

Value: The Community Bank Wall Street Report



ACBQ • CAPITAL MARKETS • ACB INVESTOR CONFERENCES

Vol. II, No. 5
August 2006

You're Invited To NASDAQ Close

Join us and be part of the live audience at the NASDAQ Marketsite as ACB closes the market on November 1.

The market close ceremony precedes the Investor Relations Bootcamp at the New York Westin hotel, and the IR Conference presentations on November 2 by member companies of the ACB NASDAQ Index.

3:15 p.m. to 4:00 p.m. The NASDAQ market close event at the NASDAQ Marketsite, 43rd & Broadway. (RSVP required).

4:15 p.m. to 6:30 p.m. Investor Relations Bootcamp at the New York Westin.

4:15 p.m. to 4:45 p.m. Effective IR Programs. Van Negris, president and CEO, Van Negris & Company on achieving a higher profile for your company.

4:45 p.m. to 5:15 p.m. The Nasdaq Stock Market and Your Listing.

5:30 p.m. to 6:30 p.m. Community Bank Investor Panel. Community bank stock analysts and investors will provide insight on how they evaluate companies for recommendation and purchase.

Contact Helen Sullivan at hsullivan@acbankers.org or (202) 857-3157 to participate.

ACB Index Continues To Rise in Volatile Market

The America's Community Bankers NASDAQ Index has held up extraordinarily well during the period of market volatility that began in late April and early May. While the ACB index showed an increase, the three indexes ACB uses for comparison were all down.

The ACB index year-to-date performance increased from 4.76 percent at the end of

April to 6.59 percent at the end of July.

During the same end-of-April to end-of-July period, the NASDAQ Composite dropped from an increase of 3.72 percent to a negative 4.81 percent. The S&P 500 declined from 5.61 percent to 3.34 percent and the Russell 3000 was down from 6.46 percent to 3.13 percent. See more comparisons on page 3. «

NASDAQ Online: Info At Your Fingertips

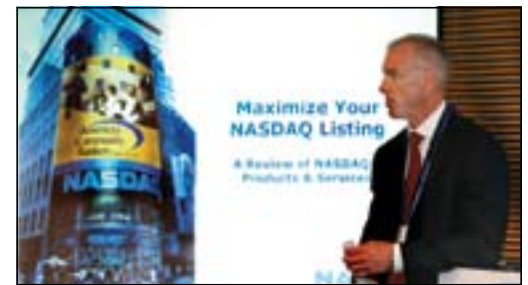
By John Koegel

For community banks looking to diversify their shareholder base and attract more investment from mutual funds, pension funds and other institutional owners, identifying prospective investors can be a time-consuming and challenging task - unless, of course, the banks are listed on the NASDAQ Stock Market.

"NASDAQ delivers unmatched support for NASDAQ-listed companies by providing access to innovative products and services that facilitate transparency, mitigate risk and inspire better corporate governance," said John Shipley, a managing director with NASDAQ's Corporate Client Group, who ad-

dressed bankers attending America's Community Bankers' Investor Relations Boot Camp in New York in May. "Companies that list on NASDAQ have the benefit of a portfolio of exceptional services and information programs geared to provide value in all stag-

Continued on page 2



2Q Roundup, 2006 Outlook for Banks, Thrifts

By Richard D. Weiss, senior analyst, Janney Montgomery Scott, Philadelphia



Banks will be challenged to power growth throughout 2006 as funding costs are likely to rise without a commensurate increase in the average yield of interest-earning assets. More balance sheet restructuring is likely as banks try

to adjust to higher short-term interest rates and the flat yield curve.

We also foresee good loan growth as business lending strengthens further and residential mortgage loan prepayments stay low. Credit quality continues to be solid. However, we doubt that companies are setting aside sufficient reserves and that earnings will be more volatile in future periods when asset quality problems eventually surface.

Continued on page 4

Continued from page 1

es of going public and being public.”

One of the benefits NASDAQ offers its listed companies is a user-friendly Web-based tool called NASDAQ Online. Designed as a strategic equity management resource to facilitate the practice of investor relations, NASDAQ Online includes a wealth of data and online applications. It includes current and historical stock and index prices, fundamental company data, ownership information, targeting tools and analyst research and forecasts. The basic level of service is available to all NASDAQ-listed companies at no additional charge.

