Zacks Small-Cap Research

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QCR Holdings, Inc.

(QCRH-NASDAQ)

QCRH: First Quarter Is Better Than It First Appears

Current Recommendation	**Outperform**
Prior Recommendation	Neutral
Date of Last Change	08/26/2013
Current Price (06/11/14)	$17.30
Twelve- Month Target Price	**$19.50**

OUTLOOK

QCRH's 2014 first quarter diluted EPS of $0.40 was a couple of pennies shy of our $0.42 estimate. Despite this, it was a better quarter than we expected in several important ways. First, the net interest margin of 3.11% was 9 basis points higher than the 3.02% we had been estimating, while loan growth of over 2% was almost double our projection. Second, improved asset quality led to loan loss provision that came in about $0.25 million below our $1.350 million estimate. Third, the effective tax rate was 10.8% versus our 25.0% estimate. Finally, our estimate of average shares outstanding was about 200,000 too high. On the negative side, the $0.26 million gain on the sale of government-guaranteed loans was more than $0.6 million below what we had estimated. Moreover, total noninterest expense of $16.1 million was about $0.5 million greater than our $15.6 million estimate. We are reducing our net earnings estimate after preferred stock dividends to $13.8 million from $14.5 million, while our diluted EPS estimate falls to $1.70 from $1.75. A significant factor causing this reduction is the increase in the SBLF preferred dividend rate to 9% from 5% during 2014's first quarter and a delay in the date of redemption for the remaining $14.9 million of SBLF preferred stock to the fourth quarter from the second quarter. Our initial 2015 diluted EPS estimate for 2015 is $1.85, a 9% increase from 2014.

SUMMARY DATA

52-Week High	**$18.10**
52-Week Low	**$14.96**
One-Year Return (%)	**15.41**
Beta	**0.22**
Average Daily Volume (sh)	**5,702**
Shares Outstanding (mil)	**8**
Market Capitalization ($mil)	**$137**
Short Interest Ratio (days)	**0.43**
Institutional Ownership (%)	**15**
Insider Ownership (%)	**13**
Annual Cash Dividend	**$0.08**
Dividend Yield (%)	**0.46**
5-Yr. Historical Growth Rates	
Net Revenue (%)	**8.6**
Earnings Per Share (%)	**20.5**
Dividend (%)	**0.0**
P/E using TTM EPS	**8.7**
P/E using 2014 Estimate	**10.2**
P/E using 2015 Estimate	**9.4**
Zacks Rank	**2**

Risk Level	**Average**
Type of Stock	**Small-Value**
Industry	**Banks-Midwest**
Zacks Rank in Industry	**6 of 35**

ZACKS ESTIMATES

Net Revenue

(in millions of $)

	Q1 (Mar)	Q2 (Jun)	Q3 (Sep)	Q4 (Dec)	Year (Dec)
2012	18.2 A	18.6 A	18.7 A	18.8 A	74.3 A
2013	19.4 A	22.7 A	23.2 A	24.6 A	89.9 A
2014	21.6 E	22.3 E	22.4 E	22.5 E	88.8 E
2015					91.4 E

Earnings per Share

(EPS is operating earnings before nonrecurring items)

	Q1 (Mar)	Q2 (Jun)	Q3 (Sep)	Q4 (Dec)	Year (Dec)
2012	0.48 A	0.44 A	0.44 A	0.49 A	1.85 A
2013	0.49 A	0.59 A	0.51 A	0.50 E	2.08 A
2014	0.40 A	0.44 E	0.43 E	0.43 E	1.70 E
201					1.85 E

Quarterly EPS may not add to total due to changes in shares outstanding.

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FIRST QUARTER RESULTS

Compared to the year-ago quarter, first quarter net earnings after preferred stock dividends jumped 30% to $3.2 million from $2.5 million, largely due to effects of the CNB acquisition in May 2013. On a diluted per share basis, EPS decreased $0.09, or 19%, to $0.40 from $0.49, reflecting a 60% increase in average diluted shares due to the CNB acquisition in the second quarter and the conversion of the Series E preferred stock in the fourth quarter, which added almost 100 basis points to the tangible common equity ratio and eliminated $1.75 million in annual preferred dividends.

QCRH's 2014 first quarter diluted EPS of $0.40 was a couple of pennies shy of our $0.42 estimate. Despite this, it was a better quarter than we expected in several important ways.

First, the net interest margin of 3.11% was 9 basis points higher than the 3.02% we had been estimating, while loan growth of over 2% was almost double our projection. Combined, these two items contributed to net interest income that was about $0.2 million more than we had anticipated. Just as important, we have increased our 2014 estimates for loan growth to 7.4% (from 5.1%) and the net interest margin to 3.09% (from 3.02%).

Second, improved asset quality led to loan loss provision that came in about $0.25 million below our $1.350 million estimate, a trend we expect to continue for the rest of the year. Accordingly, we have reduced our 2014 loan loss provision estimate by about $0.8 million, or 16%, to $4.5 million.

Third, the effective tax rate was 10.8% versus our 25.0% estimate, adding $0.7 million to the bottom relative to our projection. While there were some one-time items, QCRH's continued shift of its securities portfolio into tax-exempt municipal securities as well as tax credit carryforwards from the CNB acquisition will likely contribute to a lower effective tax rate going forward, with our new estimate at 22% for the remainder of the year and 2015.

