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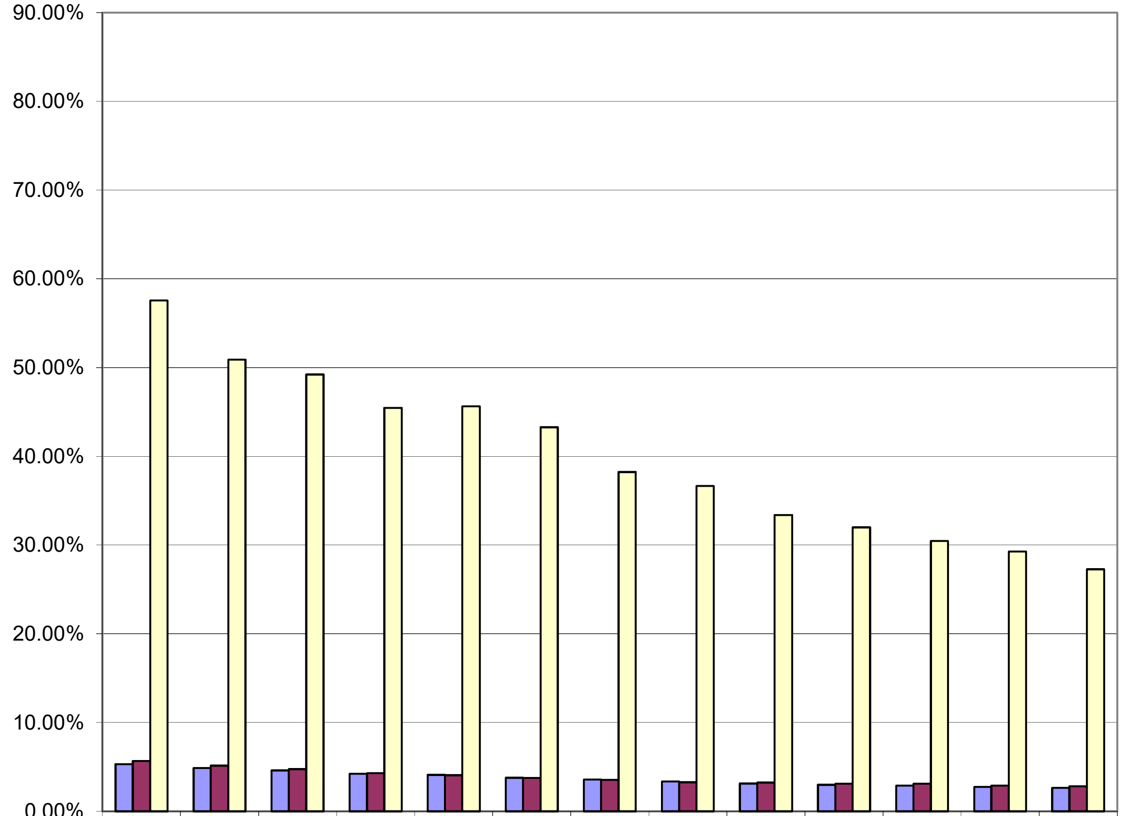
Steve H.
Powell & Company

Asset Quality Update – Q1 2018 Edition

Trends in Asset Quality – Average Levels

Based on Steve H. Powell & Company client data, during the First Quarter 2018, the average level of adversely graded assets decreased as a percentage of total assets and capital. Also, the average level of adversely graded loans decreased as a percentage of total loans. Problem assets averaged 2.65% of total assets and 27.27% of tier-one capital plus loan loss reserve as compared to 2.77% of total assets and 29.26% of tier-one capital plus loan loss reserve while problem loans averaged 2.82% of total loans as compared to 2.90% of total loans during the Fourth Quarter 2017.