“We aggregate millions of dollars of data,” said Shipley. “One of the ‘sticky apps’ that companies use again and

again is the ownership page, where they can see their list of owners, individual as well as institutional, and then see momentum, as investors increase or decrease their ownership positions.”

With this information in hand, companies can compare their shareholders to the shareholders of their peer group, and then develop a proactive investor relations program.

“You may want to reach out to institutions that own your peers, but do not own your bank,” said Shipley. “You can get your story in front of those institutions.”

Most of the data in NASDAQ Online is updated quarterly from Securities and Exchange Commission filings, but listed companies can also contact NASDAQ’s Market Intelligence Desk for real-time

information to find out who’s trading their stock and what today’s volume is like.

NASDAQ Online also enables listed companies to compare their stock performance against competitors as well as more than 200 stock indices. In addition, the online resource provides analysts’ earnings forecasts, recommendations and research reports, so that listed companies can learn what Wall Street is saying about their stock.

One of the most popular features of NASDAQ Online is its ability to generate a wide range of presentation-quality reports. “A lot of companies will put these reports in the board package each month for their directors,” said Shipley. “It’s a big time-saver and tremendous value-add.” ◀

It’s All in the Name for Connecticut Bank and Trust Company

By John Koegel

There aren’t many banks like The Connecticut Bank and Trust Company (NASDAQ: CTBC).

A publicly traded commercial community bank in a state dominated by thrifts and large financial institutions, CBT, as it is known, took the name of a defunct 200-year-old New England bank that had been revered by former customers and employees.

When the “new” CBT opened its doors for business in March 2004, with three branches in north central Connecticut, it had little trouble attracting customers. And when CBT went public five months later, it raised \$18.5 million in just 76 days - a state record. A second public offering in 2005 yielded \$16 million more, providing the Hartford-based de novo bank with enough capital to bring its total number of branches to seven by early 2007.

David A. Lentini, president and CEO of the \$100-million CBT, likes to describe his bank as serving the “bottom” of the commercial lending market.

“At one time there were 160 banks in Connecticut. Today, there are 63, and most are thrifts. The next-largest commercial bank that we compete against has \$1 billion in assets, and the one above that is \$7 billion,” he says. “So we

feel there’s tremendous opportunity at the bottom of the market for a commercial bank where you can call and talk to the president.”

Investors apparently agree. Even though CBT has yet to show a profit,



about 25 percent of its shares are held by institutional investors, including a \$35-billion mutual fund. More investors are discovering CBT since it moved from the OTC Bulletin Board to the NASDAQ Stock Market in January.

“For companies our size, NASDAQ requires a year of operating history, so we waited until we had that,” explains Lentini. “Since moving over to NASDAQ, our daily volume has gone from 200 shares to over 2,000 shares, making the stock more liquid. Plus the Hartford Courant

has been able to pick up our listing automatically, so we’re in the newspaper everyday, which makes it easier for our stockholders to follow the stock.”

Lentini and his colleagues celebrated their new listing by ringing the NASDAQ closing bell on March 1. The bank became a member of the ACB NASDAQ Index on June 1.

And about the bank’s name? “The original Connecticut Bank and Trust Company merged with The Bank of New England in 1983,” says Lentini, who worked for the first CBT for 21 years. “When The Bank of New England failed in 1991, the FDIC used its right of offset to sell it to Fleet Bank, which elected not to protect CBT’s name, so we bought it. We have the same logo, the same culture, the same way of doing business.”

Lentini reminds people that his bank is not the same CBT that they remember, but that does not appear to matter to the marketplace.

“We did market surveys and found out that eight out of ten people either worked for, banked with or remembered CBT, so we felt we had a good brand to work with,” he says. “As a result, we don’t have to advertise the name as much. We can do more product advertising.”

At CBT, that spells success. ◀

Comparison of ACB NASDAQ with Selected Indexes

Index	YTD '06	2005	2004	Cumulative*
ACB NASDAQ	6.59%	0.53%	18.44%	27.90%
NASDAQ Composite	-4.81	3.27	8.99	9.79
S&P 500	3.34	4.91	10.88	NA
Russell 3000	3.13	5.98	11.94	28.04

As of July 31, 2006. Total return basis. *Since inception of ACB NASDAQ Index, 12/5/2003.

