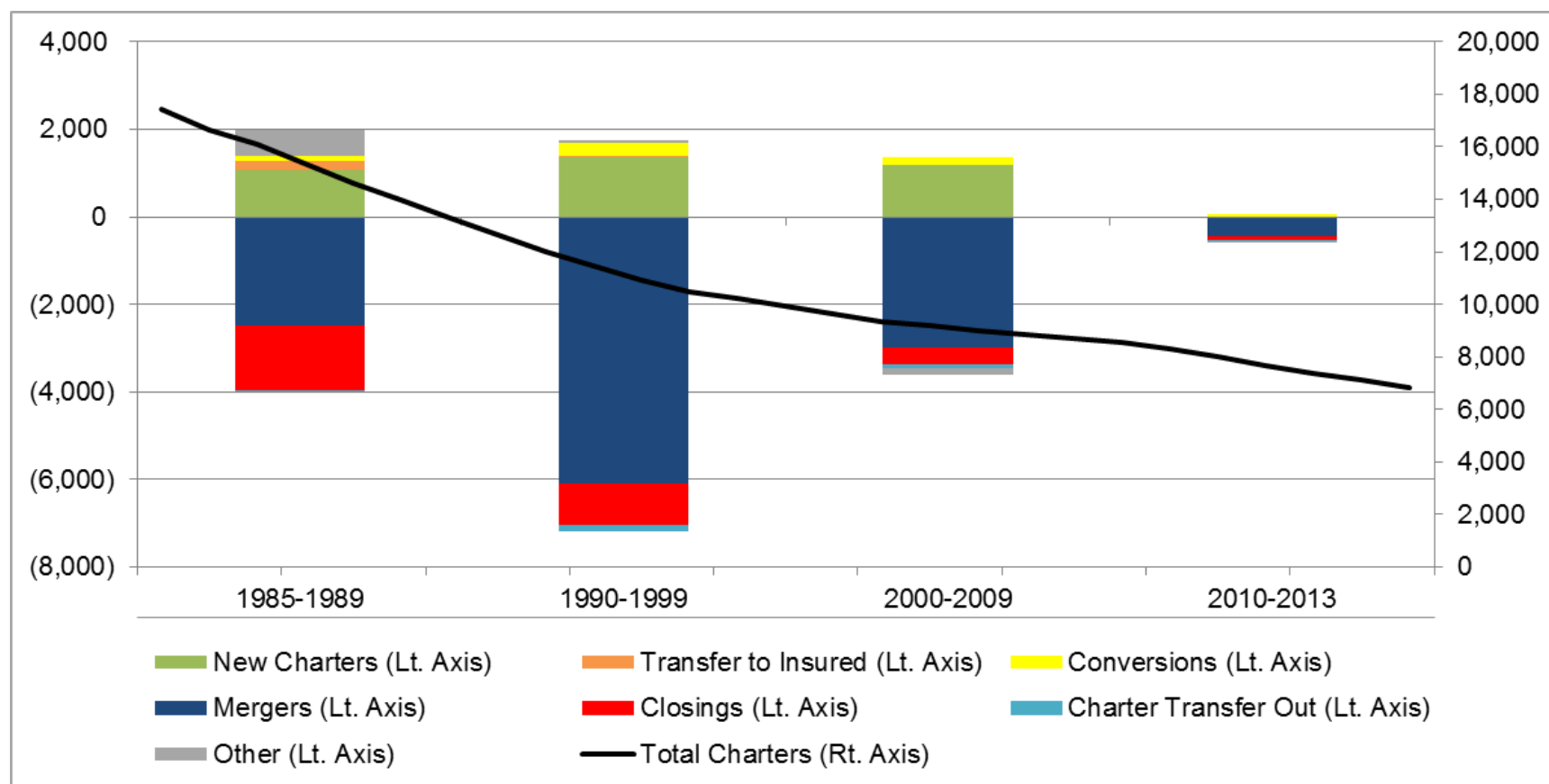
The Decreasing Number of Banks Is Creating Scarcity Value



Note: Data for all FDIC-insured institutions.