Finally, our estimate of average shares outstanding was about 200,000 too high, (this contributed about a penny to results), and we have reduced our estimate for average shares outstanding for 2014 by the same amount.

On the negative side, the $0.26 million gain on the sale of government-guaranteed loans was more than $0.6 million below what we had estimated, as timing of these gains is rather haphazard. We expect QCRH to recoup most of this shortfall during later quarters in 2014. That said, we have reduced our estimate for gains on the sale of government-guaranteed loans by $0.3 million to $3.0 million for the year.

Moreover, total noninterest expense of $16.1 million was about $0.5 million greater than our $15.6 million estimate, largely due to higher compensation costs and occupancy and equipment expense, each coming in about $0.2 million more than our projection. Consequently, we have increased our 2014 estimates for compensation by $1.2 million, or 3%, and occupancy and equipment expense by $0.5 million, or 7%.

In addition, we have adjusted our estimate of the amount of the SBLF preferred dividend as the rate was increased to 9% from 5% during 2014's first quarter and have also delayed the date for the redemption of the remaining $14.9 million of SBLF preferred stock to the fourth quarter from the second quarter ($15.0 million of SBLF preferred stock was redeemed on March 31, 2014).

Officially, the Company states that the earliest possible date of redemption for the SBLF preferred stock is the end of the second quarter in 2014 and the latest date of redemption is the fourth quarter of 2014. Should the company redeem the SBLF preferred stock earlier than we expect, this would have a positive impact on the bottom line in 2014.

Combining all of these factors, we are reducing our net earnings estimate after preferred stock dividends to $13.8 million from $14.5 million, while our diluted EPS estimate falls to $1.70 from $1.75. This compares to net earnings of $11.8 million and diluted EPS of $2.08 in 2013.

Our initial 2015 diluted EPS estimate for 2015 is $1.85, a 9% increase from 2014. Primary factors supporting this gain are a net interest margin of 3.05%, 5% growth in loans outstanding, and elimination of the SBLF preferred dividend.

Below, we discuss first quarter results more fully. Details of our projections are shown at the back of the report.

Net Interest Income

Net interest income rose $2.7 million, or 19%, year over year to $16.8 million, as a 16% gain in average interest-earning assets combined with a 9 basis-point rise in the net interest margin to 3.11% to produce this result.

The NIM gain reflected a 5 basis-point decrease in the yield on average interest-earnings assets to 3.85% that was more than offset by a 10 basis-point drop in average deposit costs to 0.41% and a 17 basis-point fall in borrowing costs to 2.37%.

The yield on the loan and lease receivables portfolio fell 14 basis points year over year to 4.70%, primarily due to competitive pricing pressures. The shift by local banks into commercial and industrial (C&I) lending away from commercial real estate lending combined with a rush to finance top-quality borrowers has resulted in margin compression. Importantly, the 4.70% yield on loans is up 5 basis points from 4.65% in 2013's fourth quarter, which appears to be a trough, as QCRH expands into higher margin businesses, such as leasing, the highest yielding of the Company's asset.

We note that the yield on the securities portfolio advanced 32 basis points to 2.61%, as QCRH continues to shift the portfolio into higher yield municipal securities, away from lower yield US Agencies and residential mortgage-backed securities, enhancing diversification of the securities portfolio at the same time.

Net interest income was about $0.2 million above our $16.7 million estimate, as average interest-earning assets were $10 million better than our estimate and the 3.11% NIM was 9 basis points higher our 3.02% estimate, as well.

We expect that expansion of higher margin lending lines and securities will offset future competitive pricing pressures. Moreover, this will be enhanced by the shift in QCRH's balance sheet into higher yield loans, away from lower yield securities. Thus, we are increasing our NIM estimate to 3.09% for full-year 2014 (up from 3.02% previously). This compares to the 3.03% that was actually posted in 2013. Our initial NIM estimate for 2015 is 3.05%.

Noninterest Income

Results were hurt by a 9% year-over-year decline in noninterest income to $4.7 million, though performance was better than it first appears. Last year's quarter includes two one-time gains—a $495,000 gain on the sale of a credit card portfolio and a $355,000 gain on the sale of the credit card operation. Excluding these two items, noninterest income was up 9%, largely due to strong growth in trust department and deposit services fees, stemming from the CNB acquisition. This was partly offset a $0.9 million drop in gains on government-guaranteed loan sales.

For 2014, we are decreasing our estimate of noninterest income to $20.3 million from $21.1 million, down 21% year over year from 2013. The reduction stems from a $0.3 million decline in gains on sales of government guaranteed loans and a $0.5 million fall in other income. Relative to 2013, while we expect solid growth in trust department and deposit service fees in 2014 and flat gains on loan sales, lower

contributions resulting from the absence of several one-time acquisition-related and other gains (as occurred in 2013) will be revenue drags.

Loan Loss Provision
The loan loss provision increased a modest 3% to $1.1 million, and was well below our $1.35 million estimate as the Company reported improved asset quality.

Going forward, our estimate for the loan loss provision for 2014 has been decreased by about $0.8 million, or 16%, to $4.5 million. This compares to $$5.9 million in 2013. We expect a very low level of loss provisions at CNB in 2014 since the loan portfolio was written down to realizable value prior to acquisition, pursuant to purchase accounting rules. For 2015, we expect the loss provision to grow in line with the loan portfolio.

