Steve H. Powell & Company

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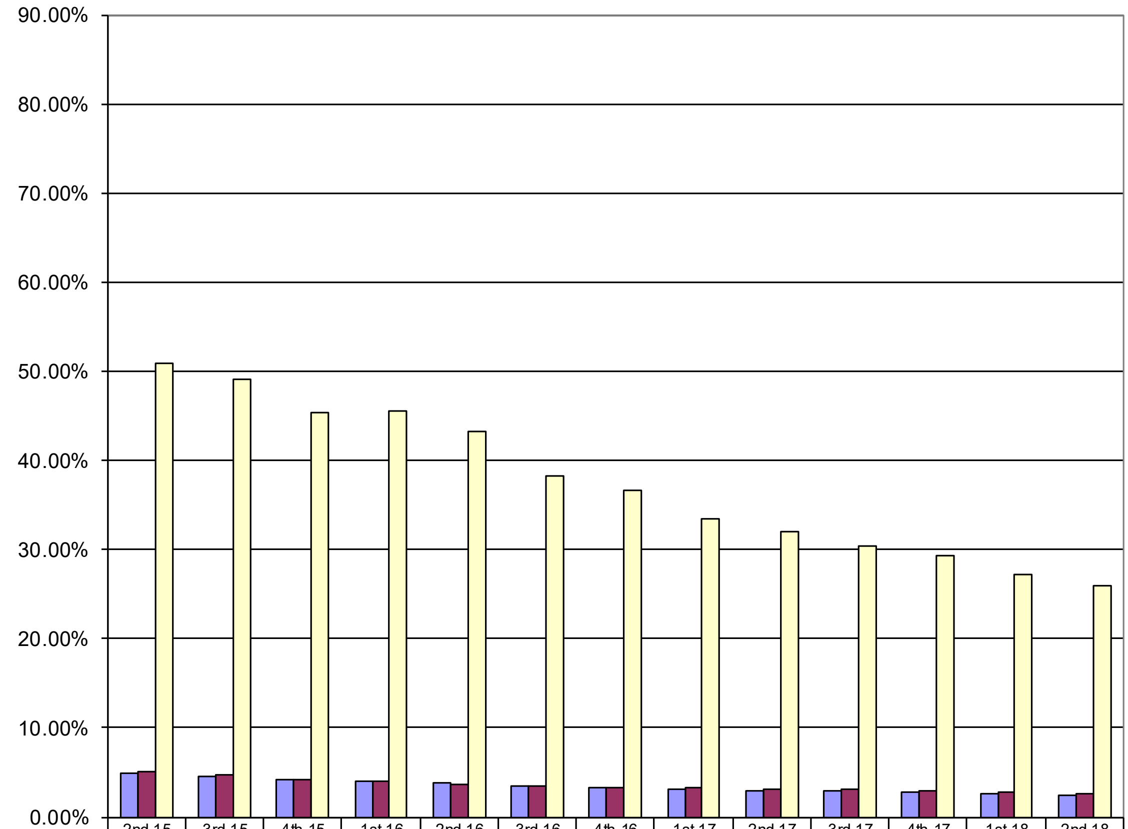
Asset Quality Update – Q2 2018 Edition

Trends in Asset Quality – Average Levels

Based on Steve H. Powell & Company client data, during the Second 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 2.49% of total assets and 25.92% of tier-one capital plus loan loss reserve as compared to 2.65% of total assets and 27.27% of tier-one capital plus loan loss reserve while problem loans averaged 2.61% of total loans as compared to 2.82% of total loans during the First Quarter 2018.

