Zacks Small-Cap Research

February 21, 2014
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QCR Holdings, Inc.

(QCRH-NASDAQ)

QCRH: Messy Fourth Quarter, But QCRH Is All Set for 2014

Current Recommendation	**Outperform**
Prior Recommendation	Neutral
Date of Last Change	08/26/2013
Current Price (02/20/14)	$17.21
Twelve- Month Target Price	**$20.25**

OUTLOOK

QCRH reported 2013 fourth quarter diluted EPS of $0.50, including a couple of partially offsetting items: a pretax $2.3 million gain on the sale of four CNB branches and a pretax $1.2 million charge for the CNB acquisition and data conversion costs. In addition, QCRH had a few other nonrecurring items, including a $576,000 gain on the sale of certain nonperforming loans and a lower-than-normal effective tax rate, which were offset by increased charges for the loan loss provision and loan/lease expense that were hit by yearend clean-up costs, as well as higher marketing and postage costs related to the rebranding of the remaining CNB branches and increased professional and data processing costs stemming from the CNB acquisition. Highlights of the quarter included a $4.4 million, or 18%, drop in nonperforming loans and the conversion of the Series E preferred stock, adding almost 100 basis points to the tangible common equity ratio and eliminating $1.75 million in annual preferred dividends. Though it was a pretty messy quarter (and year) due to the CNB acquisition, the groundwork has been laid for the combined company to achieve good performance right out of the starting gate in 2014. That said, we are reducing our 2014 diluted EPS estimate by $0.05 to $1.75 from $1.80, as we have increased our estimate for average diluted shares outstanding to 8.3 million shares from 8.075 million shares previously. Our net earnings estimate after preferred stock dividends remains the same at $14.5 million, up 23% from 2013's $11.8 million.

SUMMARY DATA

52-Week High	**$18.10**
52-Week Low	**$14.96**
One-Year Return (%)	**4.83**
Beta	**0.34**
Average Daily Volume (sh)	**12,909**
Shares Outstanding (mil)	**6**
Market Capitalization ($mil)	**$100**
Short Interest Ratio (days)	**0.26**
Institutional Ownership (%)	**4**
Insider Ownership (%)	**19**
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	**8.3**
P/E using 2013 Actual	**8.3**
P/E using 2014 Estimate	**9.8**
Zacks Rank	**3**

Risk Level	**Average**
Type of Stock	**Small-Value**
Industry	**Banks-Midwest**
Zacks Rank in Industry	**29 of 36**

ZACKS ESTIMATES

Net Revenue
(in millions of $)

	Q1 (Mar)	Q2 (Jun)	Q3 (Sep)	Q4 (Dec)	Year (Dec)
2011	17.3 A	18.1 A	18.1 A	18.1 A	71.6 A
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					90.9 E

Earnings per Share
(EPS is operating earnings before nonrecurring items)

	Q1 (Mar)	Q2 (Jun)	Q3 (Sep)	Q4 (Dec)	Year (Dec)
2011	0.23 A	0.34 A	0.24 A	0.35 A	1.17 A
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					1.75 E

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

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FOURTH QUARTER RESULTS

QCRH reported 2013 fourth quarter diluted EPS of $0.50, including a couple of partially offsetting items: a pretax $2.3 million gain on the sale of four CNB branches and a pretax $1.2 million charge for the CNB acquisition and data conversion costs. In addition, QCRH had a few other nonrecurring items, including a $576,000 gain on the sale of certain nonperforming loans and a lower-than-normal effective tax rate, which were offset by increased charges for the loan loss provision and loan/lease expense that were hit by yearend clean-up costs, as well as higher marketing and postage costs related to the rebranding of the remaining CNB branches and increased professional and data processing costs stemming from the CNB acquisition.

All-in-all, it was a pretty messy quarter (and year) due to the CNB acquisition, but the groundwork has been laid for the combined company to achieve good performance right out of the starting gate in 2014.

That said, we are reducing our 2014 diluted EPS estimate by $0.05 to $1.75 from $1.80, as we have increased our estimate for average diluted shares outstanding to 8.3 million shares from 8.075 million shares previously. Our net earnings estimate after preferred stock dividends remains the same at $14.5 million, up 23% from 2013's $11.8 million.

Relative to our $0.57 estimate, fourth quarter diluted EPS fell $0.07 short. We note that our estimate is not strictly comparable to reported results as our estimate was based on operating earnings, excluding one-time items.

