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Active Bank Consolidation Can Work Well for Investors

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Over time, the history of bank mergers has had its up and downs, largely fluctuating with the economic cycle, as well as changing dynamics in pricing and social factors. Recently, investors have become more critical of bank consolidation, particularly as we approach an eventual recession. In addition the universe of buyers has shrunk considerably.

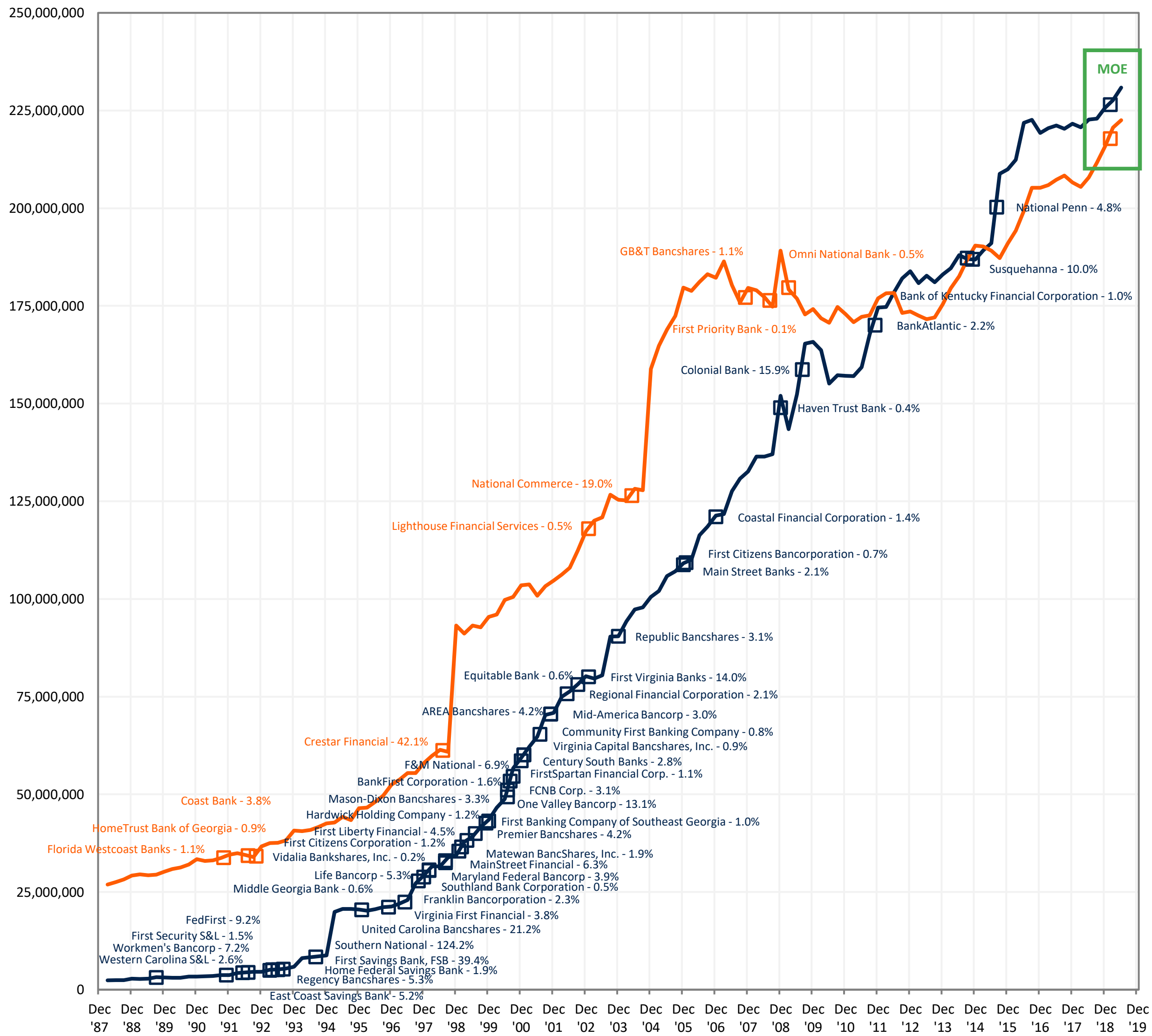
However, there are clear examples of outperformance for those who utilize disciplined acquisition models over the long-term, often besting peers primarily reliant on organic growth. We believe organic growth is critically important to valuation but also believe in combination with a well-executed acquisition and integration model, with reasonable risk limits and sensible pricing, results can be even very powerful.