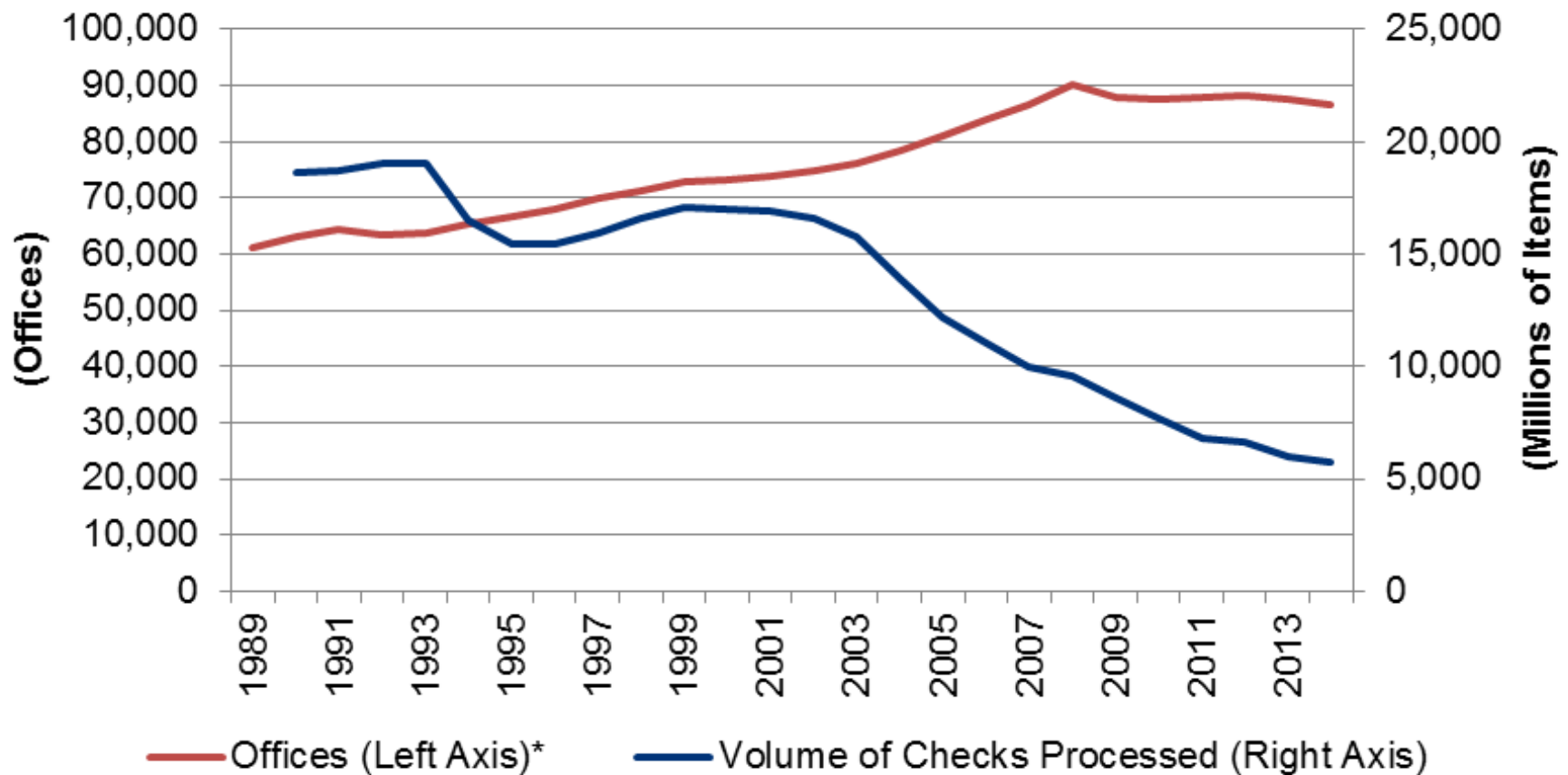
Source: Federal Deposit Insurance Corporation and KBW Research.

No New Banks Creates Opportunity



Source: Federal Deposit Insurance Corporation and KBW Research.