However, we still got some things wrong. Our projection for net interest income was too optimistic, our loan loss provision estimate was too low, and certain expenses (namely professional and data processing costs, loan/lease expense, marketing, and postage) came in significantly higher than we expected. In addition, we got loan growth wrong as QCRH experienced its first down quarter in over two years, a disappointment for the Company (excluding the impact of branch sales, loans declined $24.0 million, or 2%).

On the positive side, nonperforming loans fell $4.4 million, or 18%, during the fourth quarter, attributable to substantially increased net charge-offs ($2.6 million versus $0.5 million in both the previous quarter ands the prior year) and sales/pay-offs of certain nonperforming loans.

Also, QCRH completed the conversion of the Series E preferred stock, a major accomplishment for the Company, adding almost 100 basis points to the tangible common equity ratio and eliminating $1.75 million in annual preferred dividends.

Compared to the year-ago quarter, fourth quarter net earnings after preferred stock dividends jumped 26% to $3.1 million from $2.4 million, largely due to effects of the CNB acquisition, including nonrecurring items. On a diluted per share basis, EPS increased only $0.01, or 2%, to $0.50 from $0.49, reflecting a 23% 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.

For the year, QCRH boasted a 29% climb in net earnings (after preferred stock dividends) to $11.8 million in 2013 from $9.1 million in 2012. Diluted EPS rose only 12% to $2.08 from $1.85 in the prior year, again hurt by distortions caused by the CNB acquisition and the Series E preferred conversion.

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

Net Interest Income

Net interest income rose $2.6 million, or 18%, year over year to $16.9 million, as a 19% gain in average interest-earning assets combined with a 2 basis-point rise in the net interest margin to 3.04% to produce

this result. The Company stated that CNB branch sales at the beginning of the quarter reduced interest-earning assets, causing net interest income to be $0.4 million lower than it otherwise would have been.

The NIM gain reflected a 15 basis-point decrease in the yield on average interest-earnings assets to 3.78% that was more than offset by a 26 basis-point drop in average deposit costs to 0.35% and a 6 basis-point fall in borrowing costs to 2.44%.

The yield on the loan and lease receivables portfolio fell 41 basis points year over year to 4.65%, 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. The Company believes that lending spreads are now at a trough and does not expect them to decline significantly from this point forward.

We note that the yield on the securities portfolio advanced 11 basis points to 2.42%, 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 $0.4 million below our $17.3 million estimate, as average interest-earning assets were $60 million, or 2 ½%, lower than our estimate and the 3.04% NIM was 1 basis point beneath our 3.05% estimate, as well.

We expect that the addition of CNB's higher margin loan portfolio will partly 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 maintaining our 3.02% estimate for 2014. This compares to the 3.03% that was actually posted in 2013.

Noninterest Income

Results were also boosted by a strong a 72% year-over-year gain in noninterest income to $7.7 million, including a $2.3 million gain on the sale of four CNB branches and a $576,000 gain on the sale of nonperforming loans. Excluding these items, noninterest income was $4.8 million (versus our $5.2 million estimate, with the shortfall largely due to lower-than-expected gains on loan sales). The CNB acquisition helped propel a 42% gain in trust department fees to $1.4 million and a 25% increase in deposit service fees to $1.1 million despite a $150,000 loss in deposit fees due to the CNB branch sales.

For 2014, we are increasing our estimate of noninterest income to $21.1 million from $20.7 million, down 18% year over year from 2013. While we expect solid growth in trust department and deposit service fees in 2014 and higher gains on loan sales, reduced 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 surged $0.9 million, or 79%, year over year and $0.6 million, or 45%, quarter over quarter to $1.9 million (versus our $1.2 million projection), as the Company took the opportunity to write off loans at yearend.

Going forward, our estimate for the loan loss provision for 2014 remains $5.4 million, which represents a 9% decline from 2013's $5.9 million. 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.

Noninterest Expense

Noninterest expense rose $4.8 million, or 36%, year over year to $18.2 million, including $1.2 million in acquisition and data costs. Excluding this item, noninterest expense was $17.0 million versus our $15.8 million estimate, as certain expense items were higher than expected. Specifically, professional & data processing fees were $0.5 million larger (and included some one-time costs), loan/lease expense was

$0.4 higher than our estimate (and included some fourth quarter clean-up costs), and marketing and postage were $0.3 million more than we had anticipated (and included some rebranding costs for CNB branches).