Noninterest Expense
Noninterest expense rose $2.2 million, or 16%, year over year to $16.1 million, $0.5 million greater than our $15.6 million estimate, largely due to higher compensation costs and occupancy and equipment expense, each coming in about $0.2 million more than our projection. Consequently, we have increased our 2014 estimates for compensation by $1.2 million, or 3%, and occupancy and equipment expense by $0.5 million, or 7%.

Relative to 2013's first quarter, most line items increased substantially year over year due to the CNB acquisition. The exception was other expense, which dropped almost $0.5 million. However, we note that last year's quarter included two one-time charges—$357,000 in CNB acquisition costs and $257,000 related to the sale of the credit card portfolio and operations; excluding these items, other expense also would have increased.

The Company's efficiency ratio deteriorated, rising 280 basis points to 74.8% compared to 72.0% in 2013's first quarter.

We expect the operating efficiency ratio to come in at 73.3% in full-year 2014 and 73.9% for 2015, which compares to 72.0% actually reported in 2013.

Income Taxes
The Company's effective tax rate was 10.8% in the first quarter, compared to 25.4% in the year-ago quarter and our 25.0% estimate, adding about $0.7 million, or $0.09, to the bottom line. QCRH's continued shift of its securities portfolio into tax-exempt municipal securities as well as tax credit carryforwards from the CNB acquisition will likely contribute to a lower effective tax rate going forward, with our new estimate at 22% for the remainder of the year and for 2015. This compares to a 23.6% tax rate that was actually posted in 2013.

Net Income
QCRH posted first quarter net earnings attributable to common shareholders of $3.2 million, or $0.40 per diluted share, up 30% from $2.5 million ($0.49 diluted EPS) reported in the year-ago quarter. This compares to our $3.5 million net income estimate ($0.42 diluted EPS).

Profitability
QCRH posted a 10.4% ROE and 0.64% ROA for the first quarter of 2014, compared to a 9.3% ROE and 0.62% ROA for the first quarter of 2013.

Loans and Asset Quality
Loans jumped $32 million, or 2.2%, sequentially to $1,493 million during the first quarter, with solid growth in all lines of lending. Leading the charge was direct finance leasing, which rose $11 million, or 8 ½%, to $140 million followed by commercial and industrial, which grew $10 ½ million, or 2 ½%, to $442 million.

Following the strong first quarter, we are raising our estimate of loan growth in 2014 to 7.4% from 5%, with our initial estimate at a 5% gain for 2015. This compares to year-over-year growth of 13% in 2012 including CNB.

Nonperforming loans fell by $1.9 million, or 9%, to $18.6 million during the first quarter, attributable to the return to performing status of several troubled debt restructurings and pay-offs of certain nonperforming loans. Foreclosed assets, which includes $9.7 million of OREO, fell 1% to $9.9 million. As a percentage of total loans and OREO, total nonperforming assets improved, sliding by 18 basis points sequentially to 1.90% from 2.08% at the end of the fourth quarter, but was up 7 basis points year over year from 1.83%.

We expect asset quality to show further improvement as the Company works though problem assets, with the estimated NPA ratio falling from 2.08% at yearend 2013 to 1.62 % by the end of 2014 and 1.30% by the end of 2015.

The loan loss allowance as a percent of nonperforming assets increased sequentially to 79% at the end of the quarter from 70% at December 31, 2013, but fell from 88% a year ago. This was the result of a loan loss allowance that increased to $22.7 million, or 1.52% of gross loans, from $21.4 million, or 1.47% of gross, at December 31, 2013 and $20.8 million, or 1.61% of gross loans at March 31, 2013, plus a lower level of problem loans.

The CNB acquisition distorted loan loss reserve ratios as there was no allowance associated with CNB's loans at acquisition since CNB's loans were recorded at market value. As a result, the Company's allowance to total loans/leases fell to 1.52% at March 31, 2014 from 1.61% at March 31, 2013.

Liquidity and Funding

During the first quarter, QCRH reduced cash and short-investments by $3 million to $111 million, while the securities portfolio increased $10 million to $707 million.

Within the securities portfolio, there were shifts from the previous quarter. Sequentially, US Agency securities declined 2% to $350 million, or 50% of the total securities portfolio (down from 51% at the end of the fourth quarter), while municipal securities rose 8% to $196 million, or 28% of the securities portfolio (up from 26% at the end of the fourth quarter), and residential mortgage-backed securities gained less than 1% to $158 million, or 22% of total securities (23% at the end of the fourth quarter).

QCRH intends to reduce its reliance on more expensive wholesale funds, including Federal Home Loan Bank (FHLB) advances, wholesale structured repurchase agreements, and brokered time deposits, replacing these with less expensive core deposits, especially noninterest-bearing demand deposits related to QCBT’s correspondent banking business. At March 31, 2014, noninterest-bearing demand deposits represented 34% of total deposits of $1.7 billion (up from 33% at December 31, 2013), while interest-bearing demand deposits were 43% (the same as at yearend), time deposits were 18% (down from 20% at December 31, 2013), and brokered deposits were 5% (up from 4% at December 31, 2013).

Capital Adequacy and Dividends

The Company’s capital adequacy ratios fell during the quarter, primarily reflecting to the redemption of $15.0 million of SBLF preferred stock on the last day of the quarter. The Tier 1 capital ratio slid 62 basis points to 10.83% at the end of 2014’s first quarter from 11.37% at December 31, 2013, and the Total capital ratio tumbled 64 basis points to 12.23% from 12.87%.