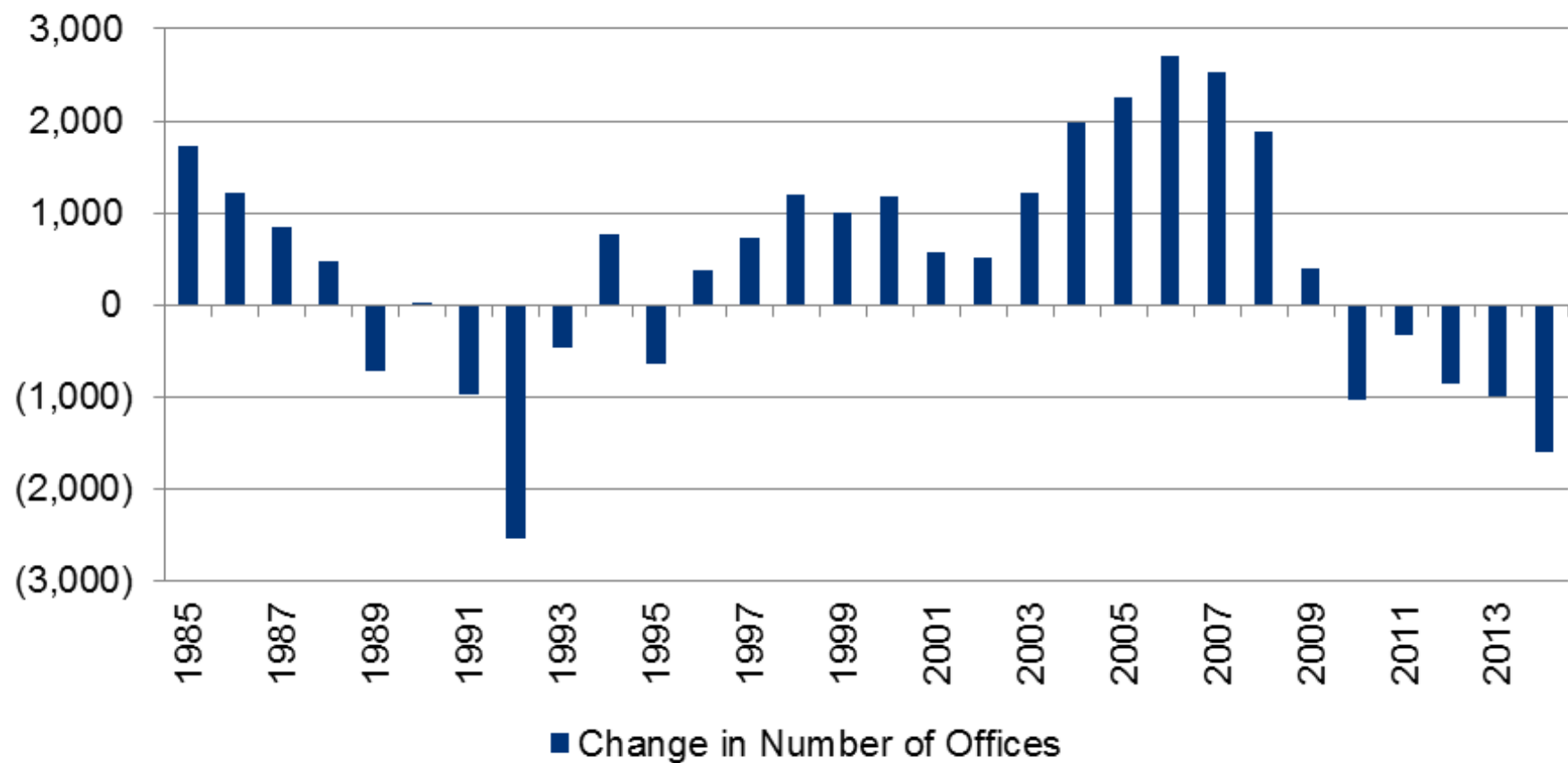
Technology Is Driving Bank Identity



*Offices measures total offices at FDIC insured commercial banks.