All line items increased year over year, with the largest impacts stemming from a 12 ½% rise in compensation expense to $9.8 million, a 99% surge in professional and data processing fees to $1.9 million, a 119% increase in loan/lease expense to $0.6 million, and a 49% jump in marketing costs to $0.6 million.

The Company's efficiency ratio deteriorated, increasing 280 basis points to 74.0% compared to 71.2% in 2012's fourth quarter.

We expect operating efficiency to improve in 2014 as CNB becomes fully integrated, and have estimated an efficiency ratio of 71.3% in full-year 2014, which compares to 72.0% actually reported in 2013.

Income Taxes

The Company's effective tax rate was 13.7% in the fourth quarter, compared to 24.4% in the year-ago quarter and our 25.0% estimate, adding about $0.6 million, or $0.10, to the bottom line. We are maintaining our 25.0% for 2014. This compares to a 23.6% tax rate that was actually posted in 2013.

Noncontrolling Interests

In August 2012, the remaining 20% of m2 Lease Funds, LLC, the Company's leasing subsidiary, was purchased, providing for 100% equity ownership. The transaction was structured in two payments, with the first payment recorded in August 2012, and the final payment scheduled three years later in August 2015. This purchase eliminates about $2.4 million of noncontrolling interests from QCRH's balance sheet and also a $0.2 million quarterly deduction from net income. However, compensation costs will increase by an amount equivalent to the noncontrolling interest deduction. This means that there will be no impact on net income and earnings per share.

Net Income

QCRH posted fourth quarter net earnings attributable to common shareholders of $3.1 million, or $0.50 per diluted share, up 26% from $2.4 million ($0.49 diluted EPS) reported in the year-ago quarter. This compares to our $3.4 million net income estimate ($0.57 diluted EPS).

Profitability

QCRH posted a 10.2% ROE and 0.63% ROA for the fourth quarter of 2013, compared to a 9.3% ROE and 0.63% ROA for the fourth quarter of 2012.

Loans and Asset Quality

Loans fell $79 million, or 5%, sequentially to $1,460 million during the fourth quarter, including a $55 million reduction stemming from the sale of the CNB branches and $24 million of organic loan decline as payoffs outpaced new loans and the Company worked out certain nonperforming loans. This was a disappointment and represented the first decline in over two years.

Our estimate of loan growth in 2014 remains 5%. This compares to year-over-year growth of 13% in 2012 including CNB.

Nonperforming loans fell during the quarter $4.4 million, or 18%, to $20.5 million during the fourth quarter, attributable to substantially increased net charge-offs ($2.6 million versus $0.5 million in both the previous quarter and the prior year) and sales/pay-offs of certain nonperforming loans. Foreclosed assets, which includes $9.7 million of OREO, rose 15% to $10.1 million. As a percentage of total loans and OREO, total nonperforming assets improved, sliding by 10 basis points sequentially to 2.08% from 2.18% at the end of the third quarter, and 21 basis points year over year from 2.29%.

We expect asset quality to show further improvement in 2014 as the Company works though problem assets, with the estimated NPA ratio falling from 2.08% at yearend 2013 to 1.72 % by the end of 2014.

The loan loss allowance as a percent of nonperforming assets increased sequentially to 70% at the end of the quarter from 66% at September 30, 2013 and 67% at December 31, 2012. This was the result of a loan loss allowance that decreased to $21.4 million, or 1.47% of gross loans, from $22.1 million, or 1.43% of gross, at September 30, 2013 and $19.9 million, or 1.61% of gross loans at yearend 2012, 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 1.47% at December 31, 2013 from 1.61% at March 31, 2013 and from 1.55% at December 31, 2012, though improved from 1.38% at June 30, 2013.

Liquidity and Funding

During the fourth quarter, QCRH reduced cash and short-investments by $8 million to $114 million, while the securities portfolio declined $6 million to $697 million.

Within the securities portfolio, there were shifts from the previous quarter. Sequentially, US Agency securities declined 3% to $356 million, or 51% of the total securities portfolio (down from 55% at the end of the third quarter), while municipal securities rose 8% to $180 million, or 26% of the securities portfolio (down from 24% at the end of the third quarter), and residential mortgage-backed securities slid 5% to $157 million, or 23% of total securities (24% at the end of the third 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 December 31, 2013, noninterest-bearing demand deposits represented 33% of total deposits of $1.6 billion (up from 30% at September 30, 2013), while interest-bearing demand deposits were fell to 43% (down from 45% at September 30, 2013), time deposits were 20% (down from 22% at September 30, 2013), and brokered deposits were 4% (flat with September 30, 2013).

