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West Town Bancorp, Inc. (WTWB - OTC Pink)

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John A. (Buddy) Howard, CFA
May 13, 2017

Price:	\$24.50	EPS *	2015A:	\$ 2.83	P/E	2015A:	8.7 x
52 Wk. Range:	\$18.75 - \$25.75	(FY: DEC)	2016A:	\$ 1.24		2016A:	19.8 x
Div/Div Yld:	\$0.00 / 0.0%		2017E:	\$ NA		2017E:	NA
Shrs/Mkt Cap:	1.5 mm / \$36 mm	Book Value:		\$ 20.01	Price/Book Value:		1.22 x

* EPS are diluted. 2017 earnings projections are temporarily suspended due to pending transaction with Sound Bank.

Background

With \$275 million in assets, West Town Bank & Trust is a North Riverside, IL based state chartered bank. The Bank provides banking services through its offices in Illinois and North Carolina and also maintains loan production offices in North Carolina, New York, Maryland, Pennsylvania, Florida, Idaho and New Jersey. Its primary deposit products are checking, savings, and time certificate accounts, and its primary lending products are residential mortgage, commercial, and installment loans. The Bank also engages in mortgage banking activities, originating and selling one-to-four family residential mortgage loans in multiple states. The Bank's primary regulators are the Illinois Department of Financial and Professional Regulation and the FDIC. The Company recently announced its intention to merge with Sound Banking Company.

The First Quarter Was Particularly Significant From a Strategic Standpoint

West Town Bancorp reported commendable financial results in the first quarter of 2017, with earnings that posted a nice increase from the year-ago numbers. However, it was really other factors that we considered to be most significant, most notably the announcement on February 17, 2017 that the Company was acquiring Sound Banking Company ("Sound Bank"), as well as the closing (also in February) on a 43.5% ownership stake in Windsor Advantage, a Chicago based company that provides a comprehensive suite of services involving SBA and USDA lending. We view both of those acquisitions as being highly complementary to West Town's existing operations, as they play off of West Town's key capabilities. Also, while the Windsor Advantage purchase is a minority interest, West Town has a three-year option to purchase the remaining interest on essentially the same terms, which gives us comfort that this operation will become a permanent and meaningful differentiator in West Town's future. The fact that the Company has put together this combination of companies and capabilities is, in many respects, a testament to the entrepreneurial vision of West Town's management team.

But getting back to the financials, net income in the first quarter of 2017 was \$879,000, or \$0.57 per diluted share, versus \$788,000, or \$0.55 per diluted share, in the year-ago quarter. There were a few nonrecurring items in the numbers, the main one being \$172,000 in merger-related charges, although those costs were partly offset by \$145,000 in gains/recoveries on foreclosed assets. Bottom line, though, it was a solid quarter, where net interest income was up sharply and expenses were held in check, the result being that profitability increased despite a higher provision. And of course, the profitability metrics were quite impressive, as they typically have been at West Town. For example, the annualized return on average equity in 2017's first quarter was 12.57%, versus 12.82% in the year-ago quarter, while the annualized return on average assets was 1.31%, versus 1.44% in the year-ago quarter.

The main driver of the higher earnings was net interest income, which was up 26% to \$2.7 million in 2017's first quarter, versus \$2.2 million in 2016's first quarter. From an investor's standpoint, one of

ASSETS: \$275 MM

HQ: NORTH RIVERSIDE, IL

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1ST QUARTER HIGHLIGHTS:

**THE SOUND BANKING DEAL
WAS ANNOUNCED AND THE
WINDSOR ADVANTAGE
INTEREST WAS ACQUIRED IN
THE FIRST QUARTER**

EPS: \$0.57 VS. \$0.55

**THERE WERE MERGER-
RELATED EXPENSES IN 2017'S
FIRST QUARTER, WHICH WERE
PARTLY OFFSET BY OREO
RECOVERIES**

ROAE: 12.57%

ROAA: 1.31%

**NET INTEREST INCOME WAS
STRONG, INCREASING 26%,
ALL OF WHICH WAS VOLUME
BASED**

NONINTEREST INCOME DECREASED DUE TO SOFTNESS IN THE MORTGAGE AREA AND LOWER FAIR VALUE ADJUSTMENTS TO MORTGAGE SERVICING RIGHTS