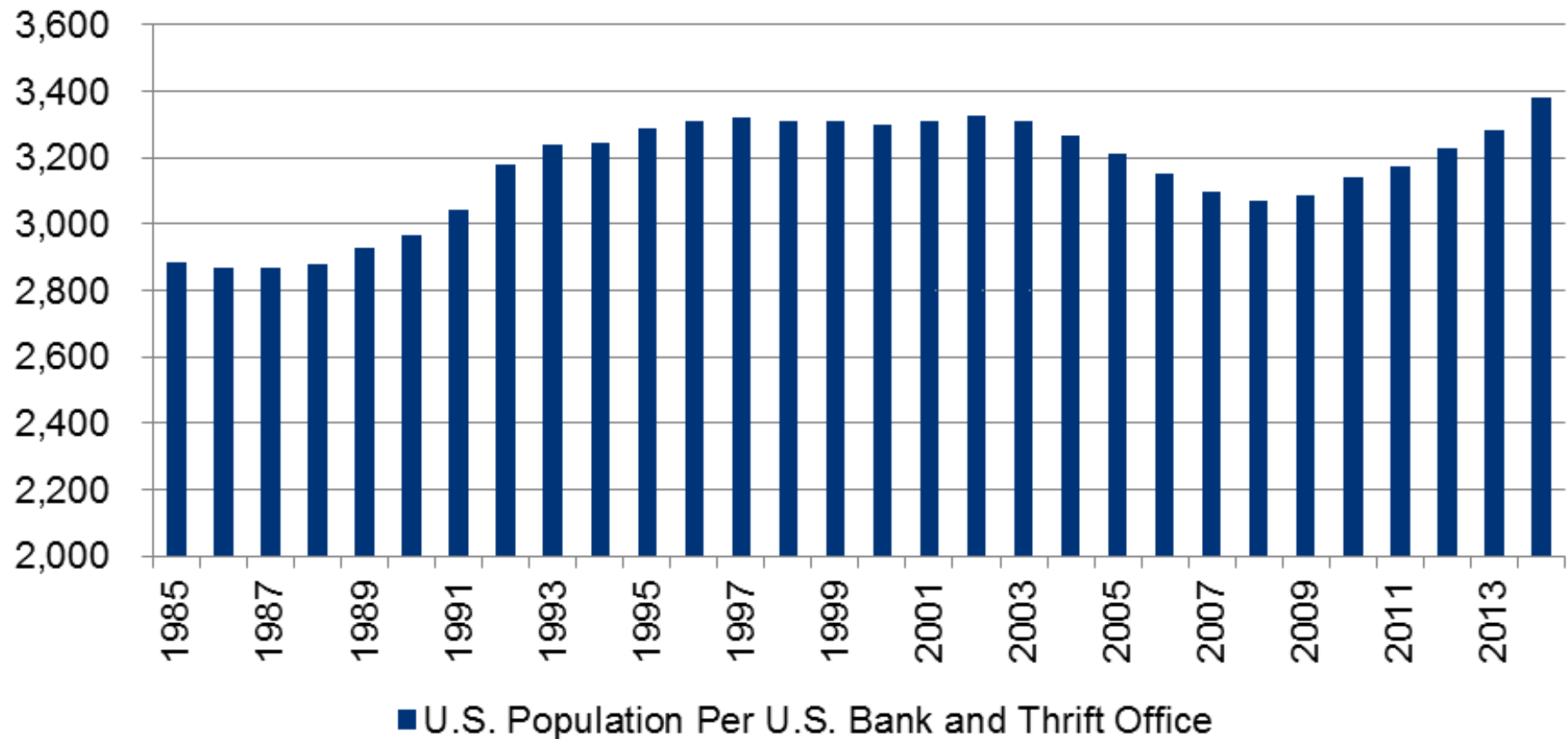
Source: Federal Deposit Insurance Corporation, Federal Reserve Board of Governors, and KBW Research.

Branches May Be in Permanent Decline



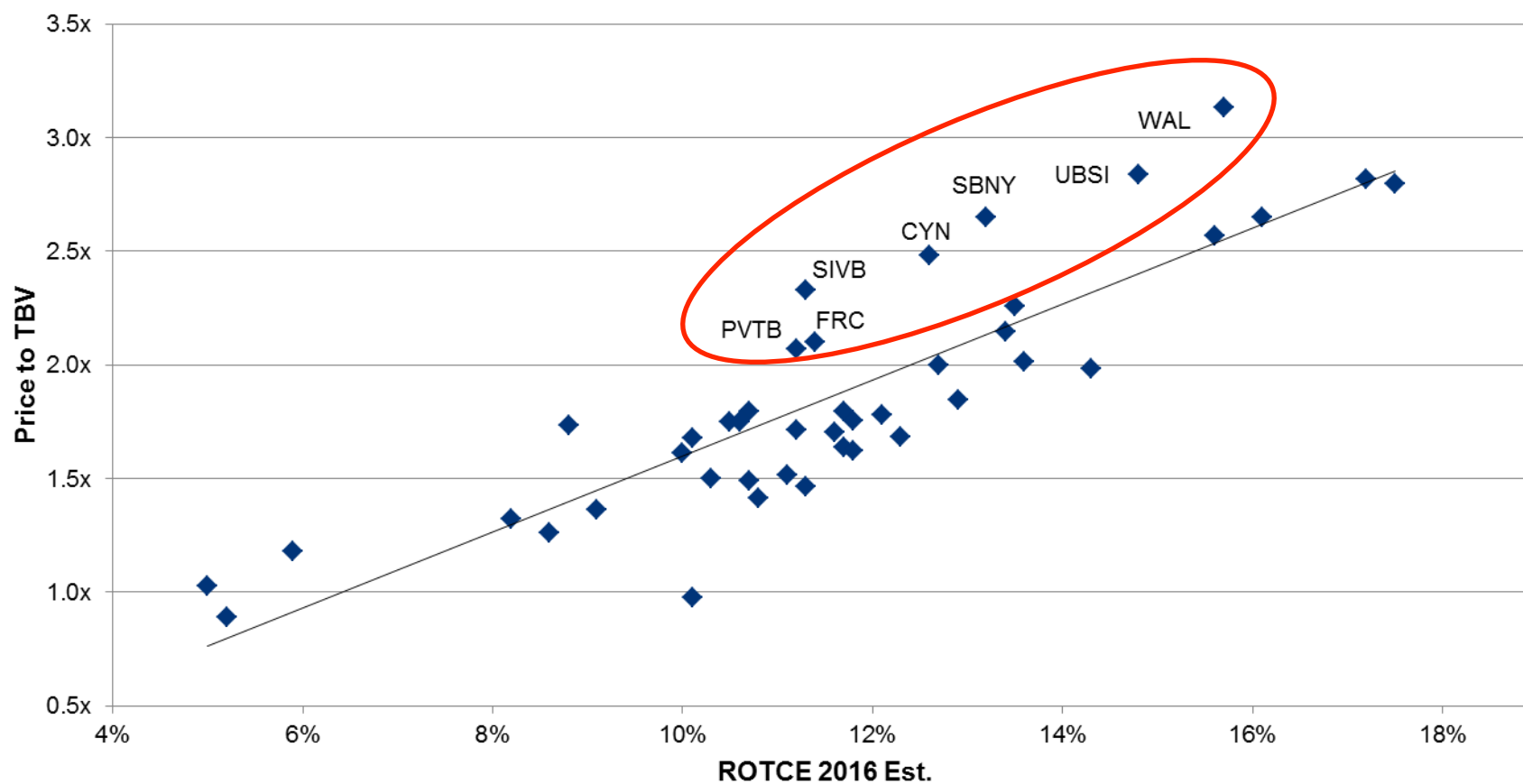
Note: Data for all FDIC insured banks and savings institutions. Data as of December 31 for 1985-1994 and June 30 for each year from 1995 on.
Source: Federal Deposit Insurance Corporation and KBW Research.