TRENDS IN ASSET QUALITY
AVERAGE LEVEL OF ADVERSELY GRADED ASSETS

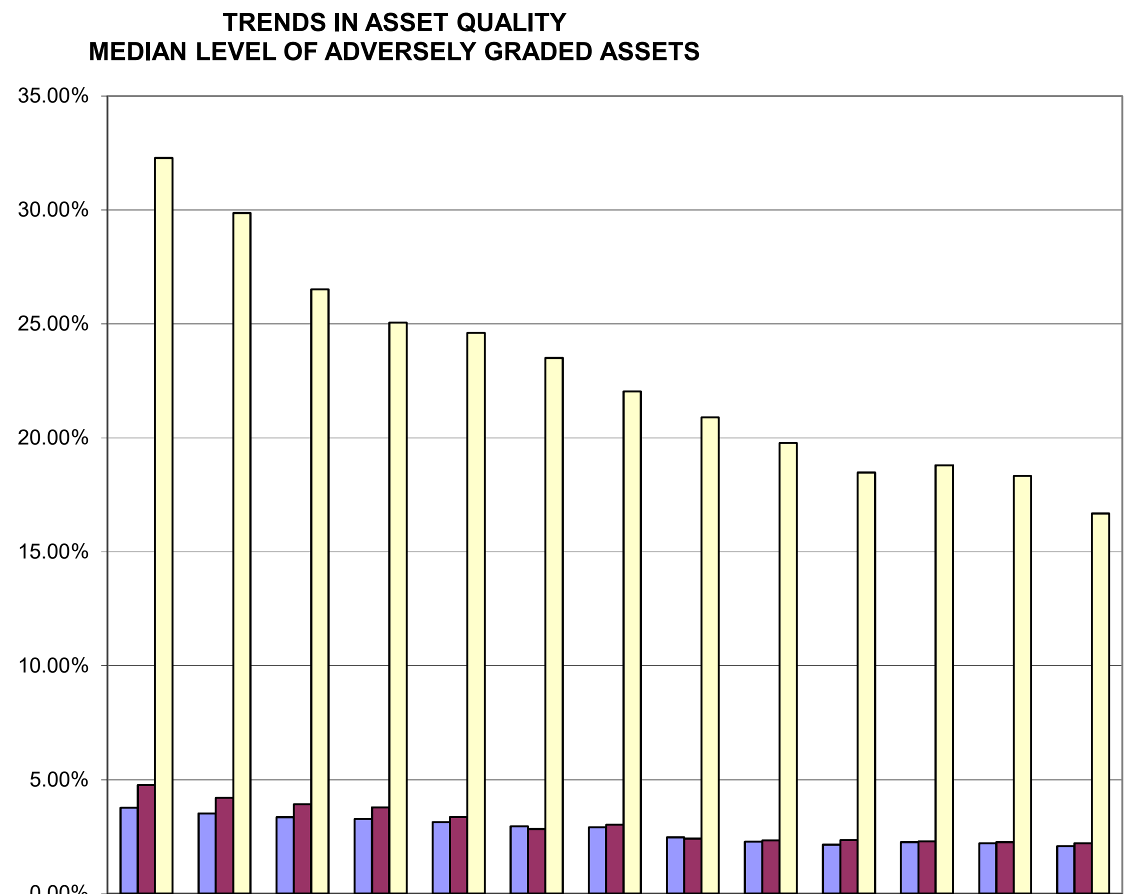


	1st 15	2nd 15	3rd 15	4th 15	1st 16	2nd 16	3rd 16	4th 16	1st 17	2nd 17	3rd 17	4th 17	1st 18
- Adversely Graded Assets / Total Assets	5.31%	4.86%	4.59%	4.22%	4.09%	3.78%	3.57%	3.36%	3.12%	2.97%	2.90%	2.77%	2.65%
- Adversely Graded Loans / Total Loans	5.64%	5.15%	4.75%	4.28%	4.06%	3.74%	3.55%	3.27%	3.23%	3.10%	3.09%	2.90%	2.82%
- Adversely Graded Assets / Tier 1 Cap' + LLR	57.57%	50.91%	49.21%	45.46%	45.62%	43.28%	38.23%	36.65%	33.39%	31.99%	30.45%	29.26%	27.27%

Steve H. Powell & Company was founded in August of 1993 by former banker and regulator, Steve H. Powell. With the goal of providing unparalleled asset quality monitoring and regulatory compliance services, the company's clientele base has grown and now exceeds 100 different financial institutions. We also provide our clients with bank charter consulting, due diligence support, regulatory applications, financial analysis, and strategic planning. The staff of Steve H. Powell & Company is comprised of former bankers & regulators who understand the complexities of today's regulatory environment. The unique skill sets possessed by our specialists are derived from extensive review experience in institutions of various sizes and charter types.

Trends in Asset Quality – Median Levels

The median level of problem assets as of Q1 2018 decreased to 16.68% of tier-one capital plus loan loss reserve as compared to 18.34% during Q4 2017. Note the downward trend as overall asset quality continues to improve.