The tangible common equity to tangible assets ratio jumped 31 basis points, rising to to 5.02% at March 31, 2014, largely due to growth in retained earnings and a large $18.9 million positive swing in other comprehensive income.

Tangible book value per share increased during the first quarter by $1.06 per share, rising to $15.34 from $14.28.

On May 15, 2014, QCRH announced its regular semi-annual cash dividend of $0.04 per share payable on July 8, 2014 to stockholders of record on June 20, 2014. We do not expect any increase in the common dividend for the foreseeable future as the Company expects to retain excess earnings to grow tangible common equity and redeem the remaining $14.9 million balance of the SBLF preferred stock (at some point later in 2014).

On December 23, 2013, QCRH completed the previously announced conversion of all 25,000 outstanding shares of the Company's Series E Non-Cumulative Convertible Perpetual Preferred Stock into shares of the Company's common stock. As a result, approximately 2.1 million shares of common stock were issued. This transaction increased tangible common equity by approximately 100 basis points and eliminated $1.75 million in annual preferred stock dividends.

Consequently, the tangible common equity rose to 4.71% of tangible assets at the end of 2013 from 3.49% at September 30, 2013. We expect further improvement to 5.26% at yearend 2014 and 5.68% by the end of 2015, due to growth in retained earnings.

The total tangible equity ratio dropped to 5.96% of total tangible assets at yearend 2013 from 6.56% at the end of 2012, reflecting negative changes in accumulated other comprehensive income due to mark-to-market declines in the bond portfolio. In 2014, the total tangible equity ratio is estimated to decline about 70 basis points to 5.26% of total tangible assets at yearend 2014 from 5.96% at the end of 2013, following the full $30 million redemption of the SBLF preferred stock by the end of 2014. This redemption is also expected to have a negative impact on the double leverage ratio at the holding company, which is estimated to deteriorate, by rising to the 145-150% level in 2014-15 from 128% at yearend 2013.

In May 2013, shareholders approved The Amended Rights Agreement, the primary purpose of which is to extend the term of the Original Rights Agreement for an additional three years to May 1, 2016, increase the trigger from 15% to 20% or more of the outstanding common stock, add additional stockholder protections, and amend certain provisions that limit the authority of the board. The Amended Rights Agreement is designed to deter the use of coercive or abusive takeover tactics by parties interested in acquiring the Company without offering fair value to all stockholders. The Rights should not interfere with any merger or other business combination that is in the best interests of the Company and its stockholders because the board may, at its option, subject to certain restrictions, redeem all of the then outstanding Rights at the Redemption Price. In addition, if the board declines a Qualifying Offer for a merger or business combination, such offer may be presented to the stockholders at a special meeting.

Basel III

The Company feels comfortable with the recent regulatory proposals for Basel III, and believes that its long-term stratgegy of increasing tangible common equity to 6% of tangible assets through conversion of Series E preferred stock into common equity and the long period of implementation will help it meet Basel III proposals. QCRH does not intend to issue any dilutive common equity.

OVERVIEW

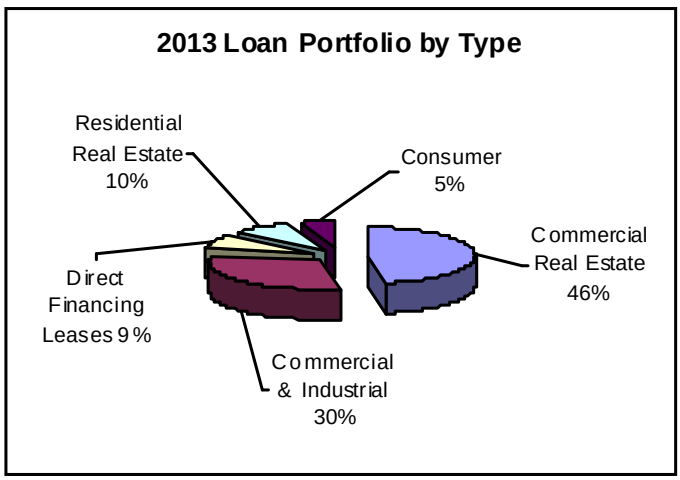
QCR Holdings, Inc. (QCRH or the Company) is a multibank holding company, which was founded in 1993 and is headquartered in Moline, Illinois, with $2.4 billion in total assets at March 31, 2014 and 14 offices. QCRH provides a broad range of business and retail lending products and investment services through four wholly owned, full-service banking subsidiaries that are located in Illinois and Iowa. These subsidiaries include Quad City Bank and Trust Company (QCBT), based in Bettendorf, Iowa; Cedar Rapids Bank and Trust Company (CRBT), based in Cedar Rapids, Iowa; Rockford Bank and Trust Company (RB&T), based in Rockford, Illinois; and Community National Bank (CNB), based in Waterloo, Iowa following the May 2013 acquisition of Parent Community National Bancorporation by QCRH.

By far the largest of these subsidiaries is QCBT, which accounts for $1.25 billion, or approximately 52%, of QCRH's total assets, and is also the oldest of its subsidiaries, having begun operations in January 1994. Its five offices are located in Bettendorf and Davenport, Iowa and Moline, Illinois. CRBT, begun in June 2001, is the next largest with $804 million of total assets, or about 34% of consolidated assets, and six offices total, with two offices each in Cedar Rapids, Waterloo, and Cedar Falls. On October 26, 2013, CNB was merged into CRBT and CNB's offices were rebranded Community Bank and Trust. RB&T began operations in September 2004. RB&T has $339 million in total assets, or roughly 14% of QCRH's total assets, and operates through two offices located in Rockford, Illinois. CNB is the final banking subsidiary, having begun operations in 1997.