Technology Should Drive More Clients Per Branch



Note: Data for all FDIC insured banks and savings institutions. Data as of December 31 for 1985-1994 , June 30 for each year for 1995-2013, and December 1 for 2014.
Source: Federal Deposit Insurance Corporation, U.S. Census Bureau, and KBW Research.

Franchise Value Creates Economic Value



Note: Banks with between \$10 billion and \$50 billion in assets as of 4/13/2015. Pricing data as of 04/13/2015.
Source: FactSet, and KBW Research.

Companies Mentioned

Company Name	Ticker	Closing Price	Analyst	Rating
		04/15/2015		
City National Corp	CYN	93.09	Brian Klock	Market Perform
First Republic Bank	FRC	57.29	Julianna Balicka	Market Perform
PrivateBancorp, Inc.	PVTB	37.06	Christopher McGratty	Outperform
Signature Bank	SBNY	131.25	Christopher McGratty	Outperform
SVB Financial Group	SVB	129.56	Julianna Balicka	Outperform
United Bankshares Inc	UBSI	37.59	Catherine Mealor	Market Perform
Western Alliance Bancorp	WAL	30.14	Brian Klock	Outperform

Source: FactSet and KBW Research.

Important Disclosures

RESEARCH ANALYST CERTIFICATION

I, Frederick Cannon, CFA, hereby certify that the views expressed in this research report accurately reflect my personal views about the subject companies and their securities. I also certify that I have not been, and will not be receiving direct or indirect compensation in exchange for expressing the specific recommendation in this report.

Analysts' Compensation: The equity research analysts responsible for the preparation of this report receive compensation based upon various factors, including the quality and accuracy of research, client feedback, competitive factors, and overall firm revenues, which include revenues from, among other business units, Institutional Equities and Investment Banking.

COMPANY SPECIFIC DISCLOSURES

For disclosures pertaining to recommendations or estimates made on a security mentioned in this report, please see the most recently published company report or visit our global disclosures page on our website at <http://www.kbw.com/research/disclosures> or see the section below titled "Disclosure Information" for further information on how to obtain these disclosures.

AFFILIATE DISCLOSURES

This report has been prepared by Keefe, Bruyette & Woods, Inc. ("KBWI") and/or its affiliate Stifel Nicolaus Europe Limited ("SNEL"), also trading as Keefe, Bruyette & Woods Europe ("KBW Europe"); collectively "KBW". Both KBWI and KBW Europe are affiliates of Stifel, Nicolaus & Company, Inc. KBWI is regulated by FINRA and the United States Securities and Exchange Commission, is a member of NYSE, and its headquarters is located at 787 7th Avenue, New York, NY 10019. Stifel Nicolaus Europe Limited, also trading as Keefe, Bruyette & Woods Europe, is registered in England and Wales, no. 03719559 and its registered office is 7th Floor, One Broadgate, London EC2M 2QS. Stifel Nicolaus Europe Limited, also trading as Keefe, Bruyette & Woods Europe, is authorised and regulated by the Financial Conduct Authority (FCA) in the UK entered on the FCA's register, no. 190412 and is a member of the London Stock Exchange. Disclosures in the Important Disclosures section referencing KBW include one or all affiliated entities unless otherwise specified.