	1st 15	2nd 15	3rd 15	4th 15	1st 16	2nd 16	3rd 16	4th 16	1st 17	2nd 17	3rd 17	4th 17	1st 18
- Adversely Graded Assets / Total Assets	3.77%	3.52%	3.36%	3.28%	3.14%	2.96%	2.91%	2.47%	2.28%	2.15%	2.27%	2.22%	2.08%
- Adversely Graded Loans / Total Loans	4.77%	4.21%	3.92%	3.79%	3.37%	2.84%	3.03%	2.42%	2.34%	2.35%	2.30%	2.27%	2.22%
- Adversely Graded Assets / Tier 1 Cap' + LLR	32.28%	29.87%	26.52%	25.06%	24.60%	23.51%	22.03%	20.91%	19.77%	18.48%	18.81%	18.34%	16.68%

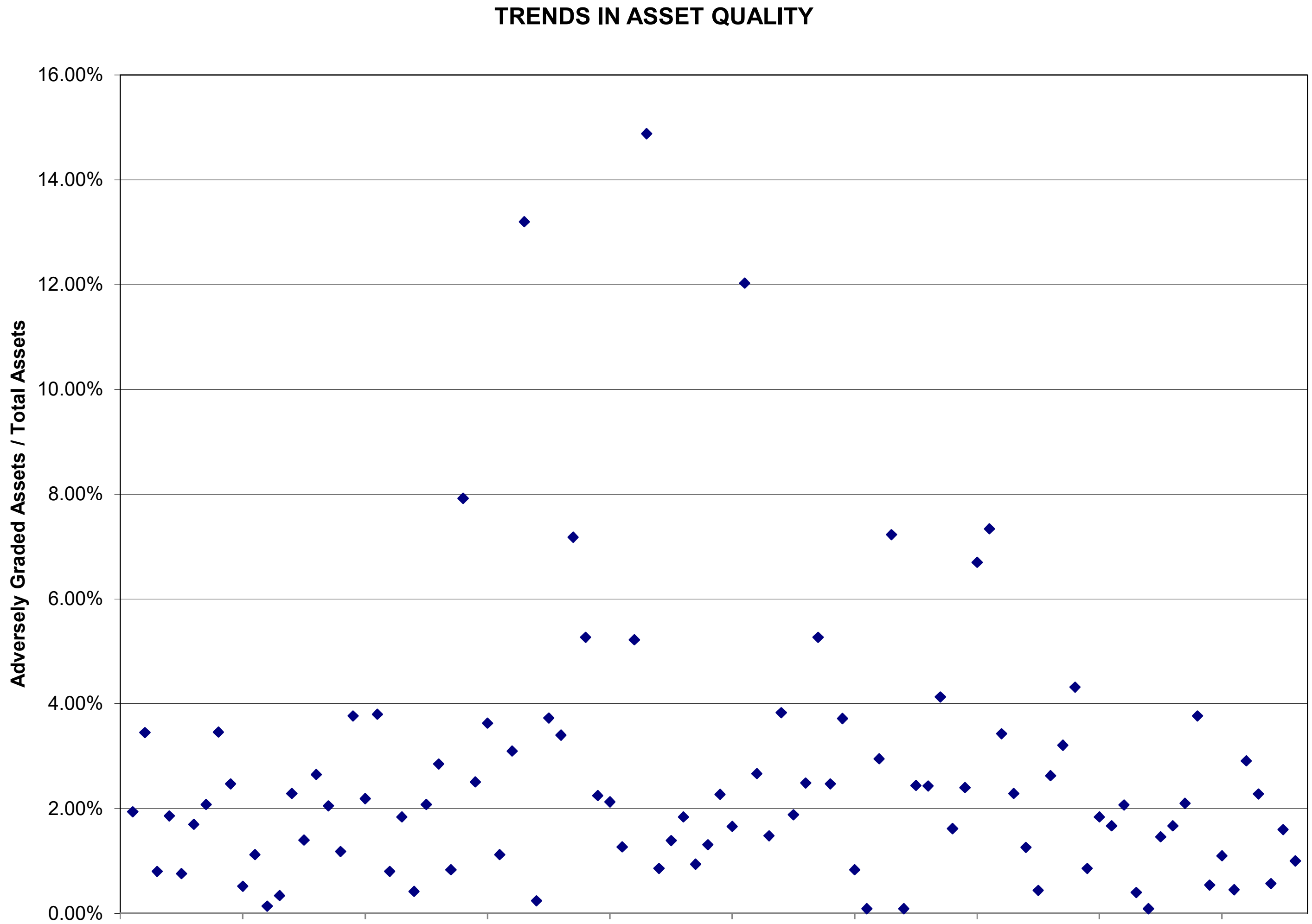
Historical Comparisons

During Q1 2018, increases in problem assets, as measured by adversely graded assets divided by tier-one capital plus loan loss reserve, were noted in approximately 15% of our clients. This quarter's increase compares to:

- 21% during the Fourth Quarter 2017
- 13% during the Third Quarter 2017
- 18% during the Second Quarter 2017
- 18% during the First Quarter 2017
- 16% during the Fourth Quarter 2016
- 19% during the Third Quarter 2016

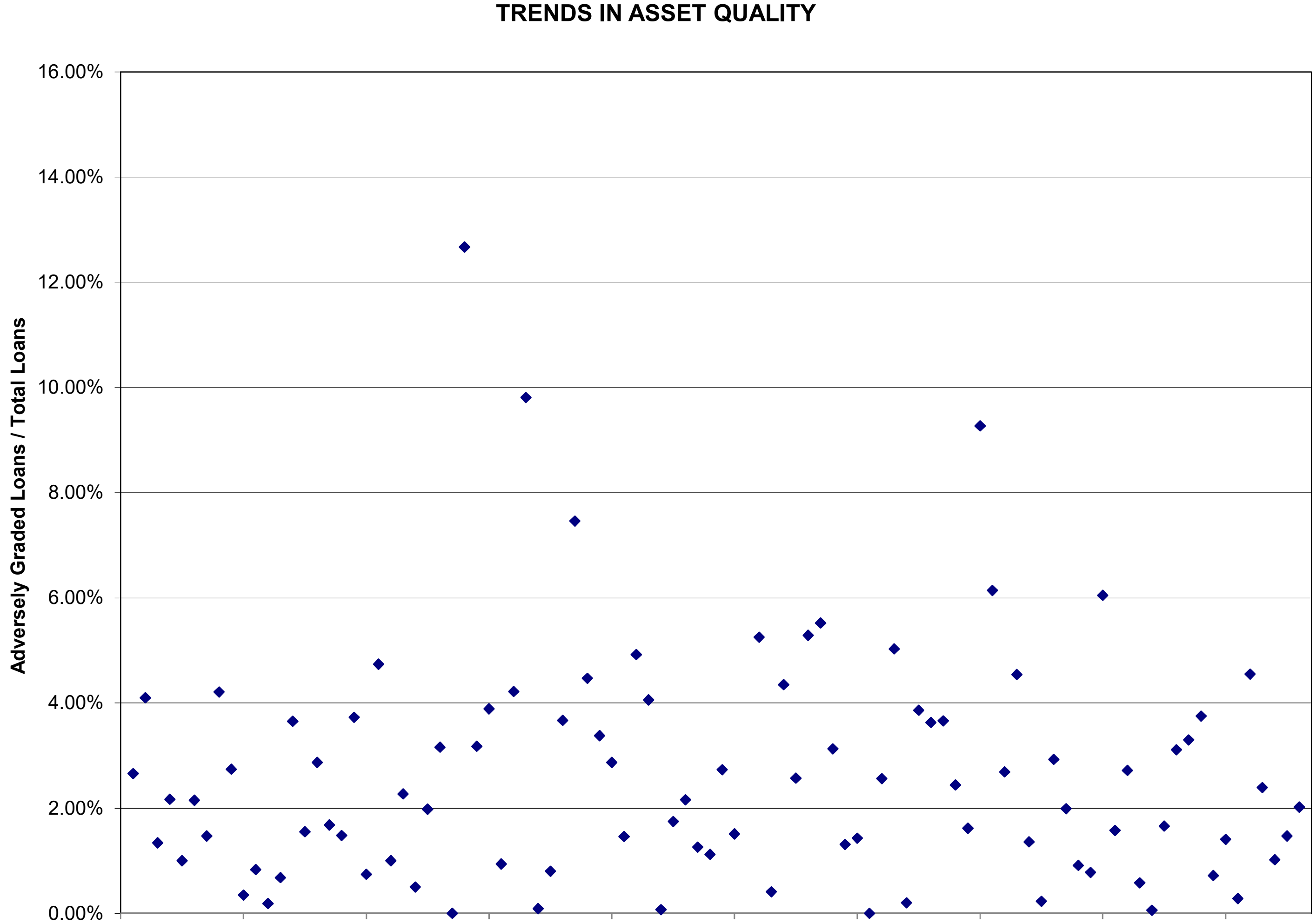
A higher level of volatility in the percentage of increases may be expected as overall asset quality stabilizes; however, increases may indicate a rise in portfolio risk.