In addition, the Company has three non-bank subsidiaries that help manage other aspects of its business. These include: (1) a 100% equity interest in m2 Lease Funds, LLC (m2), which is owned by QCBT and was acquired in August 2005. m2, which is based in Brookfield, Wisconsin and operates through one office, is engaged in the business of leasing machinery and equipment to commercial and industrial clients through full-payout direct financing leases. Accounting for $110 million, or approximately 5%, of total consolidated assets, m2 is a niche player and specializes in the key areas of marine equipment, printing, office technology, machinery/machine tools, and telecom; (2) a 100% ownership interest in Velie Plantation Holding Company, LLC (VPHC), acquired through a series of transactions beginning in 1998. VPHC manages the real estate property known as Velie Plantation Mansion in Moline, Illinois, which serves as the headquarters and Moline branch for QCRH; and (3) a 100% interest in Quad City Investment Advisors, LLC, an investment management business that was acquired in January 2008 and was formerly known as CMG Investment Advisors, LLC.

QCRH has a smaller ownership interest in Nobel Real Estate Investors, LLC (20%), though this does not contribute meaningfully to assets or net income. The Cedar Rapids Mortgage Company, LLC in which QCRH had a 50% interest, was closed in 2013's second quarter.

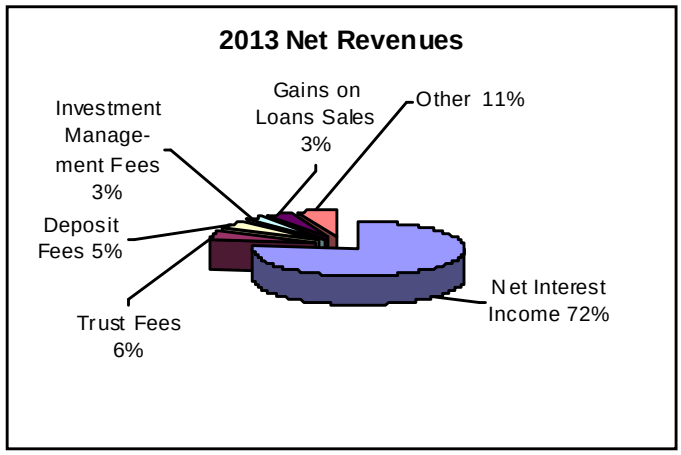
QCRH has disposed of several operating subsidiaries over the past few years as they did not contribute significantly to earnings and no longer fit into the Company's long-term strategic plans. These include: (1) the sale of the merchant credit card processing business and the liquidation of Quad City Bancard, Inc., a subsidiary that issued credit cards to consumers and businesses, in the third quarter of 2008, for which the Company recorded a $3.0 million aftertax gain; (2) the sale of Second Wisconsin Bank and Trust Company, QCRH's Milwaukee, Wisconsin banking subsidiary, for which the Company posted a $0.5 million aftertax gain on December 31, 2008; and (3) the sale of the $10 million credit card portfolio of QCBT, which was sold at an $0.8 million pretax gain in 2013. In 2008, these were reported as discontinued operations in the Company's financial statements (we have not adjusted prior-year financial data for these changes).



The $1.5 billion loan portfolio has a concentration in commercial real estate, accounting for 46% of total loans at December 31, 2013, of which about 56% is nonowner-occupied, 37% is owner-occupied, and 7% is construction and land development. The rest of the lending book consists of commercial and industrial (accounting for 30% of total gross loans), direct financing leases (9%), residential real estate (10%), and consumer (5%). Most loans are secured, usually by real estate, inventory, accounts receivable, equipment, machinery, or corporate assets.

The liquidity portfolio, consisting of cash, short-term investments, and US agency/residential mortgage-backed securities (RMBS) obligations, represents 26% of total assets, while gross loans and leases account for 61%. Noninterest-bearing demand deposits accounted for 33% of total deposits of $1.6 billion at December 31, 2013, with interest-bearing demand and savings deposits at 43%, time deposits at 20%, and brokered time deposits at 4%.

In 2013, net interest income contributed 72% of net revenue. Other significant revenue sources include trust department fees (6%), deposit service fees (5% of net revenues), gains on loan sales (3%), investment management and advisory fees (3%), and other (11%).



QCRH also managed $1.55 billion in trust accounts and $593 million in brokerage accounts at September 30, 2013.

The Company ‘s financial goals over the next thee-five years include: (1) growing tangible common equity to 6% of tangible assets from about 4.7% at the end of 2013 through growth in retained earnings; (2) funding the redemption of the remaining $15 million in SBLF preferred stock through growth in retained earnings; (3) increasing profitability as measured by the return on average assets (ROA) to the around the 70 basis-point level over the near term and to 100 basis points over the longer term from 64 basis points in 2013, by driving down the efficiency ratio to the 60%-plus area from 72% in 2013; (4) continuing to improve asset quality; (5) continuing to shift the deposit mix toward noninterest-bearing deposits from more expensive retail and wholesale borrowings, thereby expanding the net interest margin; (6) integrating the CNB acquisition as quickly possible so as to maximize cost savings and other efficiencies; (7) boosting SBA/USDA gains on loan sales; (8) growing wealth management income; and (9) improving liquidity in its common stock.