Registration of non-U.S. Analysts: Any non-U.S. Research Analyst employed by a non-U.S. affiliate of KBWI contributing to this report is not registered/qualified as research analyst with FINRA and/or the NYSE and may not be an associated person of KBWI and therefore may not be subject to NASD Rule 2711 or NYSE Rule 472 restrictions on communications with a subject company, public appearances, and trading securities held by a research analyst account.

Disclosure Information: For current company-specific disclosures, please write to one of the KBW entities: For **U.S. Research:** Keefe, Bruyette & Woods, Inc. Research Department, 787 7th Avenue, 4th Floor, New York, NY 10019. For **European Research:** The Compliance Officer, Keefe, Bruyette and Woods Europe, 7th Floor, One Broadgate, London EC2m 2QS. Or visit our website at <http://www.kbw.com/research/disclosures>. KBW has arrangements in place to manage conflicts of interest including information barriers between the Research Department and certain other business groups. As a result, KBW does not disclose certain client relationships with, or compensation received from, such companies in its research reports.

Important Disclosures (Continued)

KBW Distribution of Ratings / IB Services:

*IB Serv./Past 12 Mos.				
Rating	Count	Percent	Count	Percent
Outperform [BUY]	222	36.27	81	36.49
Market Perform [HOLD]	332	54.25	86	25.90
Underperform [SELL]	40	6.54	9	22.50
Restricted [RES]	0	0.00	0	0.00
Suspended [SP]	18	2.94	3	16.67
Covered -Not Rated [CNR]	3	0.49	1	33.33

As of April 14, 2015.

*KBW maintains separate research departments; however, the above chart, "Distribution of Ratings/IB Services," reflects combined information related to the distribution of research ratings and the receipt of investment banking fees globally. **Note: All ratings for Keefe, Bruyette and Woods, Inc. as of January 15, 2015, reflect a relative ratings system.

Explanation of Ratings: KBW Research Department provides three core ratings: Outperform, Market Perform, and Underperform, and three ancillary ratings: Suspended, Restricted, and Covered-Not Rated. For purposes of New York Stock Exchange Rule 472 and FINRA Rule 2711, Outperform is classified as a Buy, Market Perform is classified as a Hold, and Underperform is classified as a Sell. Suspended indicates that KBW's investment rating and/or target price have been temporarily suspended due to applicable regulations and/or KBW policies. Restricted indicates that KBW is precluded from providing an investment rating or price target due to the firm's role in connection with a merger or other strategic financial transaction. Covered-Not Rated indicates that KBW is not providing an investment rating and/or price target due to the lack of publicly available information and/or its inability to adequately quantify the publicly available information to sufficiently produce such metrics.

North American Stocks and European Stocks are rated based on the share price upside to target price relative to the relevant sector index performance on a 12-month horizon. Outperform rated stocks have a greater than 10 percentage point ("pp") relative performance versus the sector, Market Perform rated stocks between +10pp to -10pp relative performance versus the sector, and Underperform rated stocks a lower than 10pp relative performance versus the sector. The 12-month price target may be determined by the stock's fundamentally driven fair value and/or other factors (e.g., takeover premium or illiquidity discount).

KBW Model Portfolio: "Model Portfolio Buy" - Companies placed on this list are expected to generate a total rate of return (percentage price change plus dividend yield) of 10% or more over the next 3 to 6 months. "Model Portfolio Sell" - Companies placed on this list are expected to generate a total rate of return (percentage price change plus dividend yield) at or below -10% over the next 3 to 6 months.

The purpose of the Model Portfolio is to inform institutional investors of KBWI's short-term (as described above) outlook for a particular industry sector. The Portfolio is not available for purchase or sale, cannot be duplicated as shown, is hypothetical and is for illustrative purposes only. For a more detailed description of the selection criteria and other specifics related to the construction of the Model Portfolio, please refer to the January 5, 2010 Model Portfolio Primer and/or contact your KBWI representative for more information.

The Model Portfolio should be viewed as a short-term outlook of a particular industry sector, not as individual security recommendations. The Model Portfolio uses a three-to-six-month time horizon and should not be considered when making longer term investments. KBWI Research publishes research with a 12-month outlook on each issuer of securities contained in the Model Portfolio. Investors who are interested in a particular security should request KBWI Research's coverage of such securities by contacting your KBWI representative. KBW research contains analyses of fundamentals underlying each issuer.

KBWI's long-term recommendations may differ from recommendations made for the Model Portfolio. These differences are the result of different time horizons—KBWI research has a 12-month outlook and the Model Portfolio has a three-to-six-month outlook.