Dispersion of Problem Assets – as a Percentage of Total Assets



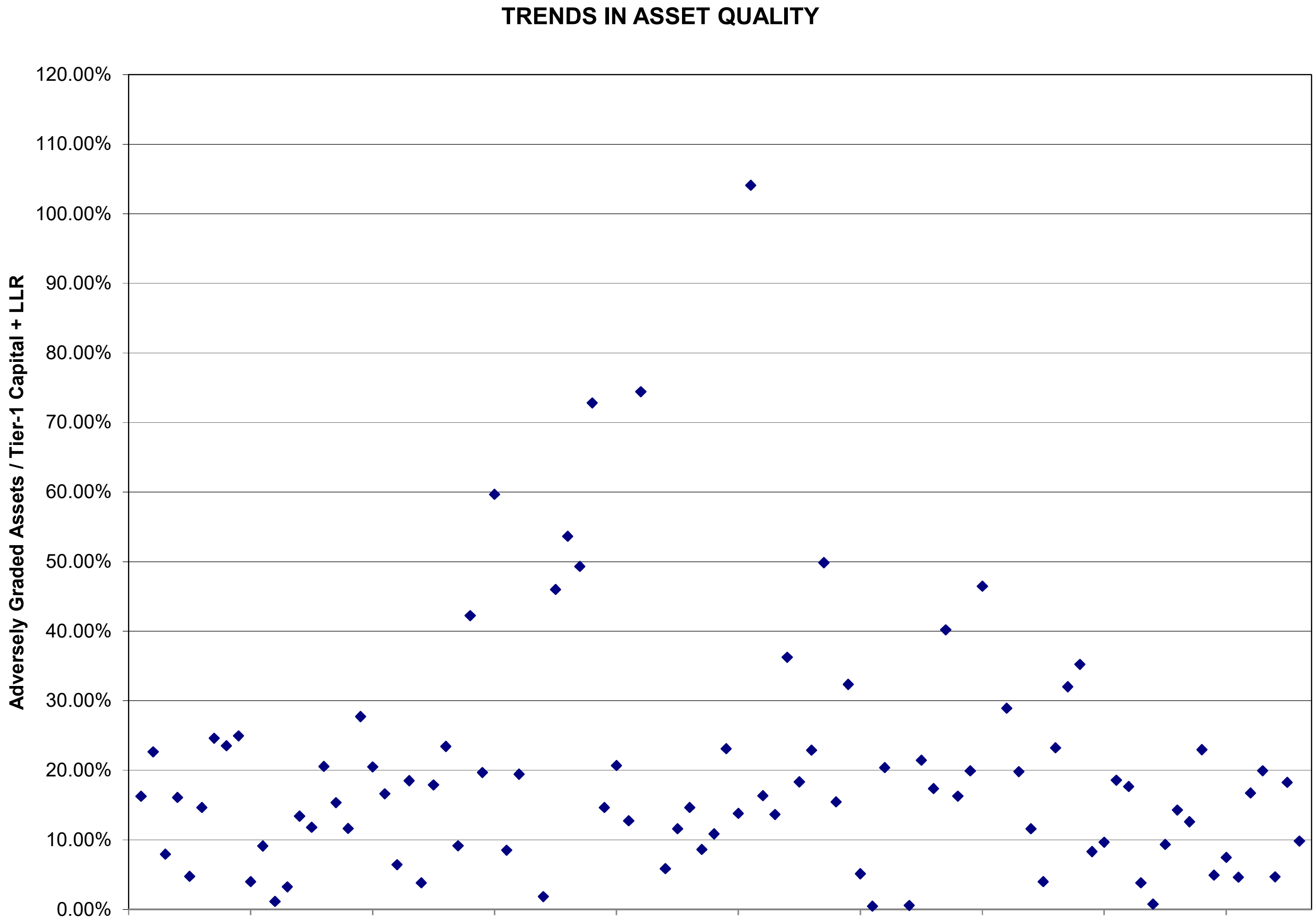
The above graph shows the dispersion of problem assets as a percentage of total assets. A traditional benchmark for significant asset quality concern is adversely graded assets that exceed 10% of total assets.