Mitigating Risk Through Intrusion Testing

By Matt Rodger, business advisory services audit manager, Grant Thornton LLP



As the Internet has become indispensable to businesses and consumers, it is now more important than ever for businesses to be aware of the power of the Internet and how to leverage it to advantage in the competitive marketplace.

While bankers recognize that the Internet is an important delivery channel for new products and services, they are also acutely aware that customers and regulators expect and require effective policies to help assure that their websites are secure, protected from hackers and resistant to computer viruses.

According to Grant Thornton's 13th Annual Survey of Bank Executives (2006), even though 83 percent of bankers say that verifying their systems' operations and controlling their technology risks is important, only 59 percent say they are confident about their strengths in this area. Furthermore, the three operational issues survey participants most frequently identified as important to their ongoing success are protecting customers' privacy (91 percent), assuring security of Internet services (91 percent) and assuring quality of financial reporting (85 percent).

According to Grant Thornton's 13th Annual Survey of Bank Executives (2006), even though 83 percent of bankers say that verifying their systems' operations and controlling their technology risks is important, only 59 percent say they are confident about their strengths in this area. Furthermore, the three operational issues survey participants most frequently identified as important to their ongoing success are protecting customers' privacy (91 percent), assuring security of Internet services (91 percent) and assuring quality of financial reporting (85 percent).

The Intrusion Risk Assessment Plan

When developing an intrusion risk assessment plan, one of the first steps is to identify possible costs that can result from a security breach. These costs typically stem from transaction risk, compliance risk, strategic risk and reputation

risk. They may stem from litigation and regulatory sanctions arising from a financial institution's failure to use due diligence in safeguarding Internet banking services and confidential customer information.

Risks of Internet-based transactions include spoofing; unauthorized disclosure of confidential information; unauthorized action, including denial of service; and interception and data alteration. Hackers use these techniques to deny services to clients, compromise the privacy of customer data or cause system malfunctions.

To mitigate these risks, bank management needs to identify and rate the risks specific to its organization, determine the critical functions necessary to continue business operations, define controls that are currently in place to reduce organizational exposure and evaluate the cost of these controls.

The final result is a security plan that describes the institution's security posture. This plan should be reviewed and updated periodically as the bank's security needs change.

Risk Mitigation Controls

Various controls that banks may opt to use to diminish risk include encryption and two-factor authentication schemes.

Several other important factors to deter hackers include maintaining software integrity, minimizing the number of system components and services required to perform necessary functions and using caution when allowing remote dial-up access to the internal network. Once these steps are taken, controls such as an intrusion detection system and firewalls can further secure a system from hackers.

Intrusion Response Policies, Procedures

If an intrusion occurs, it is imperative for management to quickly begin damage assessment and recovery activities. Having a disaster recovery plan in place will ensure there is a sequence of steps management can take to more effectively contain and remediate the intrusion. Some of these precautions include assigning appropriate staff members to respond to intrusions, following incident response procedures and filing a suspicious activity report.

Staff Training and Procedures

The final step in an effective intrusion risk management plan comes with empowering bank employees with security awareness, the result of which is a safer, more reliable electronic banking environment. Some pertinent topics to incorporate in training include: written security policies and procedures, applicable laws and regulations, procedures for reporting possible intrusions and sanctions for non-compliance. New employee orientation is a good time to begin this training, and this training should be repeated annually.

Management should also ensure that Internet banking systems and related networks are tested regularly to identify vulnerabilities and mitigate the risk of intrusion.

By following these basic steps, banks should be able to draft and implement IT security policies and procedures that meet the minimum requirements to protect customers and the bank.

To receive a free copy of Grant Thornton's *Intrusion Testing Manual for Financial Institutions*, please e-mail financialservices@gt.com, call toll free at (877) 835-1723, or visit www.GrantThornton.com/intrusion. «

Get Noticed By Wall Street: Write Your Own Research Report

Obtaining coverage from securities analysts is an elusive goal that is becoming harder and harder to achieve for many publicly traded community banks.

Consolidation in the brokerage industry has meant there are fewer analysts, with less time, to follow greater numbers of newly minted public companies. Throw Regulation FD and other new corporate governance rules into the mix, and it's easy to see why community banks – and other public companies – can have a difficult time getting on Wall Street's radar.