TRENDS IN ASSET QUALITY
AVERAGE LEVEL OF ADVERSELY GRADED ASSETS

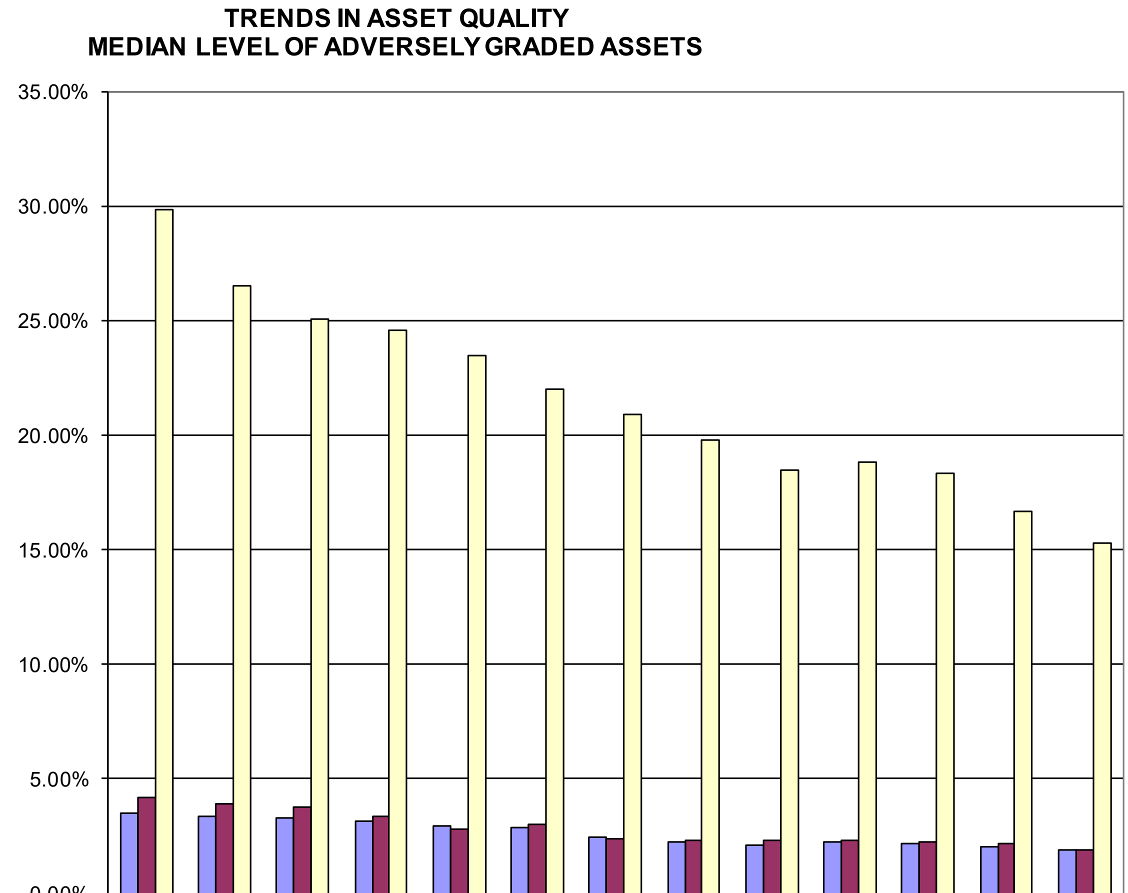


	2nd 15	3rd 15	4th 15	1st 16	2nd 16	3rd 16	4th 16	1st 17	2nd 17	3rd 17	4th 17	1st 18	2nd 18
- Adversely Graded Assets / Total Assets	4.86%	4.59%	4.22%	4.09%	3.78%	3.57%	3.36%	3.12%	2.97%	2.90%	2.77%	2.65%	2.49%
- Adversely Graded Loans / Total Loans	5.15%	4.75%	4.28%	4.06%	3.74%	3.55%	3.27%	3.23%	3.10%	3.09%	2.90%	2.82%	2.61%
- Adversely Graded Assets / Tier 1 Cap' + LLR	50.91%	49.21%	45.46%	45.62%	43.28%	38.23%	36.65%	33.39%	31.99%	30.45%	29.26%	27.27%	25.92%

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 Q2 2018 decreased to 15.31% of tier-one capital plus loan loss reserve as compared to 16.68% during Q1 2018. Note the downward trend as overall asset quality continues to improve.



	2nd 15	3rd 15	4th 15	1st 16	2nd 16	3rd 16	4th 16	1st 17	2nd 17	3rd 17	4th 17	1st 18	2nd 18
- Adversely Graded Assets / Total Assets	3.52%	3.36%	3.28%	3.14%	2.96%	2.91%	2.47%	2.28%	2.15%	2.27%	2.22%	2.08%	1.90%
- Adversely Graded Loans / Total Loans	4.21%	3.92%	3.79%	3.37%	2.84%	3.03%	2.42%	2.34%	2.35%	2.30%	2.27%	2.22%	1.93%
- Adversely Graded Assets / Tier 1 Cap' + LLR	29.87%	26.52%	25.06%	24.60%	23.51%	22.03%	20.91%	19.77%	18.48%	18.81%	18.34%	16.68%	15.31%