Capital Adequacy and Dividends

The Company’s capital adequacy ratios improved during the quarter. The Tier 1 capital ratio rose 53 basis points to 11.37% at the end of 2013’s fourth quarter from 10.84% at September 30, 2013, and the Total capital ratio gained 51 basis points to 12.76% from 12.25%. This improvement was the result of the sale of the CNB branches.

In addition, tangible common equity to tangible assets jumped 122 basis points, rising to to 4.71% at December 31, 2013, largely due conversion of the Series E preferred stock into common shares.

As a result of dilution from the Series E conversion, tangible book value per share decreased during the fourth quarter, by $0.61 per share, tumbling to $14.28 from $14.89.

On November 8, 2013, QCRH announced its regular semi-annual cash dividend of $0.04 per share paid on January 7, 2014 to stockholders of record on December 20, 2013. 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 balance of the SBLF preferred stock ($10 million in 2014’s first quarter, and the $20 million balance in 2014’s second quarter 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 in 2014 to 5.12% at yearend 2014, 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 to 5.12% 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 mid 2014.

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 December 31, 2013 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.

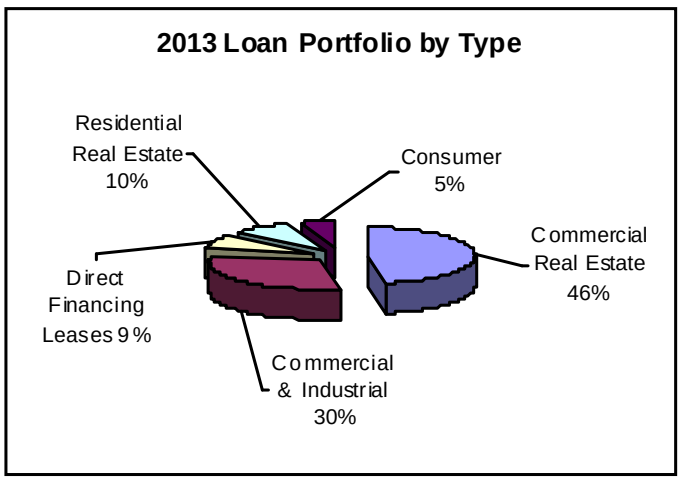
By far the largest of these subsidiaries is QCBT, which accounts for $1.25 billion, or approximately 52%, of QCRH's total assets, and is also the oldest of its subsidiaries, having begun operations in January 1994. Its five offices are located in Bettendorf and Davenport, Iowa and Moline, Illinois. CRBT, 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.

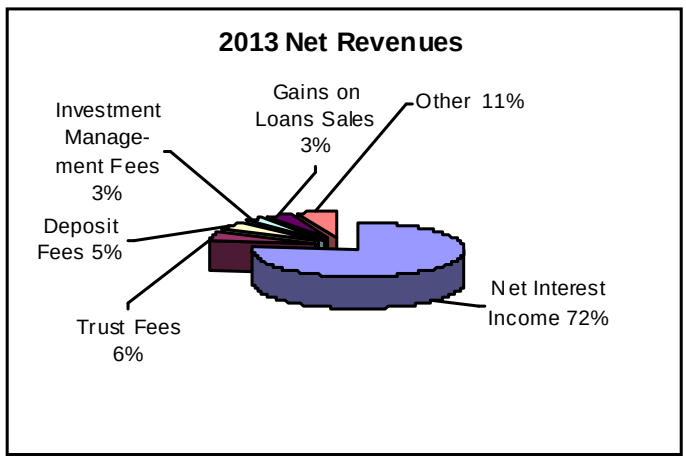
QCRH has disposed of several operating subsidiaries over the past few years as they did not contribute significantly to earnings and no longer fit into the Company's long-term strategic plans. These include: (1) the sale of the merchant credit card processing business and the liquidation of Quad City 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 $30 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 1.1% year to date and has outperformed the S&P 500’s 0.5% decline, but is short of the industry’s median price increase of 2.0%, 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 26% discount to the industry median P/E, based upon our diluted EPS estimate for 2014. This is 13 points worse than the five-year average historical discount of 13%. Applying the 13% historical average discount to our 2014 EPS estimate of $1.75 results in a price of roughly $20.50

Turning to Price/Tangible Book Value, QCRH is valued at 1.15X versus the industry median of 1.25X. While this is 8% below the industry median, it is also 8% 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 1.25X ratio to estimated book value for QCRH twelve months out results in a price of approximately $20.00.