Importantly, QCRH is committed to not diluting existing shareholder interests by issuing common shares at below book value, but would consider a capital raise for accretive acquisitions, as occurred with the recent $19 million stock and cash purchase of Community National Bancorporation.

VALUATION

QCRH stock has risen 1.6% year to date , though this is short of the industry’s median price increase of 5.9% and the S&P 500’s 5.2% gain, as shown in the following table. The stock was up 28.8% in 2013 and 45.3% in 2012, which compares with the S&P 500’s 29.6% and 13.3%, respectively.

At its current price, QCRH is trading at a 22% discount to the industry median P/E, based upon our diluted EPS estimate for 2015. This is roughly the same as the five-year average historical discount of 23%.

Turning to Price/Tangible Book Value, QCRH is valued at 1.16X versus the industry median of 1.23X. While this is 6% below the industry median, it is also 7points better than QCRH’s historical average. However, we believe a higher valuation is justified as the Company’s earnings and profitability prospects are much improved and QCRH has taken a number of steps over the last few years to strengthen its balance sheet. Moreover, the CNB acquisition will provide additional growth opportunities in the future. Applying the 1.23X ratio to estimated book value for QCRH twelve months out results in a price of approximately $21.50.

Taking the midpoint of these two valuation measures results in a price of $19.50, compared to the current stock price of $17.30. When price appreciation of more than 12 ½% is combined with the dividend yield, this represents a total return of over 13%, above our expectations for gains in the broader market index over the next year.

Accordingly, we are maintaining our Buy recommendation on QCRH.

Industry Comparables- Small-Cap Banks

		Price / Earnings Ratios					Return on Equity		Return on Assets		
	Pr Chg YTD	TTM* EPS	2014E	2015E	5-Yr Avg	Price/ Book	TTM*	5-Yr Avg	TTM*	5-Yr Avg	Div Yld
QCR Holdings	**1.6**	**8.7**	**10.2**	**9.4**	**12.1**	**1.16**	**10.7**	**6.9**	**0.64**	**0.43**	**0.5**
S&P 500	5.2	18.1	16.6	15.6	16.6	4.9	23.0	-----	8.5	-----	1.9
Median	**5.9**	**13.5**	**13.3**	**12.1**	**15.8**	**1.23**	**8.7**	**5.2**	**0.88**	**0.43**	**1.4**
Average	7.3	14.0	16.1	12.7	22.7	1.1	8.6	2.7	0.9	0.4	1.4
High	66.4	23.9	45.7	18.9	88.4	2.2	26.6	13.9	3.6	1.9	4.2
Low	(13.9)	4.5	9.3	8.5	6.6	0.7	(13.1)	(67.8)	(1.5)	(1.5)	-----

*Trailing twelve months

QCR Holdings, Inc.

Income Statement and Balance Sheet

(Dollars in millions, except per share data)

Summary Financial Data	12/09	12/10	12/11	12/12	12/13	12/14 E	12/15 E
Net interest income	50.4	49.9	54.1	57.6	64.1	68.5	70.2
Non-interest income	15.6	15.4	17.5	16.7	25.8	20.3	21.2
Total net revenue	66.0	65.3	71.6	74.3	89.9	88.8	91.4
Loan loss provision	17.0	7.5	6.6	4.4	5.9	4.5	4.7
Non-interest expense	46.7	48.5	51.0	52.3	64.4	65.0	67.6
Income taxes & other	4.4	6.8	8.4	8.5	7.8	5.5	3.8
Zacks adjusted income before NRI	(2.1)	2.5	5.6	9.1	11.8	13.8	15.3
GAAP net income	(2.1)	2.5	4.4	9.1	11.8	13.8	15.3
Diluted EPS before NRI	(0.46)	0.53	1.17	1.85	2.08	1.70	1.85
Reported EPS	(0.46)	0.53	0.92	1.85	2.08	1.70	1.85
Dividends per share	0.08	0.08	0.08	0.08	0.08	0.08	0.08
Liquid assets	417.3	546.0	638.5	612.7	629.3	601.4	577.8
Loans & leases, gross	1,244.3	1,172.5	1,200.7	1,287.4	1,460.3	1,568.4	1,648.3
Total assets	1,779.6	1,836.6	1,966.6	2,093.7	2,395.0	2,481.3	2,556.6
Core deposits	761.5	844.2	960.9	1,129.5	1,341.7	1,418.5	1,490.7
Purchased funds	340.9	307.1	263.6	266.2	415.8	415.0	405.0
Long-term debt	378.8	388.5	358.1	355.0	303.6	310.0	325.0
Shareholders' equity	123.9	130.9	142.4	140.4	147.6	135.4	150.0
Profitability							
Return on avg assets	0.10%	0.36%	0.51%	0.62%	0.64%	0.63%	0.61%
Return on avg equity	1.43%	5.03%	7.09%	8.90%	10.24%	10.66%	10.69%
Net interest margin	3.15%	2.92%	3.08%	3.10%	3.03%	3.09%	3.05%
Loan loss provision % avg assets	0.98%	0.41%	0.35%	0.22%	0.25%	0.19%	0.19%
Noninterest income % avg assets	0.91%	0.84%	0.92%	0.82%	1.11%	0.83%	0.84%
Noninterest expense % avg assets	2.71%	2.64%	2.67%	2.58%	2.76%	2.65%	2.68%
Preprovision pretax income % avg assets	1.12%	0.91%	1.08%	1.09%	1.09%	0.97%	0.95%
Tangible efficiency ratio	72%	74%	73%	70%	72%	73%	74%
Payout ratio	(18)%	15%	9%	4%	4%	5%	4%
Asset Quality							
Net charge-offs % avg loans	1.00%	0.79%	0.70%	0.27%	0.31%	0.18%	0.21%
Allowance % loans	1.81%	1.74%	1.56%	1.55%	1.47%	1.48%	1.49%
NPAs % loans & related assets	3.22%	4.24%	3.35%	2.29%	2.08%	1.62%	1.30%
Allowance % NPAs	56%	41%	46%	67%	70%	91%	114%
Liquidity & Funding							
Liquid assets % purchased funds	122%	178%	242%	230%	151%	145%	143%
Core deposits % loans	61%	72%	80%	88%	92%	90%	90%
Liquid assets % assets	23%	30%	32%	29%	26%	24%	23%
Loans % assets	70%	64%	61%	61%	61%	63%	64%
Capital Adequacy							
Total equity % assets	6.96%	7.13%	7.24%	6.71%	6.16%	5.46%	5.87%
Tangible equity % assets	6.79%	6.97%	7.09%	6.56%	5.96%	5.26%	5.68%
Tier 1 capital ratio	11.14%	12.12%	12.24%	11.27%	11.45%		
Total capital ratio	12.52%	13.70%	13.84%	12.71%	12.87%		
Parent Company Statistics							
Interest coverage	1.4X	0.7X	2.8X	5.5X	3.9X	3.5X	3.5X
Interest & dividend coverage	0.5X	0.3X	0.8X	1.4X	1.2X	1.6X	2.6X
Short-term debt coverage	N/A	N/A	N/A	N/A	N/A	N/A	N/A
Total debt coverage	N/A	N/A	N/A	N/A	N/A	N/A	N/A
Double leverage	133.4%	132.5%	128.9%	130.8%	127.9%	149.6%	145.2%

