

May 30, 2008

## Cyclical Nature of New Bank Sale Pricing

In my last letter, I wrote about the decline in the number of new banks that were sold and the fall-off in pricing multiples. In this letter, I'm trying to add a little historical perspective about where pricing is today and how long the cycle might last.

In the back of this report, on pages 27 to 31, we list the "new bank" that sold each year and some pricing data related to each deal. While there have been only three "new bank" deals thus far in 2008, the median price to tangible book of 138% is very similar to the 1994 median of 133%. While three deals is not a lot, consider that if the two new bank sales announced in December 2007 were included, the median would still be 138% with three of the five deals priced at 131%, 137% and 138% of tangible book.

### New Bank Deal Comparison – 2008 vs. 1994

<u>Buying Bank</u>	<u>Selling <i>de novo</i> Bank</u>	<u>Year De Novo Opened</u>	<u>Deal Value (in mill.)</u>	<u>Price/ Tang. Book</u>
<u>2008 New Bank Deals*</u>				
Village B&T (VA)	River City Bank (VA)	2004	\$20	131%
Savings Bank-Maine	Rivergreen Bank (ME)	2006	13	186
NOVA Financial (PA)	Pennsylvania Business (PA)	1999	<u>11</u>	<u>138</u>
Total or Median			\$44	<b>138%</b>
<u>1994 New Bank Deals</u>				
Jefferson (VA)	Bank of Loudoun (VA)	1988	\$11	210%
Valley National (NJ)	American Union (NJ)	1990	7	176
First Fidelity (NJ)	First State Bank (DE)	1988	7	133
First State Fin. (NJ)	Ocean Independent (NJ)	1988	5	135
JeffBanks (PA)	Security First (PA)	1988	3	100
Franklin (DC)	George Washington (VA)	1989	3	108
Village (CT)	Liberty National (CT)	1989	<u>1</u>	<u>111</u>
Total or Median			\$37	<b>133%</b>

\* Deals through May 23, 2008.

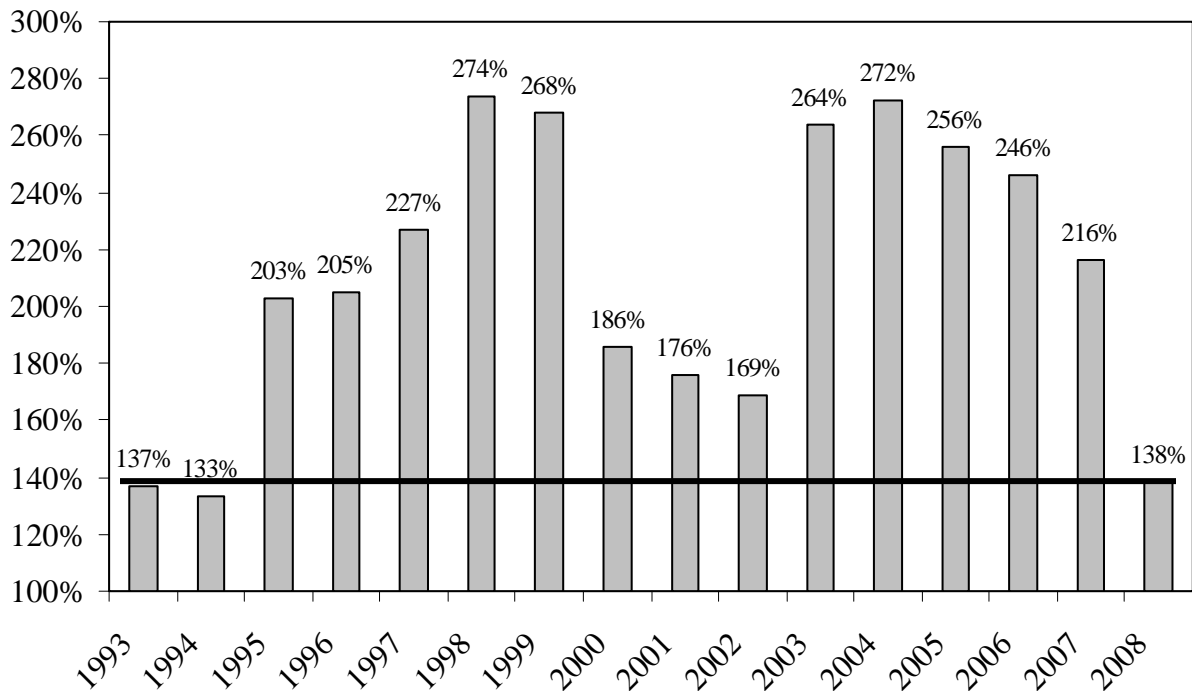
Source: SNL Financial, Charlottesville, Virginia.

The two sales in December of 2007 and the three in early 2008 were not sales from strength. At least one bank got caught up in the mortgage crisis, others had NPA issues and one had a failed stock offering. In the latter, the bank set a target range of capital to raise, priced it too high and then failed to achieve the minimum.