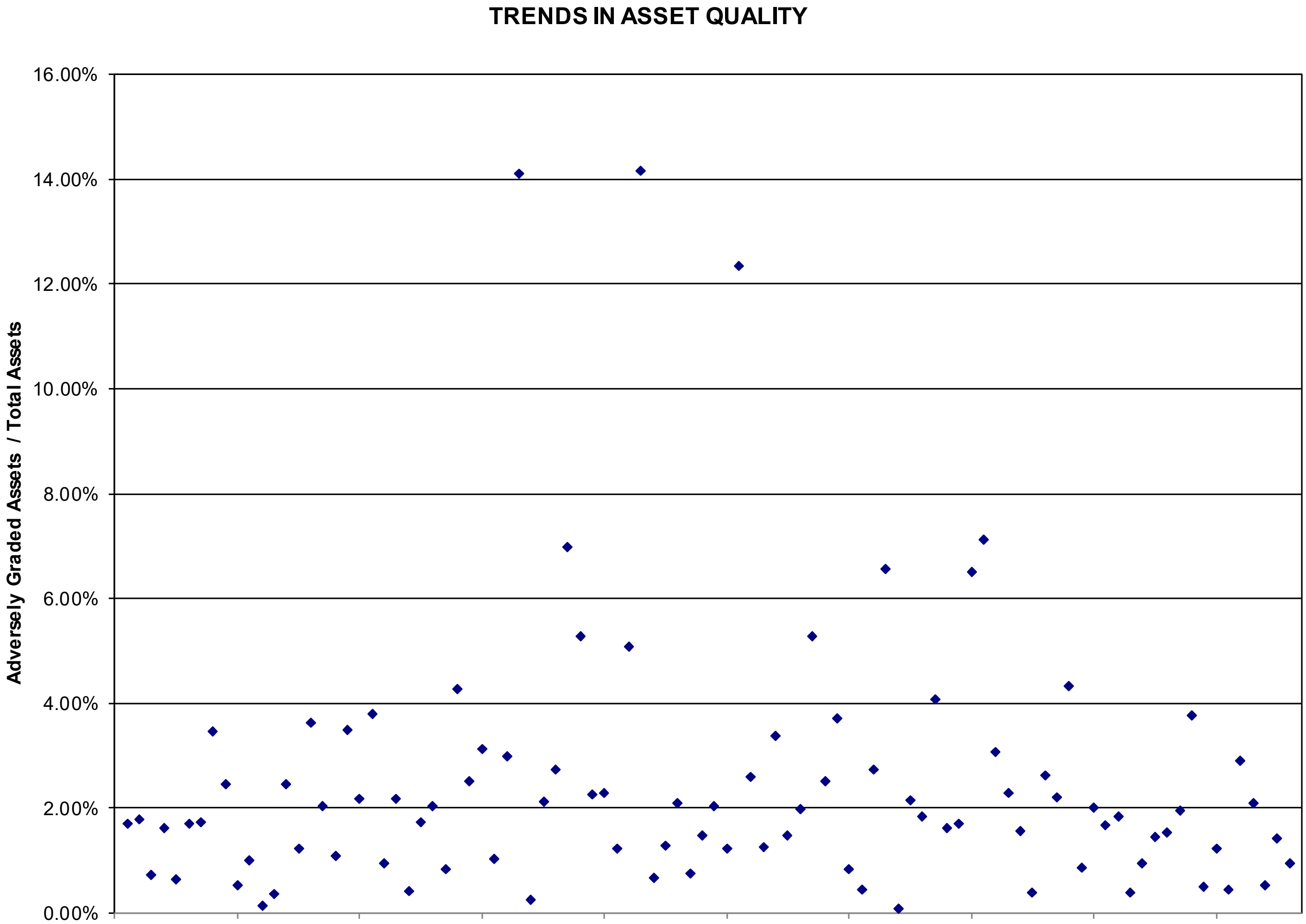
Historical Comparisons

During Q2 2018, increases in problem assets, as measured by adversely graded assets divided by tier-one capital plus loan loss reserve, were noted in approximately 20% of our clients. This quarter's increase compares to:

- 15% during the First Quarter 2018
- 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