One of the most successful active acquisition models also happens to be a prominent, large Mergers-of-Equals partner due to close shortly. The long-term historical perspective for these two partners, in comparison, carries a strong acquisition advocacy message well worth examining. While both arrived at similar asset footprints at the time of their announcement this past February, their journey was very different.

Sun Banks of Florida and Trust Company of Georgia formed SunTrust in 1985. The straightforward logic at the time was to combine a strong source-of-funds bank market (Florida) with an equally strong use-of-funds market (Georgia.) By early 1988, SunTrust was $26.9B in assets while BB&T, at $2.4 billion, was less than 10% of SunTrust's size.

Since 1988, and spanning three recessions, BB&T remarkably closed forty-nine whole bank acquisitions to SunTrust's eleven, allowing it to meet and slightly surpass SunTrust's asset base, making this MOE possible. The following exhibit captures the difference in consolidation activity and scale building.

BBT vs. STI Assets ($000s)

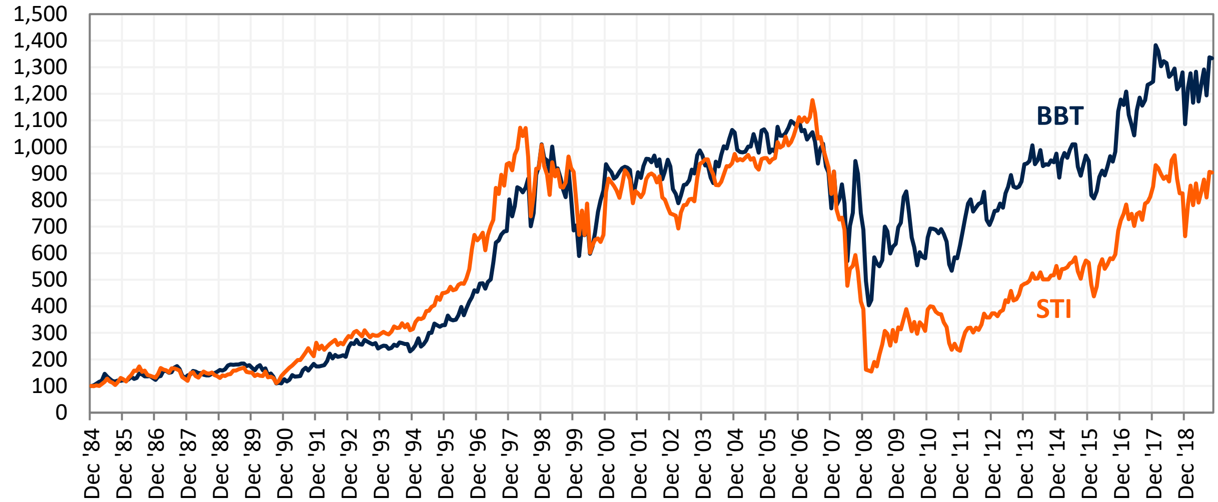


Source: S&P Global Market Intelligence, Sandler O'Neill

By late 2013 BB&T's assets had finally caught up with SunTrust, after growing at a 15.7% CAGR against 7.0% for SunTrust. But the real eye-opener is that book value and total shareholder return also outpaced SunTrust. BB&T's organic growth coupled with its active acquisitioning model did not dent shareholder returns while massively expanding asset scale.