QCR Holdings, Inc.

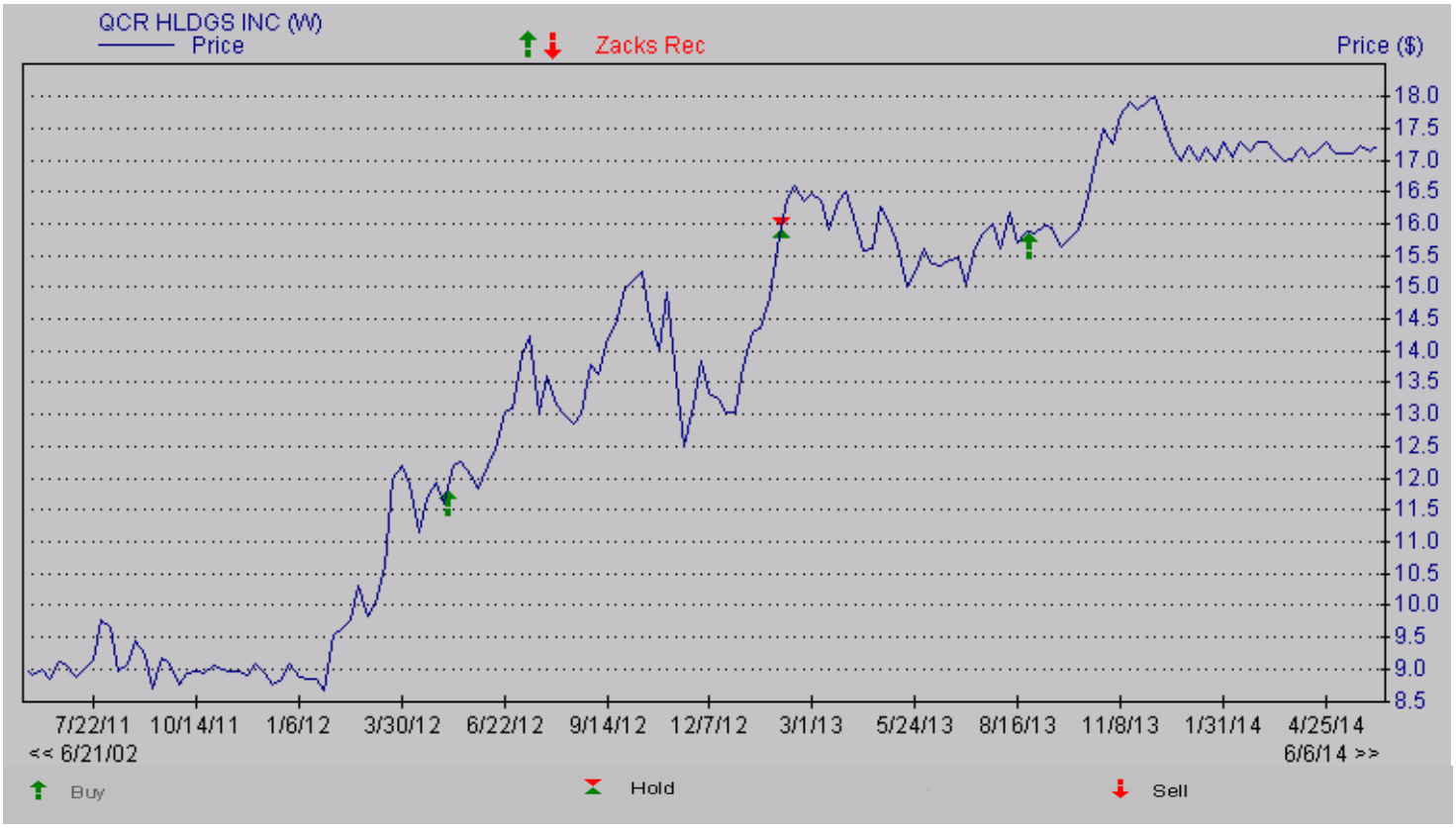
Income Statement and Balance Sheet

(Dollars in millions, except per share data)

	2013				2014			
Summary Financial Data	**Q1 A**	**Q2 A**	**Q3 A**	**Q4 A**	**Q1**	**Q2 E**	**Q3 E**	**Q4 E**
Net interest income	14.2	15.7	17.3	16.9	16.9	17.0	17.2	17.4
Non-interest income	5.2	7.0	5.9	7.7	4.7	5.3	5.2	5.1
Total net revenue	19.4	22.7	23.2	24.6	21.6	22.3	22.4	22.5
Loan loss provision	1.1	1.5	1.4	2.0	1.1	1.2	1.2	1.2
Non-interest expense	14.0	15.2	17.0	18.2	16.1	16.2	16.3	16.4
Income taxes & other	1.8	2.8	1.8	1.3	1.2	1.3	1.4	1.4
Zacks adjusted income before NRI	2.5	3.2	3.0	3.1	3.2	3.6	3.5	3.5
GAAP net income	2.5	3.2	3.0	3.1	3.2	3.6	3.5	3.5
Diluted EPS before NRI	0.49	0.59	0.51	0.50	0.40	0.44	0.43	0.43
Reported EPS	0.49	0.59	0.51	0.50	0.40	0.44	0.43	0.43
Dividends per share	-----	0.04	-----	0.04	-----	0.04	-----	0.04
Liquid assets	645.7	655.0	656.8	629.3	619.9	613.7	607.5	601.4
Loans & leases, gross	1,291.8	1,530.7	1,539.4	1,460.3	1,492.6	1,522.4	1,552.9	1,568.4
Total assets	2,144.0	2,446.8	2,485.7	2,395.0	2,426.3	2,444.5	2,462.9	2,481.3
Core deposits	1,175.9	1,467.1	1,492.2	1,341.7	1,366.6	1,383.6	1,400.9	1,418.5
Purchased funds	266.2	293.8	268.2	415.8	415.8	415.0	415.0	415.0
Long-term debt	358.0	348.7	369.8	303.6	307.8	310.0	310.0	310.0
Shareholders' equity	142.2	145.4	148.0	147.6	141.4	144.3	147.5	135.4
Profitability								
Return on avg assets*	0.62%	0.70%	0.62%	0.63%	0.64%	0.64%	0.62%	0.62%