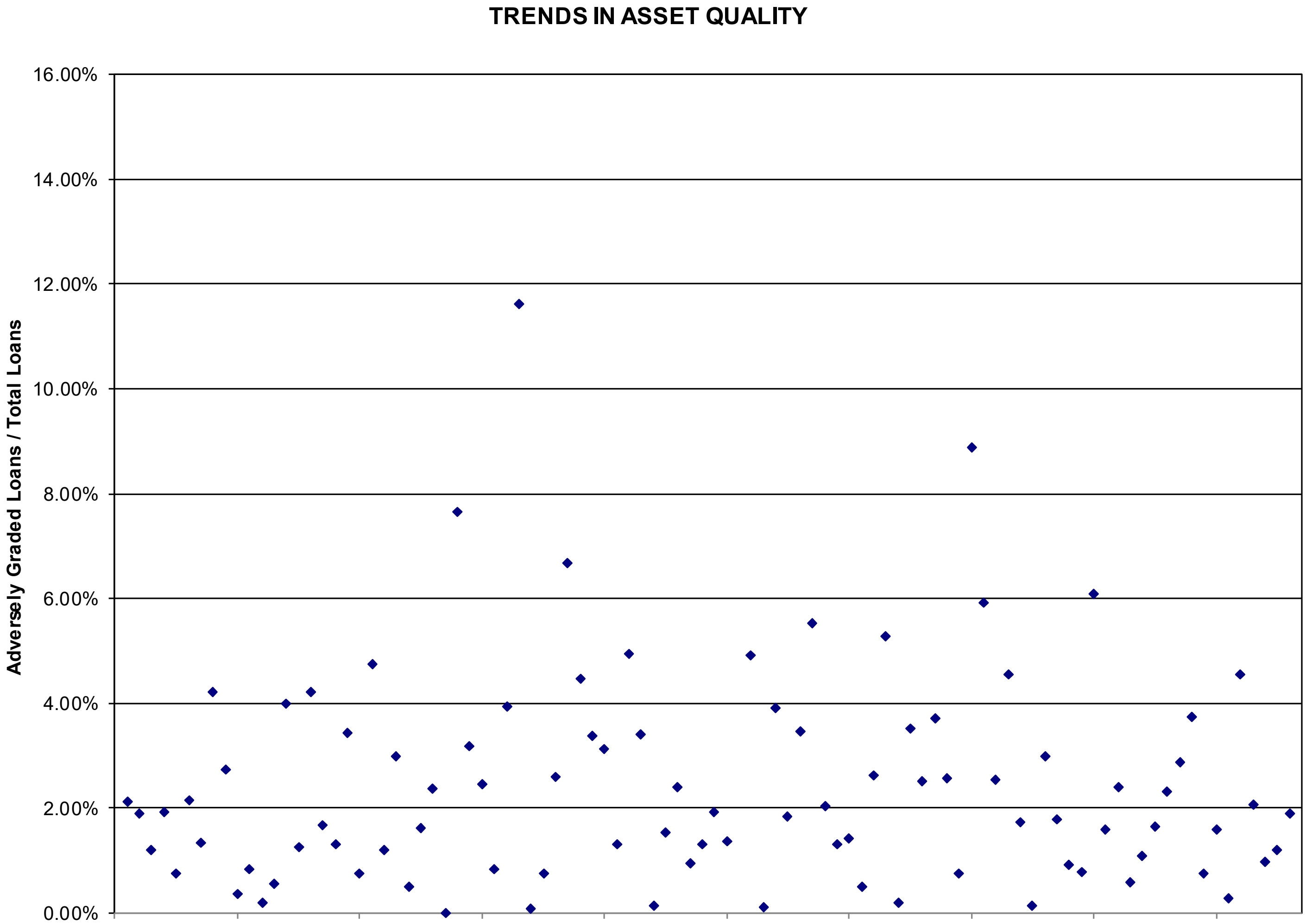
A higher level of volatility in the percentage of increases may be expected as overall asset quality stabilizes; however, increases may indicate a rise in portfolio risk.

Dispersion of Problem Assets – as a Percentage of Total Assets



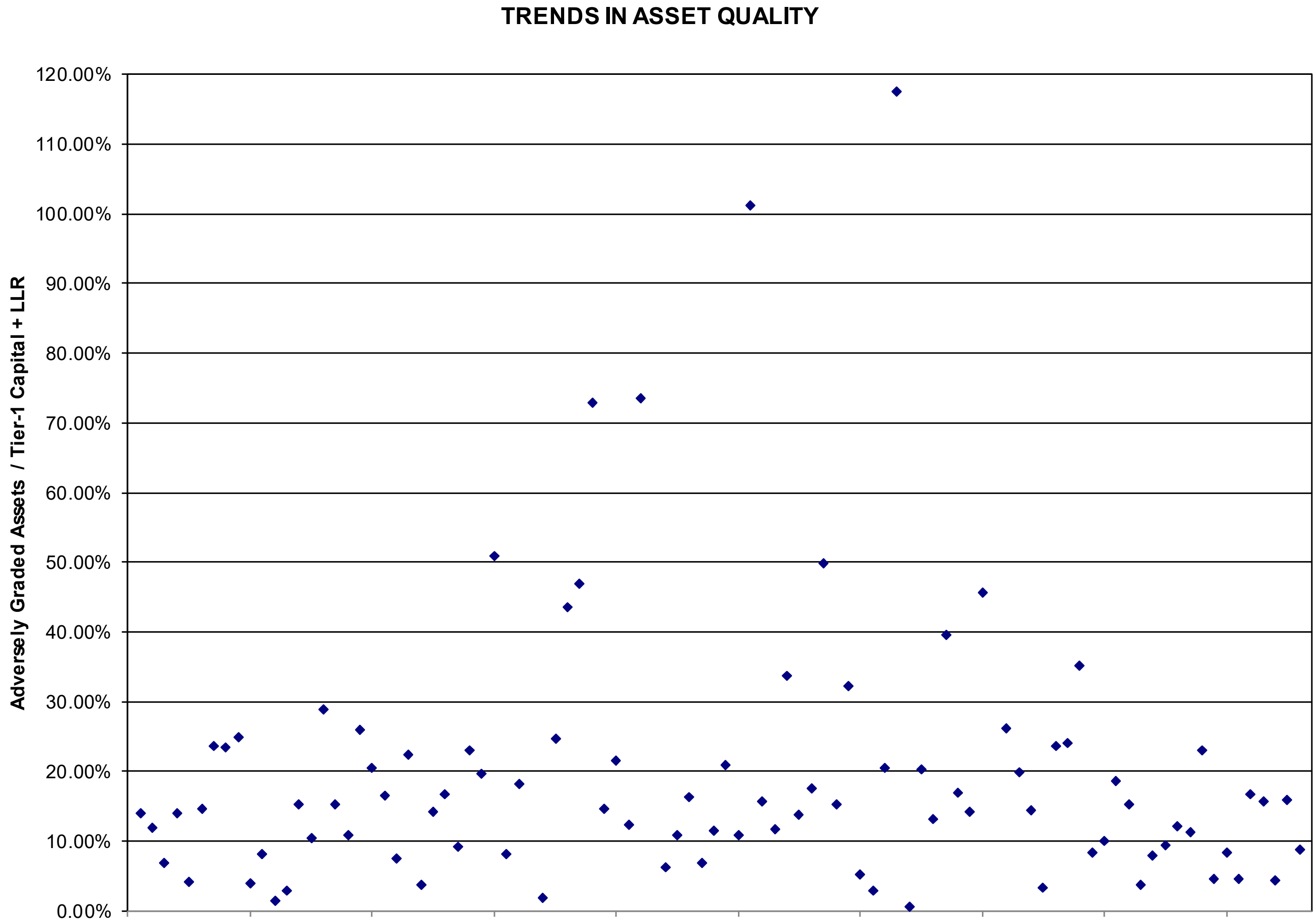
The above graph shows the dispersion of problem assets as a percentage of total assets. A traditional benchmark for significant asset quality concern is adversely graded assets that exceed 10% of total assets.

