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## Potomac Bancshares, Inc. (OTC Pink - PTBS)

5003 Falls of Neuse Road

Raleigh  
North Carolina  
27609

919-876-8868 ph

[www.equityresearch.com](http://www.equityresearch.com)

**John A. (Buddy) Howard, CFA**  
November 26, 2017

<b>Price:</b>	\$12.96	<b>EPS *</b>	<b>2016A:</b>	\$ 0.66	<b>P/E</b>	<b>2016A:</b>	17.1x
<b>52 Wk. Range:</b>	\$8.75 - \$12.99	(FY: DEC)	<b>2017E:</b>	\$ 1.05		<b>2017E:</b>	19.6x
<b>Div/Div Yld:</b>	\$0.28 /2.2%		<b>2018E: *</b>	\$ 1.16		<b>2018E:</b>	12.5x
<b>Shrs/Mkt Cap:</b>	3.3 mm / \$43 mm	<b>Book Value:</b>		\$10.69	<b>Price/Book Value:</b>		1.21x

\* Diluted. 2017 earnings estimate excludes \$0.20 per share in life insurance proceeds, as well as a \$0.06 securities gain.

### Background

Founded in 1871, Potomac Bancshares, Inc. (the "Company") is a Charles Town, West Virginia bank holding company for the Bank of Charles Town. With approximately \$422 million in assets as of September 30, 2017, the Company conducts operations through its main office and branch office facilities in Jefferson and Berkeley Counties (WV), Washington County (MD) and Loudoun County (VA). The Bank provides various banking products and services for individuals, businesses, and local governments. Deposit products include noninterest-bearing and interest-bearing checking accounts, savings accounts, certificates of deposits, money market accounts, and individual retirement accounts. The Bank also offers loan products comprising commercial, financial, and agricultural loans; mortgage loans on real estate properties; secondary market and adjustable rate mortgage loans; equipment loans and construction financing products; and retail loan products consisting of home equity lines of credit. In addition, the Bank provides financial management, investment, trust, and brokerage services, as well as online banking services. The Company's shares are quoted on the OTC Pink Sheet marketplace under the symbol "PTBS."

### Net Income Was Quite Strong, Even Adjusting For Nonrecurring Items

Potomac Bancshares reported an excellent quarter in the three months ended September 30, 2017. Earnings growth was excellent, and while some of the strength relative to the year-ago comparisons was due to nonrecurring items, the operating profitability was still greatly improved from the year-ago figures. Specific items in the year-ago quarter included: 1) a much higher than normal provision for loan losses of \$261,000; 2) security losses of \$45,000, and 3) OREO-related charges totaling \$144,000. As can be seen in the adjacent table, even if we exclude all of these items, we see that the pretax income before nonrecurring and credit charges was still up an impressive 29% to \$1,411,000 in 2017's third quarter from \$1,092,000 in the year-ago quarter. The strong operating earnings growth was primarily due to continued momentum in net interest income and noninterest income, along with lower noninterest expense. Balance sheet growth in the quarter was also strong, with increases in the double digits, and the Company's overall asset quality continued to improve.

	2016 Q3	2017 Q3
<b>Quarterly Results (\$000s)</b>		
Net Income	485	953
Pretax Income	732	1,411
Adjustments:		
Provision (Add)	261	-
Security Gains (Deduct)	(45)	-
OREO Valuation	137	-
Gains/Losses on Sale of OREO (Add Losses)	7	-
<b>Pretax Inc. Bef. Nonrec/Credit Charges</b>	<b>1,092</b>	<b>1,411</b>

Net income for the third quarter of 2017 was \$953,000, or \$0.29 per diluted share, up from \$485,000, or \$0.14 per diluted share, in the year-ago quarter. We had projected the Company would earn \$0.24 per diluted share, so the results were a nickel above projections. The primary driver behind the earnings growth was net interest income, which increased 11% to \$3,558,000 in 2017's third quarter from \$3,129,000 in the year-ago quarter. All of the growth in net interest income came from higher average earning assets (up 13%), as margins declined slightly to 3.57% in 2017's third quarter from

ASSETS: \$422 MM

HQ: CHARLES TOWN, WV

CONTACT:  
ALICE FRAZIER, CEO  
DEAN J. COGNETTI, CFO

304-725-8431

### 3<sup>RD</sup> QUARTER HIGHLIGHTS:

THE QUARTER WAS QUITE  
STRONG

EPS: \$0.29 vs. \$0.14

PRETAX INCOME BEFORE  
NONRECURRING FACTORS AND  
CREDIT RELATED CHARGES  
INCREASED 29%

NET INTEREST INCOME  
INCREASED 11% DUE TO RAPID  
GROWTH IN AVERAGE EARNING  
ASSETS

NONINTEREST INCOME,  
EXCLUDING SECURITY GAINS,  
WAS UP 6%

NONINTEREST EXPENSE  
ACTUALLY *DECLINED* IN THE  
QUARTER

3.63% in the year-ago quarter. Noninterest income, excluding security gains in the year-ago quarter, increased 6% to \$1,100,000 in 2017's third quarter from \$1,037,000 in the year-ago quarter, while noninterest expense *declined* about 1% to \$3,247,000 from \$3,281,000 over this period.