Although the model portfolio is based upon actual performance of actual investments, KBWI did not recommend that investors purchase this combination—or hypothetical portfolio—of investments during the time period depicted here. As this hypothetical portfolio was designed with the benefit of hindsight, the choice of investments contained in it reflects a subjective choice by KBWI. Accordingly, this hypothetical portfolio may reflect a choice of investments that performed better than an actual portfolio, which was recommended during the depicted time frame, would have performed during the same time period. Moreover, unlike an actual performance record, these results do not represent actual trading wherein market conditions or other risk factors may have caused the holder of the portfolio to liquidate or retain all or part of the represented holdings.

Important Disclosures (Continued)

Stifel/KBW Income Opportunity List, Stifel/KBW Analyst Select List, and Stifel/KBW Select Income Opportunity—The Crossovers List: These lists include companies that analysts believe have the most attractive risk-adjusted return potential over the next 12 months, or, in the case of the Stifel/KBW Income Opportunity Ideas List, have yield in excess of 2%. In some cases, analysts who cover more than one sub-sector may have more than one name on the list.

Other Research Methods: Please be advised that KBW provides to certain customers on request specialized research products or services that focus on covered stocks from a particular perspective. These products or services include, but are not limited to, compilations, reviews, and analysis that may use different research methodologies or focus on the prospects for individual stocks as compared to other covered stocks or over differing time horizons or under assumed market events or conditions.

OTHER DISCLOSURES

Indices: The following indices: U.S.: KBW Bank Index (BKX), KBW Insurance Index (KIX), KBW Capital Markets Index (KSX), KBW Regional Banking Index (KRX), KBW Mortgage Finance Index (MFX), KBW Property & Casualty Index (KPX), KBW Premium Yield Equity REIT Index (KYX); KBW Financial Sector Dividend Yield Index (KDX) and Global: KBW Global ex-U.S. Financial Sector Index (KGX), are the property of KBWI.

KBWI does not guarantee the accuracy and/or completeness of the Indices, makes no express or implied warranties with respect to the Indices and shall have no liability for any damages, claims, losses, or expenses caused by errors in the index calculation. KBWI makes no representation regarding the advisability of investing in options on the Index. Past performance is not necessarily indicative of future results.

ETFs: The shares ("Shares") of KBW ETFs are not sponsored, endorsed, sold, or promoted by KBWI. KBWI makes no representation or warranty, express or implied, to the owners of the Shares or any member of the public regarding the advisability of investing in securities generally or in the Shares particularly or the ability of its Indices to track general stock market performance. The only relationship of KBWI to Invesco PowerShares Capital Management LLC and ProShares is the licensing of certain trademarks and trade names of KBWI and its Indices which are determined, composed, and calculated by KBWI without regard to Invesco PowerShares Capital Management LLC and ProShares, the fund, or the Shares. KBWI has no obligation to take the needs of Invesco PowerShares Capital Management LLC and ProShares or the owners of the shares into consideration in determining, composing, or calculating the Indices. KBWI is not responsible for and has not participated in any determination or calculation made with respect to issuance or redemption of the Shares. KBWI has no obligation or liability in connection with the administration, marketing, or trading of the Shares.

ETFs trade like stocks, are subject to investment risk, fluctuate in market value and may trade at prices above or below the ETFs net asset value. Investing in a single sector may be subject to more volatility than funds investing in a diverse group of sectors. Brokerage commissions and ETF expenses will reduce returns. In general, ETFs can be expected to move up or down in value with the value of the applicable index. Although ETFs may be bought and sold on the exchange through any brokerage account, ETFs are not individually redeemable from the Fund. Investors may acquire ETFs and tender them for redemption through the Fund in Creation Unit Aggregations only, please see the [prospectus](#) for more details. There are risks involved with investing in ETFs, including possible loss of money. Shares are not actively managed and are subject to risks including those regarding short selling and margin maintenance requirements. **Past performance is not necessarily indicative of future results.**

Leverage and Inverse ETFs: ProShares Ultra KBW Regional Banking (KRU) and ProShares Short KBW Regional Banking (KRS) ETFs seek returns that are either 2x, -1x, respectively, the return of an index or other benchmark (target) **for a single day**, as measured from one NAV calculation to the next. **Due to the compounding of daily returns, returns over periods other than one day will likely differ in amount and possibly direction from the target return for the same period.** These effects may be more pronounced in funds with larger or inverse multiples and in funds with volatile benchmarks. These funds may not be suitable for all investors and should be used only by knowledgeable investors who understand the potential consequences of seeking daily leveraged investment results. **Investing involves risk, including the possible loss of principal. ProShares Short are non-diversified and should lose value when their market indexes rise—a result that is opposite from traditional ETFs**—and they entail certain risks including risk associated with the use of derivatives, imperfect benchmark correlation, leverage, and market price variance, all of which can increase volatility and decrease performance.