Dispersion of Problem Loans – 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 three data points exceeding 120% are not included in the graph above for aesthetic reasons.

Historical Comparisons

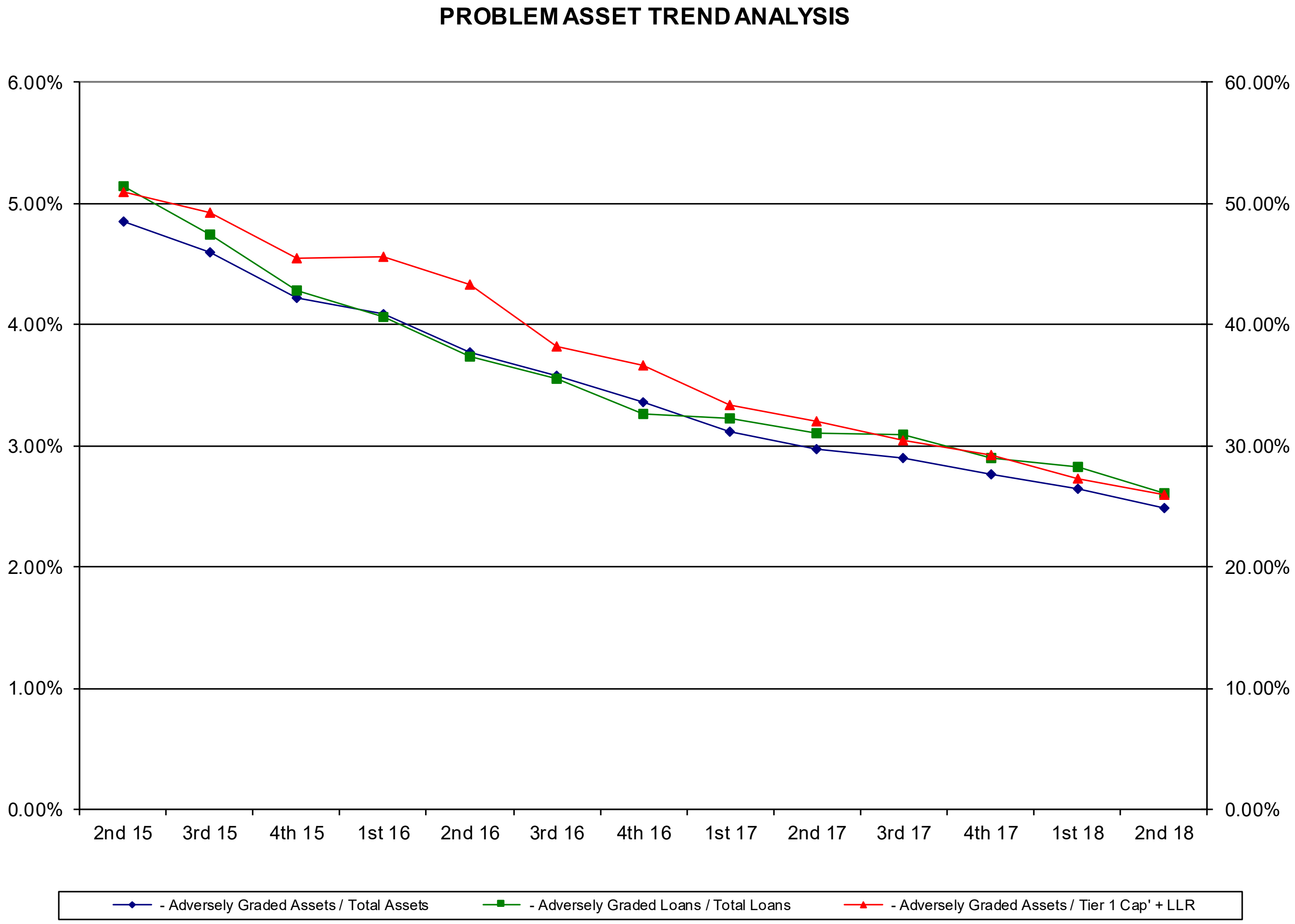
Our sample group includes seven (7) banks with problem assets exceeding 60% of tier-one capital plus loan loss reserve. This number compares to:

- Eight (8) during the First Quarter 2018
- Ten (10) during the Fourth Quarter 2017
- Ten (10) during the Third 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 First Quarter 2018
- Five (5) during the Fourth Quarter 2017
- Five (5) during the Third 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.

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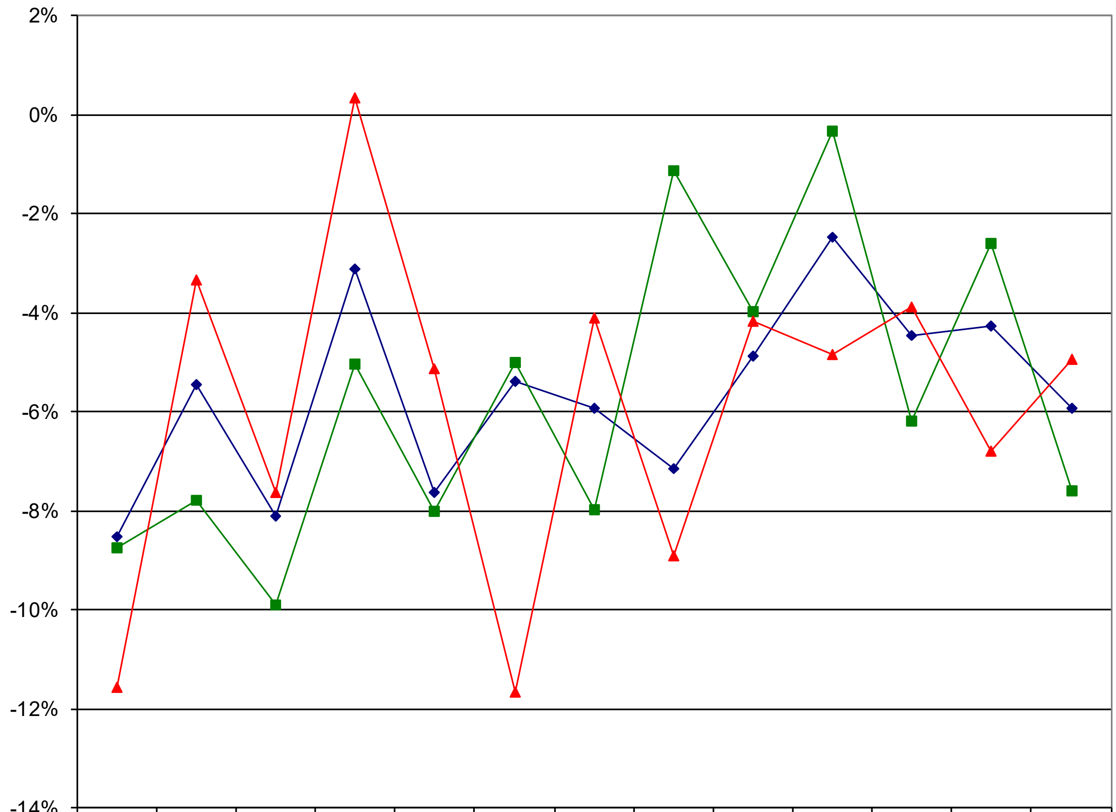
Problem Asset Comparative Change Analysis

COMPARATIVE % CHANGE IN ADVERSELY CLASSIFIED ASSETS
Comparative to Assets, Loans and Tier One Capital + LLR