**YEAR-TO-DATE HIGHLIGHTS:**

EPS: **\$1.01 (\$0.81 EXCLUDING  
THE LIFE INSURANCE AND  
SECURITY GAIN) VS. \$0.49**

BALANCE SHEET GROWTH WAS  
IN THE **11% TO 12% RANGE**

For the first nine months of 2017, Potomac Bancshares had net income of \$3,389,000, or \$1.01 per dilute share, up from \$1,631,000, or \$0.49 per diluted share, in the year-ago period. Year-to-date earnings for 2017 included \$670,000 in life insurance proceeds, while the year-ago period was impacted by the aforementioned sale of foreclosed property, though even excluding these factors, earnings growth was still quite strong. Net interest income increased 12%, noninterest income (excluding the life insurance proceeds and security gains) was up 2% and noninterest expense grew a modest 1%. Balance sheet growth was also excellent, generally in the 11% to 12% range from September 30, 2016 to September 30, 2017, and stockholders' equity was \$35.5 million, or 8.4% of assets.

PTBS'S ROAA AND ROAE  
WERE HIGHER THAN THE PEER  
GROUP MEDIAN

**Potomac Compares Favorably to the Majority of Peers in Terms of Fundamentals and Value**

In the below table, we have included several key performance and valuation metrics for Potomac Bancshares compared to a group of 38 publicly traded banks located in West Virginia, Virginia and Maryland (with assets between \$250 million and \$1 billion). As can be seen from the table, Potomac Bancshares has a far better ROAA and ROAE relative to the median for the peer group, and its asset quality ratio of NPAs-to-assets also was superior to the peer group median. The Company's dividend yield of 2.2% was above the peer group median of 1.7%, and its ability to build value over time has been better as well, as measured by a five-year total return. Despite the superior performance, the shares are actually trading at a discount to the median on a price to latest 12 months earnings basis, and its price to tangible book value ratio was only slightly above the median, which we believe is more than warranted given the strong ROAE. The compelling value of PTBS shares is one of the reasons that insiders continue to buy the stock, in addition to the Company repurchasing shares from time to time (during the third quarter of 2017, the Company repurchased 22,000 shares of stock).

THE COMPANY'S NPAs/ASSETS  
RATIO WAS BETTER THAN THE  
PEER GROUP MEDIAN

THE DIVIDEND YIELD AND 5  
YEAR TOTAL RETURN WERE  
BETTER COMPARED TO THE  
PEER GROUP

THE P/E MULTIPLE WAS BELOW  
THE PEER MEDIAN

PEER GROUP COMPARISON: PTBS VS. WV, VA MD PUBLIC BANKS, ASSETS BETWEEN \$250M AND \$1 BB							
	ROAA MRQ	ROAE MRQ	NPAs/ Assets	Dividend Yield	5 Year Total Return	Price/ LTM EPS	Price/Tang. Book Value
PTBS	0.91%	10.80%	0.28%	2.2%	133%	10.9x	1.21x
Peer Median	0.73%	7.65%	0.90%	1.7%	122%	17.4x	1.15x

ASSET QUALITY IS EXCELLENT

NPAs/ASSETS: **0.28%**

RESERVES/LOANS: **1.02%**

**Nonperforming Assets Continue to Decline, Asset Quality is Superior to Peers**

Potomac Bancshares, Inc.'s nonperforming assets decreased from June 30, 2017 and the year-ago date. Specifically, NPAs (which we define as nonaccruing loans, over 90 day past due loans that are still accruing and OREO) totaled \$1.2 million, or 0.28% of total assets, at September 30, 2017, versus \$1.6 million, or 0.39% of total assets, at June 30, 2017 and \$2.0 million, or 0.53% of total assets, at September 30, 2016. (Note that these figures exclude restructured loans that are still accruing.) At September 30, 2017, the allowance for loan losses was \$3.5 million, or 1.02% of gross loans, up 20% from \$2.9 million, 0.94% of gross loans, at the year-ago date. Both the NPAs/assets and reserves/gross loans ratios were better compared to the peer group median.

**Projections Increased**

Based on the strength of the third quarter results, we are raising our 2017 earnings projections to \$3.4 million, or \$1.05 per diluted share (excludes the life insurance proceeds and recent security gain, which in aggregate total \$0.26 per share). For 2018, we are projecting earnings of \$3.8 million, or \$1.16 per diluted share. These projections could vary widely depending on changing economic and credit conditions.

EPS:  
2016A: \$ 0.66  
2017E: \$ 1.05 \*  
2018E: \$ 1.16

EXCLUDES LIFE INSURANCE  
PROCEEDS OF ROUGHLY \$0.20  
PER SHARE AND A SECURITY  
GAIN OF \$0.06 PER SHARE

ADDITIONAL INFORMATION UPON REQUEST

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