



A CASE for continuing investment opportunities in community banks.

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Executive Summary

Have Investors Missed Their Opportunity To Invest In Community Banks?

Small cap bank stocks have continued their rise, up greater than 98%, from credit crisis lows reached on October 3rd, 2011, the result of nine quarters of credit quality improvement, “better” capitalization, a stabilized housing market, and a return to loan growth albeit slow loan growth.

We believe banks are still attractively valued as banks historically have traded at a price-to-tangible book value of 1.7x for the ten year historical average and 2.5x for the twenty year average and banks currently trade at 1.45x TBV. We believe the current discount to historical levels provides an attractive opportunity to invest in quality banks at bargain prices.

While buyers and sellers have yet to close the bid/ask spread enough to drive a “wave” in merger activity. We have seen year over year growth in the number of mergers announced and consummated. We believe that the continued regulatory burden will contribute to an increase in banks with less than \$1 billion in assets becoming willing sellers. As the anticipated merger activity takes place, we believe we will see small cap bank and thrift valuations move towards historical levels.

We agree that if the domestic economy does not materially improve, low interest rates will likely persist well into 2014. We view this as an opportunity for stock pickers to outperform as quality banks are better positioned than others to manage through this challenging operating environment.

We believe that Emerald’s 10 Step Research Process enables us to pick winners in the type of bifurcated market that exists in the bank sector today. We believe that we have and will continue to identify attractively valued banks that have better growth prospects, lower deposit costs, liquidity deployment, credit tailwinds and cost reduction capacity.

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