Return on avg equity *	9.25%	11.03	10.44%	10.19%	10.37%	10.96%	10.47%	10.88%
Net interest margin	3.02%	2.99%	3.07%	3.04%	3.11%	3.08%	3.08%	3.08%
Loan loss provision % avg assets*	0.20%	0.26%	0.22%	0.33%	0.18%	0.19%	0.19%	0.19%
Noninterest income % avg assets*	0.99%	1.20%	0.97%	1.27%	0.78%	0.87%	0.84%	0.82%
Noninterest expense % avg assets*	2.65%	2.55%	2.77%	2.99%	2.65%	2.65%	2.66%	2.65%
Preprovision pretax inc.% avg assets*	1.03%	1.35%	1.01%	1.05%	0.90%	1.01%	0.99%	0.98%
Tangible efficiency ratio	72%	65%	75%	74%	75%	72%	73%	73%
Payout ratio	-----	7%	-----	8%	-----	9%	-----	9%
Asset Quality								
Net charge-offs % avg loans*	0.07%	0.32%	0.12%	0.71%	(0.03)%	0.27%	0.26%	0.23%
Allowance % loans	1.61%	1.38%	1.43%	1.47%	1.52%	1.50%	1.48%	1.48%
NPAs % loans & related assets	1.83%	2.22%	2.18%	2.08%	1.90%	1.80%	1.70%	1.62%
Allowance % NPAs	88%	62%	66%	70%	79%	83%	86%	91%
Liquidity & Funding								
Liquid assets % purchased funds	243%	223%	245%	151%	149%	148%	146%	145%
Core deposits % loans	91%	96%	97%	92%	92%	91%	90%	90%
Liquid assets % assets	30%	27%	26%	26%	26%	25%	25%	24%
Loans % assets	60%	63%	62%	61%	62%	62%	63%	63%
Capital Adequacy								
Total equity % assets	6.63%	5.94%	5.95%	6.16%	5.83%	5.90%	5.99%	5.46%
Tangible equity % assets	6.49%	5.69%	5.70%	5.96%	5.63%	5.71%	5.79%	5.26%
Tier 1 capital ratio	11.60%	10.82%	10.84%	11.45%	10.83%			
Total capital ratio	13.04%	12.20%	12.25%	12.87%	12.23%			

*Annualized.

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