In fact over the last three decades, BB&T's book value grew at a 7.8% CAGR against SunTrust's 6.9% CAGR. Moreover, since 1992 BB&T grew tangible book value also at a respectable 5.6% CAGR, edging out SunTrust's 5.4% pace. On total shareholder return the difference is even more impressive at 11.2% versus 9.2% for SunTrust. So much for not being able to consistently and quickly earn back book dilution and generate recurrent EPS accretion on the journey to advance scale.

BBT vs. STI Stock Price (Indexed)



Source: FactSet

BB&T started subscale to say the least. The idea that it would one day rival SunTrust, let alone make an MOE desirable, would have been scoffed at throughout most of its history, from its late 1980s size relative to SunTrust at 10%, expanding to only half in the mid-1990s, and two-thirds prior to the 2008-09 recession. BB&T leaped to 80% mid-recession while SunTrust gave up growth and suffered greater losses. BB&T attained asset parity five years later.

The average acquisition size for SunTrust's far fewer transactions was $6.1 billion, more than twice that of BB&T at $2.8B. BB&Ts largest transaction as a percent of assets was 124% with Southern National in 1994 (in this report we are using Southern National for the data prior to 1995), early in its expansion. Crestar was SunTrust's largest at 42% of assets. Interestingly, excluding the two largest acquisitions for each, BB&T's average size was $2 billion, above $820 million for SunTrust

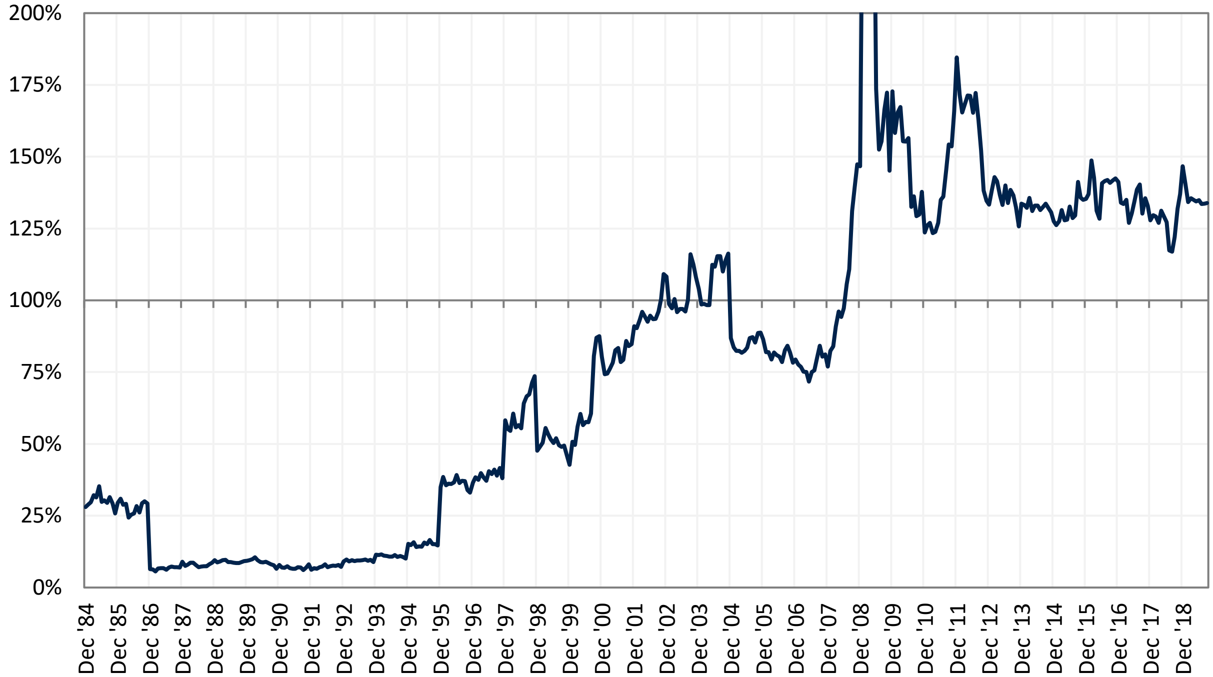
BB&T's overall asset expansion from bank acquisitions was $134 billion or 48% of current assets against SunTrust's overall asset expansion from bank acquisitions of $55 billion or 25% of current assets. (All the above for both are from whole bank transactions and exclude branch purchases and nonbank activity.)