The sales in 1994 were similar as all of the new banks that were sold had issues. Several of them had NPAs greater than 4% of assets that threatened their capital levels while others had few loan quality issues, but had earnings deterioration or losses coupled with low capital.

To get a better look at the cyclical nature of bank sale pricing, the graph below clearly shows three “down” periods and two five-year “up” periods. Pricing in 1993 and 1994 was low, but it was actually an improvement over pricing in prior years as the economy and banks were emerging from the crises of the late 80s and early 90s. In the following five years, from 1995 through 1999, pricing was well over 200% of tangible book before it fell below that level for three years, from 2000 to 2003. After 2003, pricing again moved over 200% of tangible book for five years before retreating dramatically in late 2007 and early 2008.

New Bank Sales  
Trends in Median Price to Tangible Book



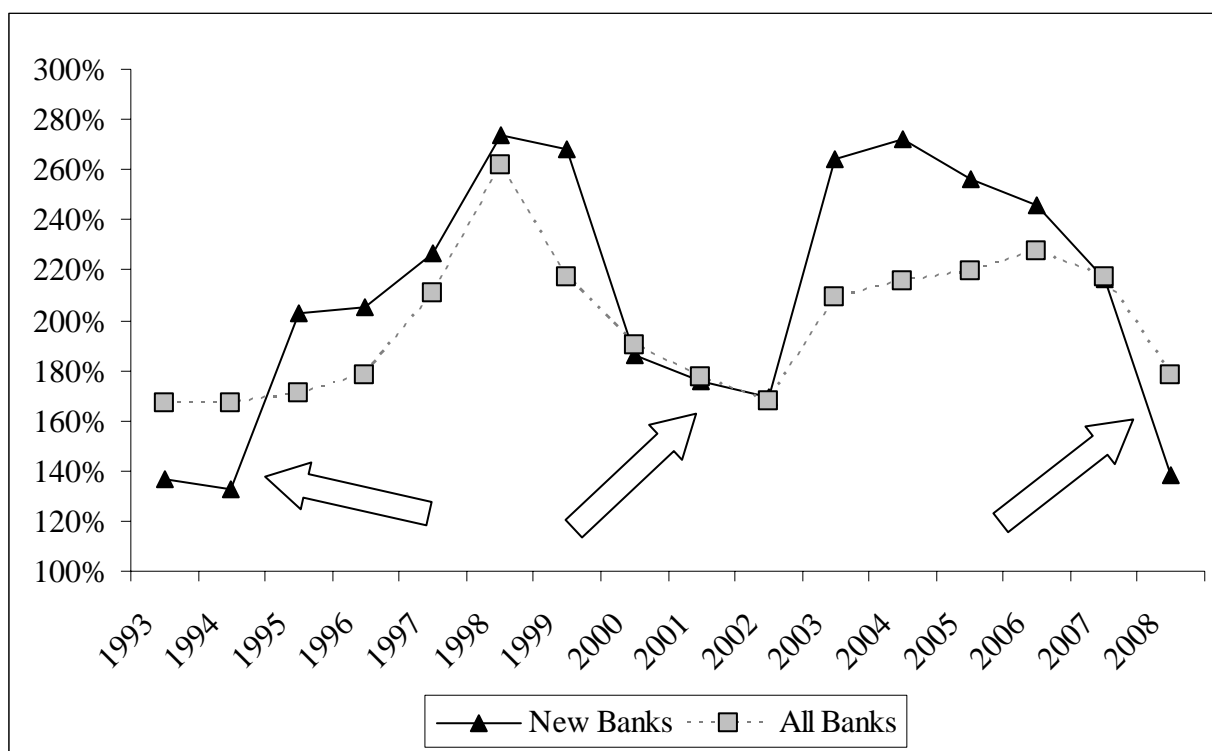
Note: Pricing from 1990 to 1994 was fairly constant

Source: Danielson Capital and SNL Financial

The two up cycles have been good, each lasting about five years, and the down cycles have all lasted more than two years. Pricing was low throughout much of the late 80s and early 90s and again, although to a much lesser extent, when the tech bubble burst in 2000 and after 9/11. This current down cycle started in the fourth quarter of 2007, and is only about three quarters old which implies that pricing may stay low through 2009 before starting to come back in late 2010 or 2011.

When “new bank” sale pricing moves, it tends to have larger swings than normal bank sale pricing. This seems to reflect values placed on their growth opportunities in good times and questions about realizing earning potential in tough times. In good times from 1995-1999 and from 2003-2007, new banks sold at a higher price to tangible book than the national median. In down cycles, the median price to tangible book of new banks is below, or similar to, the national median. This is where we were in late 2007 and through early 2008.

Bank Sale Pricing Multiples  
Price to Tangible Book Trends - New Bank Median vs. National Median



Source: SNL Financial

What is not shown above is the number of deals in each year. As one would expect, the number of deals drops dramatically in the down periods as those banks that can, wait it out.

As always, we hope you enjoy the report. If you have any questions, please feel free to give me a call.

Sincerely,

A handwritten signature in blue ink that reads "Dave Danielson". The signature is written in a cursive, flowing style.

David G. Danielson  
President  
Danielson Associates, LLC