	2nd 15	3rd 15	4th 15	1st 16	2nd 16	3rd 16	4th 16	1st 17	2nd 17	3rd 17	4th 17	1st 18	2nd 18
% Change in ACA/TA	-8.53%	-5.44%	-8.10%	-3.13%	-7.62%	-5.40%	-5.94%	-7.14%	-4.89%	-2.48%	-4.47%	-4.28%	-5.93%
% Change in ACL/TL	-8.76%	-7.79%	-9.90%	-5.04%	-8.02%	-5.01%	-7.99%	-1.13%	-3.98%	-0.35%	-6.19%	-2.61%	-7.60%
% Change in ACA/Tier 1 Cap' + LLR	-11.57%	-3.33%	-7.63%	0.35%	-5.13%	-11.66%	-4.12%	-8.90%	-4.19%	-4.83%	-3.90%	-6.81%	-4.93%

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 2.26% of total assets, 2.54% of total loans, and 20.20% of tier-one capital plus loan loss reserve. Second Quarter 2018 modified data compares to the following First Quarter 2018 modified average data set:

- 2.43% of total assets
- 2.79% of total loans, and
- 21.69% of tier-one capital plus loan loss reserve

Senior Loan Officer Opinion Survey

The Federal Reserve recently published their July 2018 Senior Loan Officer Opinion Survey. The survey encompassed 72 domestic banks and 22 U.S. branches and agencies of foreign banks. The survey included a question regarding the "range over which their lending standards have varied from 2005 to the present, and where the level of standards on such loans currently resides, relative to the midpoint of that range".

- Current lending standards on all categories of C&I loans remained at levels that are at the easier ends of their respective ranges since 2005
- CRE lending standards for domestic banks, within most major categories, are reported at levels at the tighter ends of their ranges since 2005
- Banks reported that current lending standards are tighter than the midpoints on construction and land development loans and on loans secured by multifamily residential properties

Overall, respondents indicated a continuation of underwriting standards for most loans. Of note, some respondents indicated they had eased their standards and terms on commercial and industrial (C&I) loans: "moderate net shares of banks increased the maximum maturity of loans, reduced the cost of credit lines and premiums charged on riskier loans, and eased loan covenants on such loans". The reasoning for easing standards should be noted: "banks that reportedly eased standards or terms on C&I loans over the past three months cited increased competition from other lenders as a reason for easing."

While we are currently operating, as based on the previous decade, within the 'best of times', competition should not be the driving force to lessen underwriting standards or allow exceptions to bank policy.

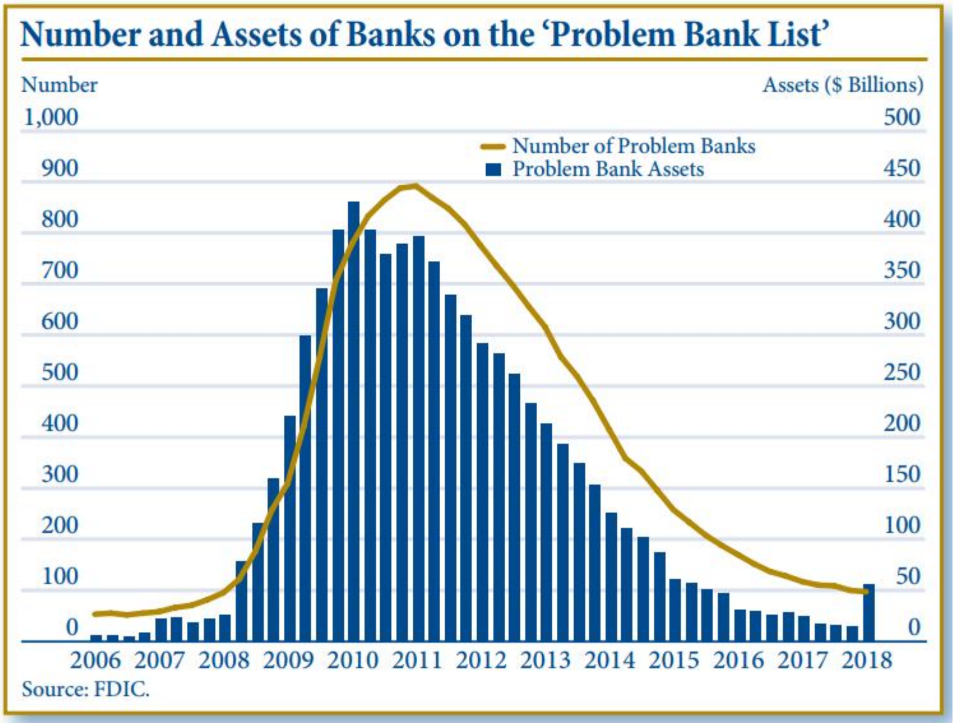
Quarterly Banking Profile

The most recent issue of the FDIC's Quarterly Banking Profile reported continued improvements in industry performance. The QBP contained indicated increasing loan loss reserve provisions. Of note the 3% increase (year over year) was "due to higher net charge-offs, and a growing loan portfolio". Encouragingly, charge-offs, have overall remained at 'normal' levels – 0.50%. Roughly 43% of all banks indicated a year over year increase in net charge offs. Loss reserves represented 110% of non-current loans.