GOVERNMENT LENDING REVENUE, HOWEVER, WAS STRONG, INCREASING 47%

EXPENSE CONTROL WAS EXCELLENT, WITH NONINTEREST EXPENSE DECLINING FROM THE PREVIOUS YEAR

ORGANIC GROWTH HAS BEEN COMMENDABLE, WITH LOANS UP 8% IN THE PAST YEAR, AND DEPOSITS GROWING 30%

WEST TOWN CLOSED ON ITS ACQUISITION OF A 43.5% STAKE IN WINDSOR ADVANTAGE

THE SOUND BANKING DEAL IS EXPECTED TO CLOSE IN THE THIRD QUARTER OF THIS YEAR

THERE ARE A NUMBER OF ADVANTAGES THAT ARE EXPECTED FROM THE TRANSACTIONS

NPAS/ASSETS: 1.48%

RESERVES/LOANS HFI: 1.44%

EPS:
2015A: \$2.83
2016A: \$1.24
2017E: NA

the key aspects of West Town's performance is its ability to generate high-quality loan growth. In our view, there are few more critical functions of a bank than this, as it tends to drive long-term earning asset growth. And in this regard, West Town has built, and continues to build, its "origination engine," which includes not only relationships but also systems and platforms (such as Windsor) that are highly scalable. That success in growing loans (and low-cost deposits, which has also fueled increases in West Town's investments) over the past year accounts for essentially all of the net interest income growth, as margins were unchanged at 4.39%. Noninterest income was lower, decreasing to \$3.6 million in 2017's first quarter from \$4.0 million in the year-ago quarter, principally as a result of a drop in mortgage revenue (reflecting lower originations) and a decline in the fair value adjustment on mortgage servicing rights (the latter being driven mainly by loan mix and faster prepayment assumptions). Offsetting much of that weakness, though, was the growth in government lending revenue, which increased 47% to \$1.6 million in 2017's first quarter, versus \$1.1 million in the year-ago quarter. We expect the trends in organic noninterest income to become stronger as 2017 progresses. As was stated in our opening paragraph, cost containment was another reason for the improved earnings, as noninterest expense was lower at \$4.4 million in 2017's first quarter, versus \$4.5 million in the year-ago quarter. Finally, we would note that the growth in earnings was achieved despite an increase in the provision for loan losses to \$276,000 in the first quarter of 2017, versus \$123,000 in the year-ago period.

Balance Sheet Growth Was Strong As Well – All of Which Was Organic

While West Town will significantly increase its size as a result of the Sound Bank acquisition, it continues to achieve solid organic growth. Gross loans held for investment increased 8% to \$176 million at March 31, 2017 from \$163 million at March 31, 2016, while assets over the past year were up 20% and deposits increased 30%. The Company's capital position remains strong, as the equity-to-assets ratio was 10.7% as of March 31, 2017.

Update on Acquisitions

As was stated previously, West Town closed on the purchase of the 43.5% interest in Windsor Advantage in 2017's first quarter, and the acquisition with Sound Bank is expected to close in 2017's third quarter. We view both of these two acquisitions as uniquely enhancing West Town's franchise. We have identified a few of the expected benefits from the transactions in the adjacent table.

Anticipated Benefits From Acquisitions to West Town ("WTWB")	
Windsor Advantage ("WA")	Sound Bank ("SB")
Vertical integration <ul style="list-style-type: none">- Operating efficiencies- Better quality/control of process	Low cost funding source <ul style="list-style-type: none">- SB's cost of funds is lower than WTBW
Differentiator in market <ul style="list-style-type: none">- Turn key solution- 75 lending partners in 27 states- Potential strategic relationships with existing and new WA clients/lenders	Broadens franchise <ul style="list-style-type: none">- Expands franchise in Eastern NC- Opportunities to market mortgages
Critical mass <ul style="list-style-type: none">- Boosts WTBW's asset size to ~ \$0.5 BB- Cost saving initiatives- Potential higher valuation from larger size; possible broader sponsorship from the investment community	

Asset Quality Continues to Improve

At March 31, 2017, nonperforming assets (including nonaccruing loans, accruing loans more than 90 days past due and OREO) were \$4.0 million, or 1.48% of assets, versus \$4.3 million, or 1.54% of assets, at December 31, 2016 and \$3.6 million, or 1.55% of total assets, at March 31, 2016. The allowance for loan losses totaled \$2.5 million, or 1.44% of loans held for investment, at March 31, 2017, as compared to \$1.9 million, or 1.14% of loans held for investment, at the year-ago date.

Projections Temporarily Suspended Until Merger Is Completed

Given the upcoming merger with Sound Banking Company, we are temporarily suspending our earnings projections. We will resume publishing projections once the transaction is completed.

ADDITIONAL INFORMATION UPON REQUEST

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