Dispersion of Problem Assets – as a Percentage of Total Loans



A traditional benchmark for significant asset quality concern is adversely graded loans that exceed 10% of total loans.

Dispersion of Problem Assets – as a Percentage of Tier-One Capital & Reserves



Note that four data points exceeding 120% are not included in the graph above for aesthetic reasons.

Historical Comparisons

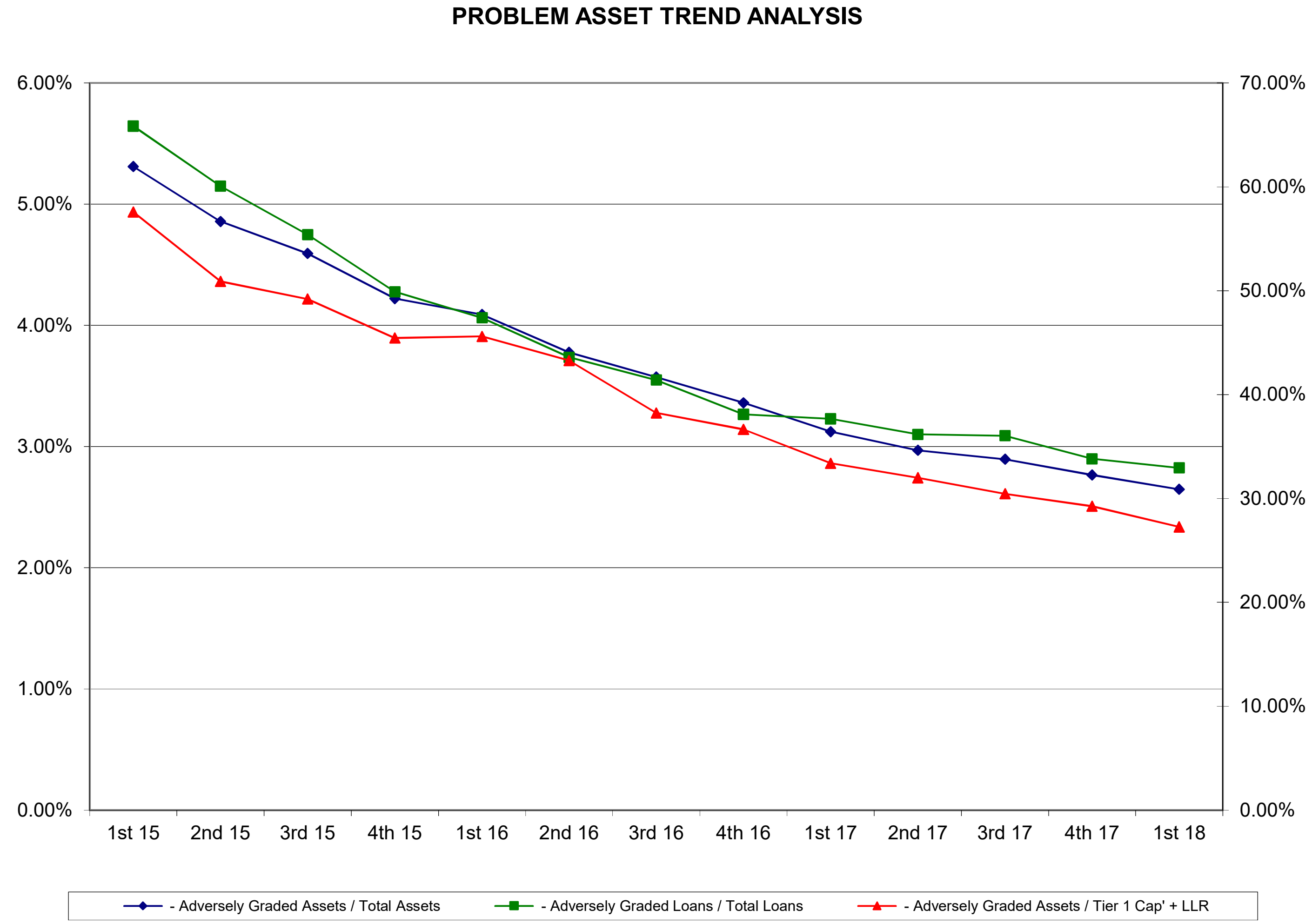
Our sample group includes seven (7) banks with problem assets exceeding 60% of tier-one capital plus loan loss reserve. This number compares to:

- Eight (8) during the Fourth Quarter 2017
- Ten (10) during the Third Quarter 2017
- Eleven (11) during the Second Quarter 2017

Five (5) banks now exceed 80% of tier-one capital plus loan loss reserve – a level normally associated with some form of formal regulatory action – as compared to:

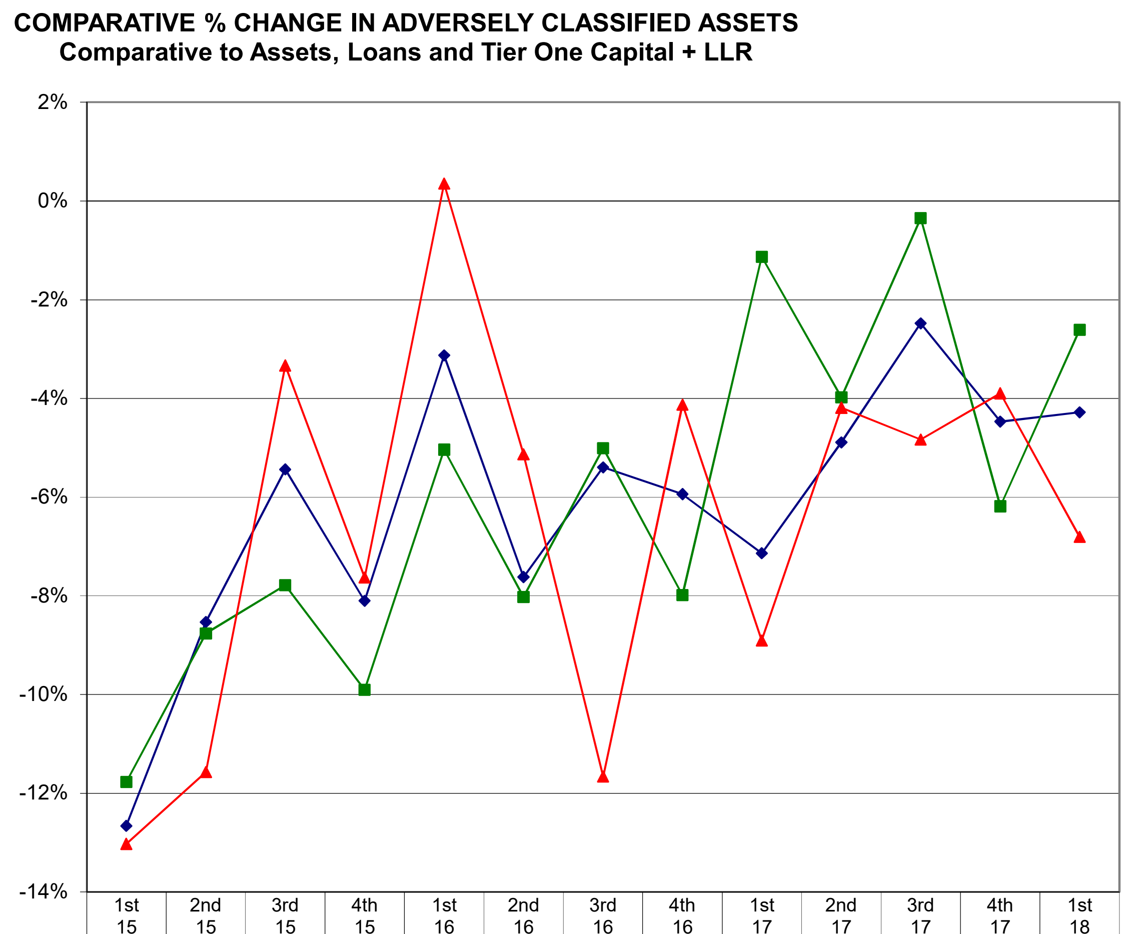
- Five (5) during the Fourth Quarter 2017
- Five (5) during the Third Quarter 2017
- Seven (7) during the Second Quarter 2017

Problem Asset Trend Analysis



The above graph again shows the trend in asset quality over the past three years as measured by adversely graded assets to total assets, adversely graded loans to total loans, and adversely graded assets to tier-one capital plus LLR.