As indicated by general past due data, it would appear industry asset quality continues to improve. Non-accruals and 90+ day past dues were 3.4% lower than the previous quarter. The following chart details various past due data as based on bank size as well as region:

		Asset Size Distribution					Geographic Regions*					
March 31, 2018	All Insured Institutions	Less Than $100 Million	$100 Million to $1 Billion	$1 Billion to $10 Billion	$10 Billion to $250 Billion	Greater Than $250 Billion	New York	Atlanta	Chicago	Kansas City	Dallas	San Francisco
Percent of Loans 30-89 Days Past Due												
All loans secured by real estate	0.66	1.20	0.64	0.38	0.52	0.94	0.51	0.75	0.66	0.96	0.62	0.36
Construction and development	0.38	0.74	0.51	0.43	0.31	0.34	0.49	0.41	0.20	0.40	0.39	0.37
Nonfarm nonresidential	0.32	0.94	0.47	0.29	0.23	0.37	0.37	0.22	0.31	0.44	0.37	0.21
Multifamily residential real estate	0.12	0.75	0.27	0.09	0.15	0.05	0.14	0.13	0.10	0.10	0.10	0.11
Home equity loans	0.66	0.78	0.49	0.38	0.50	0.85	0.53	0.79	0.72	0.71	0.48	0.31
Other 1-4 family residential	1.05	1.59	0.89	0.57	0.89	1.34	0.77	1.19	0.98	1.48	1.16	0.55
Commercial and industrial loans	0.29	1.22	0.65	0.46	0.25	0.25	0.24	0.23	0.29	0.30	0.48	0.37
Loans to individuals	1.32	1.66	1.20	1.29	1.23	1.42	1.14	1.76	0.97	1.31	0.83	1.32
Credit card loans	1.28	4.23	1.92	2.98	1.36	1.12	1.16	1.39	1.10	1.16	0.66	1.63
Other loans to individuals	1.37	1.61	1.16	0.99	1.07	1.72	1.10	2.13	0.92	1.55	0.91	1.04
All other loans and leases (including farm)	0.31	1.09	0.98	0.51	0.28	0.27	0.09	0.23	0.38	0.31	0.31	0.81
Total loans and leases	0.65	1.22	0.69	0.46	0.60	0.73	0.54	0.75	0.57	0.76	0.59	0.63
Percent of Loans Noncurrent**												
All real estate loans	1.60	1.25	0.88	0.74	1.27	2.63	1.27	2.00	1.80	2.34	1.04	0.48
Construction and development	0.47	0.95	0.98	0.58	0.27	0.31	0.51	0.72	0.43	0.38	0.37	0.39
Nonfarm nonresidential	0.61	1.47	0.78	0.61	0.53	0.59	0.72	0.59	0.66	0.64	0.60	0.39
Multifamily residential real estate	0.15	1.03	0.44	0.15	0.11	0.10	0.15	0.18	0.15	0.15	0.25	0.07
Home equity loans	2.45	0.41	0.57	0.62	1.27	3.99	2.33	3.09	2.38	2.91	1.06	0.63
Other 1-4 family residential	2.61	1.26	0.97	1.11	2.32	3.63	2.07	3.03	2.69	3.81	2.10	0.57
Commercial and industrial loans	0.85	1.57	1.09	1.51	0.92	0.65	0.83	0.71	0.76	0.80	1.51	1.07
Loans to individuals	0.96	0.85	0.66	0.85	1.13	0.79	1.06	1.08	0.55	0.93	0.82	1.02
Credit card loans	1.40	2.68	1.69	2.99	1.53	1.17	1.33	1.45	1.18	1.23	1.26	1.80
Other loans to individuals	0.51	0.82	0.60	0.47	0.60	0.42	0.64	0.72	0.30	0.47	0.62	0.33
All other loans and leases (including farm)	0.22	1.13	0.87	0.44	0.29	0.12	0.22	0.15	0.15	0.27	0.36	0.39
Total loans and leases	1.15	1.24	0.89	0.85	1.06	1.37	1.04	1.28	1.17	1.41	1.07	0.71

Trends in SHP & Co. client data seems to mirror that within the overall industry. Please refer to the newsletter's graphs and asset quality details. The QBP reflects a 3% decline in the number of banks on the FDIC's 'Problem Bank List' – currently 92% as compared to 95% previously.



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

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