Van Negris, senior managing director of Van Negris & Company, Inc., a New York strategic advisory firm and pre-

sender at America's Community Bankers' Investor Relations Boot Camp, suggests that community banks seeking attention from analysts and investors consider producing their own version of a traditional investment research report, which could be called a "quarterly financial review."

The key is to repackage and present the bank's financial information in a research report format that is familiar to and valued by the financial community. The document would resemble a typical Wall Street analyst's report and contain only legally approved information taken from the 10-K, 10-Q, annual report, press releases and other related documents.

Instead of financial projections, there would be historical financials, presented in the format of an analyst's model, with fill-in-the-blanks to accommodate future earnings announcements. There could also be a discussion of management's vision, goals, growth plans and expectations, where appropriate.

The document could then be mailed with a cover letter from the chief executive officer to analysts and investors who follow similar banks, offering to meet or answer questions about the information in the report.

Your own research report is an effective way to begin to get noticed by analysts and investors alike. «

Continued from page 1

Earnings

For the quarter ending June 30, 2006, the reported median year-over-year earnings per share growth rates versus the same period a year ago (for essentially the same companies) were: for mid-cap banks, 3.8 percent vs. 10.4 percent; for small-cap banks, 0.0 percent vs. 10.0 percent; and for thrifts, -0.7 percent vs. 16.7 percent. Intense pricing competition regarding both lending and deposit gathering, exacerbated by the flat yield curve, was the primary factor for the earnings growth slowdown.

The more subtle reason for the feeble year-over-year earnings comparison is that 2005 reported earnings were inflated by the overall decline in loan loss provisioning. Companies generally reduced loan loss provisions to accommodate Securities and Exchange Commission and auditor demands, rather than to reflect loan charge-offs or higher non-performing assets.

Stock Performance

Bank and thrift stock price performance was generally lackluster over the first half of 2006, as generally high bank stock valuations and the challenges posed by the flat yield curve dampened

investor enthusiasm. As of July 31, 2006, the median year-to-date price increases were 2.2 percent for mid-cap banks; 2.7 percent for small-cap banks; and 3.2 percent for thrifts. We view 5 percent core earnings growth expectations as reasonable for much of the group, and consider many of the valuations to be fully priced based on projected core earnings growth rates.

Valuations

Bank valuations have not changed much over the past year despite significantly slower growth rates. As of July 31, 2006, mid-cap banks traded at 14.7 times vs. 15.1 times at the same time last year; small-cap banks at 15.3 times vs. 15.9 times; and thrifts at 15.9 times vs. 15.1 times. On an earnings basis, banks trade at nearly the same multiple as the S&P 500 Index, which trades at 15.3 times estimated 2006 earnings compared with the historical range of approximately 55 percent to 80 percent.

We believe that bank valuations remain rich due to the prevalent opinion that the end is near regarding Federal Reserve interest rate hikes, an investor preference for stocks that pay attractive dividends given the more favorable tax treatment, and merger speculation. These factors, rather than improved

fundamentals, have contributed to the approximately 2.5 percent to 3.0 percent year-to-date increase in bank stock prices.

There is little differential between mid-cap and small-cap banks and thrifts versus a historical 1.0-3.0x multiple premium for banks. We believe the odds favor multiple contraction to 12-13 times forward earnings from today's elevated levels, given less earnings momentum.

Outlook

The economic outlook remains uncertain and interest rate forecasts seem to change on a daily basis. The prolonged flatness of the yield curve has caused much of the industry to aggressively seek loan growth, which has heightened competition and caused even more pricing pressure.

Revenue growth is challenging as net interest margins remain under pressure. Deposit rates, which typically lag market interest rates, should continue to rise over the next few quarters given the upward movement of short-term interest rates. We believe banks and thrifts, in general, will be fortunate to retain core deposits when rates go up versus actually growing them, because of the availability of higher-yielding alternative investments. «

Value: The Community Bank Wall Street Report is a monthly publication of America's Community Bankers, 900 19th St., N.W., Washington, D.C. 20006. Diane Casey-Landry, president and CEO; Jim Eberle, editor; Debra Cope, Helen Sullivan, contributing editors; John Koegel, contributing writer. Copyright 2006, America's Community Bankers. To contact ACB, call (202) 857-3100 or e-mail info@acbankers.org.