For more on correlation, leverage, and other risks, please read the [prospectus](#).

An investor should consider the Funds' investment objectives, risks, charges, and expenses carefully before investing. This and other information can be found in their prospectuses. For this and more complete information about the Funds, call InvescoPowerShares at 1-800-983-0903 or visit <https://invescopowershares.com>; or call ProShares Client Services at 1-866-776-5125 or visit <http://www.proshares.com/resources/litcenter/> for a prospectus. The prospectus should be read carefully before investing.

Shares of the ETFs funds are not guaranteed or insured by the FDIC or by another governmental agency; they are not obligations of the FDIC nor are they deposits or obligations of or guaranteed by KBWI, Invesco PowerShares Capital Management LLC or ProShares. ETFs are distributed by Invesco Distributors, Inc. the distributor of the PowerShares Exchange-Traded Fund Trust II. PowerShares® is a registered trademark of Invesco PowerShares Capital Management LLC; ProShares are distributed by SEI Investments Distribution Co., which is not affiliated with ProFunds Group or its affiliates.

Important Disclosures (Continued)

General Risk Disclosure: Investments in securities or financial instrument involve numerous risks which may include market risk, counterparty default risk, liquidity risk and exchange rate risk. No security or financial instrument is suitable for all investors, and some investors may be prohibited in certain states or other jurisdictions from purchasing securities mentioned in this communication. The securities of some issuers may not be subject to the audit and reporting standards, practices and requirements comparable to those companies located in the investor's local jurisdiction. Where net dividends to ADR investors are discussed, these are estimated, using withholding tax rate conventions, and deemed accurate, but recipients should always consult their tax advisor for exact dividend computations.

COUNTRY-SPECIFIC AND JURISDICTIONAL DISCLOSURES

United States: This report is being distributed in the U.S. by KBWI. Where the report has been prepared by a non-U.S. affiliate, KBWI accepts responsibility for its contents. **U.K. and European Economic Area (EEA):** This report is issued and approved for distribution in the EEA by Stifel Nicolaus Europe Limited, also trading as Keefe, Bruyette & Woods Europe, which is regulated in the United Kingdom by the Financial Conduct Authority (FCA).

In jurisdictions where KBW is not already licensed or registered to trade securities, transactions will only be affected in accordance with local securities legislation which will vary from jurisdiction to jurisdiction and may require that a transaction is carried out in accordance with applicable exemptions from registration and licensing requirements. Non-U.S. customers wishing to effect a transaction should contact a representative of the KBW entity in their regional jurisdiction except where governing law permits otherwise. U.S. customers wishing to effect a transaction should do so by contacting a representative of KBWI.

ONLY DISTRIBUTE UNDER REGULATORY LICENSE

This communication is only intended for and will only be distributed to persons residing in any jurisdictions where such distribution or availability would not be contrary to local law or regulation. This communication must not be acted upon or relied on by persons in any jurisdiction other than in accordance with local law or regulation and where such person is an investment professional with the requisite sophistication and resources to understand an investment in such securities of the type communicated and assume the risks associated therewith.

The securities discussed in this report may not be available for sale in all jurisdictions. Clients considering an investment in the securities discussed should speak with their sales representative prior to making an investment decision.

CONFIDENTIAL INFO

This communication is confidential and is intended solely for the addressee. It is not to be forwarded to any other person or copied without the permission of the sender. Please notify the sender in the event you have received this communication in error.

NO SOLICITATION OR PERSONAL ADVICE

This communication is provided for information purposes only. It is not a personal recommendation or an offer to sell or a solicitation to buy the securities mentioned. Investors should obtain independent professional advice before making an investment.

ASSUMPTIONS, EFFECTIVE DATE, AND UPDATES

Certain assumptions may have been made in connection with the analysis presented herein, so changes to assumptions may have a material impact on the conclusions or statements made in this communication. Facts and views presented in this communication have not been reviewed by, and may not reflect information known to, professionals in other business areas of KBW, including investment banking personnel.

The information relating to any company herein is derived from publicly available sources and KBW makes no representation as to the accuracy or completeness of such information. Neither KBW nor any of its officers or employees accept any liability whatsoever for any direct, indirect, or consequential damages or losses arising from any use of this report or its content.

This communication has been prepared as of the date of the report.

KBW does not undertake to advise clients of any changes in information, estimates, price targets, or ratings, all of which are subject to change without notice. The recipients should assume that KBW will not update any fact, circumstance, or opinion contained in this report.

COPYRIGHT

This report is produced for the use of KBW customers and may not be reproduced, re-distributed or passed to any other person or published in whole or in part for any purpose without the prior consent of KBW.