Problem Asset Comparative Change Analysis



	1st 15	2nd 15	3rd 15	4th 15	1st 16	2nd 16	3rd 16	4th 16	1st 17	2nd 17	3rd 17	4th 17	1st 18
% Change in ACA/TA	-12.66%	-8.53%	-5.44%	-8.10%	-3.13%	-7.62%	-5.40%	-5.94%	-7.14%	-4.89%	-2.48%	-4.47%	-4.28%
% Change in ACL/TL	-11.77%	-8.76%	-7.79%	-9.90%	-5.04%	-8.02%	-5.01%	-7.99%	-1.13%	-3.98%	-0.35%	-6.19%	-2.61%
% Change in ACA/Tier 1 Cap' + LLR	-13.03%	-11.57%	-3.33%	-7.63%	0.35%	-5.13%	-11.66%	-4.12%	-8.90%	-4.19%	-4.83%	-3.90%	-6.81%

The above graph shows the pace of asset quality deterioration or improvement. The calculation is based on the percent change of problem asset levels from one quarter to the next. The graph indicates a favorable trend in asset quality ratios. Please note any data points below 0% indicate improvement in asset quality.

Modified Peer Data Analysis

We again performed an analysis in which a total of six outlier data points were excluded – the three lowest and the three highest data points, as based on classifications as a percentage of tier-one capital plus loan loss reserve.

With the outlier data points excluded, problem assets (or loans when compared to total loans) averaged 2.43% of total assets, 2.79% of total loans, and 21.69% of tier-one capital plus loan loss reserve. First Quarter 2018 modified data compares to the following Fourth Quarter 2017 modified average data set:

- 2.54% of total assets
- 2.84% of total loans, and
- 23.18% of tier-one capital plus loan loss reserve

Georgia Department of Banking & Finance Rule 80-1-5-.11. Combination of Debt for Legal Lending Limit Purposes

For Georgia State chartered banks, legal lending limit's combining rules (for loans to one borrower calculations) changed as of June 2017. Gone are the former tests for separate sources of repayment and financial interdependence. Under the changes, loans to separate entities are aggregated based on ownership & control of the borrower (person or corporation). Two projects could have separate sources of repayment as well as maintain completely separate financial statements systems, but they will now be grouped together for loans to one borrower / legal lending purposes because of common ownership or control. As defined in the Regulations, common control exists, much like Reg O, when an entity owns ≥25% of the borrowing entity.

To access the Rule directly: http://rules.sos.ga.gov/GAC/80-1-5-.11

Excerpts from the Ruel are detailed below:

- When proceeds of a loan or extension of credit are to be used for the direct benefit of the other person
- When a common enterprise is deemed to exist between the persons as the persons within the group are directly or indirectly related through common control
- When there is a common use of funds between the persons

"Common control" The direct or indirect possession of the power to direct or cause the direction of the management and policies of a person, whether through the ownership of voting securities, by contract, or otherwise.

A) Owns, controls or holds with power to vote 25 percent or more of any class of voting securities of the other person;
(B) Controls in any manner the election of a majority of the directors, trustees, or persons performing similar functions of the other person; or
(C) Exercises a controlling influence over the management or policies over the other person as determined by the department.

Certified Appraisal Changes

During April 2018, banking federal banking Regulators issued changes for appraisal, FIRREA, requirements. The change became effective on April 10, 2018 (the day after it was published in the Federal Register).

The change has, over simplified, established three thresholds for real estate related loans are which certified real estate appraisals will be required. For simple residential real estate loans, the requirements are unchanged – if the loan exceeds $250,000 a certified appraisal will be required. For CRE transactions, a certified appraisal will not be required for transactions of $500,000 (note the increase from the previous $250,000 limit) and those that exceed $1 million.

The joint pronouncement can be accessed at https://www.federalregister.gov/documents/2018/04/09/2018-06960/real-estate-appraisals

Excerpts from the Rule include:

- The final rule increases the threshold level at or below which appraisals are not required for commercial real estate transactions from $250,000 to $500,000
- It excludes all transactions secured by a single 1-to-4 family residential property; not proposing any threshold increases for transactions secured by a single 1-to-4 family residential property
- Require that regulated institutions entering into commercial real estate transactions at or below the proposed commercial real estate appraisal threshold obtain evaluations that are consistent with safe and sound banking practices unless the institution chooses to obtain an appraisal for such transactions

For more information about Steve H. Powell & Company, please visit us on the web at www.shpco.net.

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