Finally, during this period BB&T averaged 13.0% return on equity against SunTrust's 11.3% and did so with less profit volatility. The efficiency ratio at BB&T also exceeded SunTrust, averaging 56% versus 62% over the period.

It is important not to view this history as demeaning SunTrust in any way. Most investors would agree that SunTrust built one of the most impressive banking franchises across the Southeast. The point of reviewing this history is that active acquisitioning can produce even better returns than one of the best in the banking business.

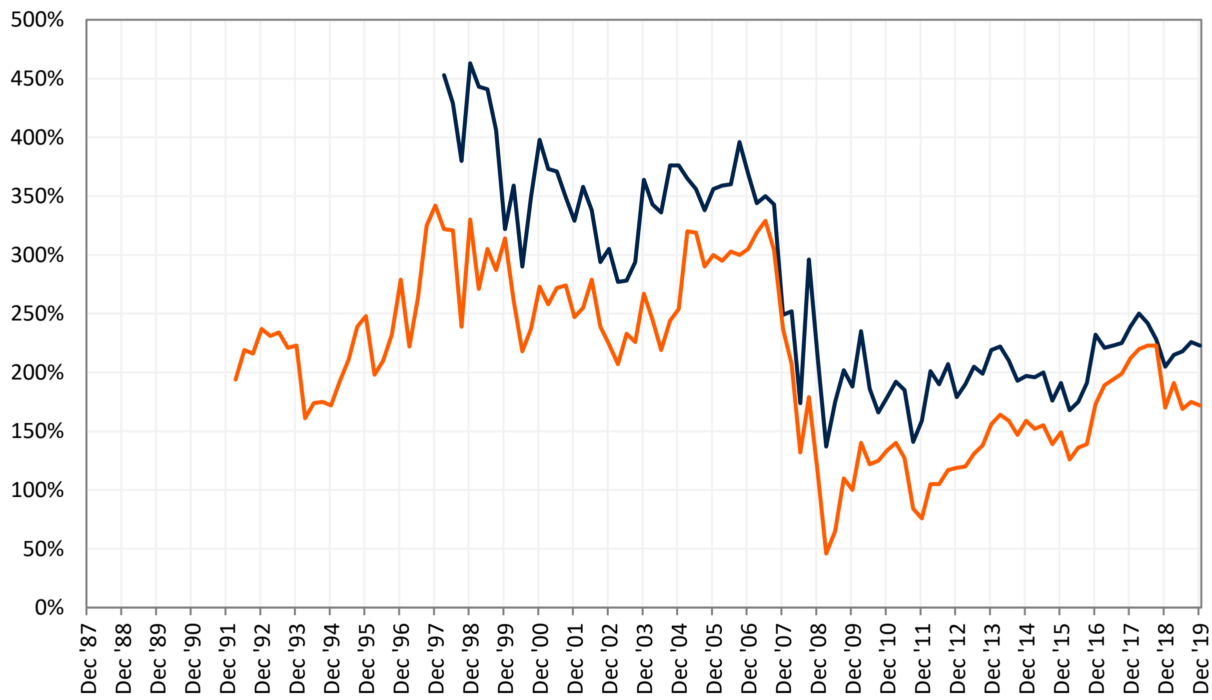
Steady consolidation as a business line works.

BBT Market Value as a % of STI Market Value



Source: S&P Global Market Intelligence, Sandler O'Neill

BBT vs. STI P/TBV



Source: FactSet

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