Taking the midpoint of these two valuation measures results in a price of $20.25, compared to the current stock price of $17.21. When price appreciation of 17 ½% is combined with the dividend yield, this represents a total return of over 18%, above our expectations for gains in the broader market index over the next year.

Accordingly, we are maintaining our Buy recommendation on QCRH, as well as our twelve-month target price of $20.25.

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	**1.1**	**8.3**	**9.8**		**14.2**	**1.15**	**10.3**	**6.5**	**0.63**	**0.41**	**0.5**
S&P 500	(0.5)	18.0	15.7	14.7	16.7	4.8	24.7	-----	8.7	-----	2.1
Median	**2.0**	**13.1**	**13.3**	**12.3**	**16.4**	**1.25**	**9.1**	**4.8**	**0.88**	**0.43**	**1.4**
Average	3.8	17.7	15.1	12.9	23.8	1.2	9.2	2.5	0.9	0.3	1.4
High	35.1	174.5	35.7	22.6	94.8	2.3	29.5	14.1	3.7	2.0	4.0
Low	(13.5)	4.5	8.8	8.8	6.4	0.7	(7.0)	(69.8)	(0.8)	(1.7)	-----

*Trailing twelve months

QCR Holdings, Inc.

Income Statement and Balance Sheet

(Dollars in millions, except per share data)

Summary Financial Data	12/08	12/09	12/10	12/11	12/12	12/13 P	12/14 E
Net interest income	45.0	50.4	49.9	54.1	57.6	64.1	67.5
Non-interest income	13.6	15.6	15.4	17.5	16.7	25.8	21.1
Total net revenue	58.6	66.0	65.3	71.6	74.3	89.9	88.6
Loan loss provision	9.2	17.0	7.5	6.6	4.4	5.9	5.4
Non-interest expense	42.3	46.7	48.5	51.0	52.3	64.4	63.2
Income taxes & other	3.9	4.4	6.8	8.4	8.5	7.8	5.5
Zacks adjusted income before NRI	3.2	(2.1)	2.5	5.6	9.1	11.8	14.5
GAAP net income	4.9	(2.1)	2.5	4.4	9.1	11.8	14.5
Diluted EPS before NRI	0.69	(0.46)	0.53	1.17	1.85	2.08	1.75
Reported EPS	1.06	(0.46)	0.53	0.92	1.85	2.08	1.75
Dividends per share	0.08	0.08	0.08	0.08	0.08	0.08	0.08
Liquid assets	287.8	417.3	546.0	638.5	612.7	628.3	603.6
Loans & leases, gross	1,214.7	1,244.3	1,172.5	1,200.7	1,287.4	1,460.3	1,534.7
Total assets	1,605.6	1,779.6	1,836.6	1,966.6	2,093.7	2,395.0	2,467.6
Core deposits	711.3	761.5	844.2	960.9	1,129.5	1,397.3	1,468.5
Purchased funds	367.6	340.9	307.1	263.6	266.2	268.2	325.0
Long-term debt	310.4	378.8	388.5	358.1	355.0	395.8	350.0
Shareholders' equity	90.6	123.9	130.9	142.4	140.4	147.6	131.1
Profitability							
Return on avg assets	0.32%	0.10%	0.36%	0.51%	0.62%	0.64%	0.62%
Return on avg equity	5.66%	1.43%	5.03%	7.09%	8.90%	10.24%	11.29%
Net interest margin	3.32%	3.15%	2.92%	3.08%	3.10%	3.03%	3.02%
Loan loss provision % avg assets	0.59%	0.98%	0.41%	0.35%	0.22%	0.25%	0.22%
Noninterest income % avg assets	0.88%	0.91%	0.84%	0.92%	0.82%	1.11%	0.87%
Noninterest expense % avg assets	2.73%	2.71%	2.64%	2.67%	2.58%	2.76%	2.60%
Preprovision pretax income % avg assets	1.04%	1.12%	0.91%	1.08%	1.09%	1.09%	1.04%
Tangible efficiency ratio	73%	72%	74%	73%	70%	72%	71%
Payout ratio	8%	(18)%	15%	9%	4%	4%	5%
Asset Quality							
Net charge-offs % avg loans	0.24%	1.00%	0.79%	0.70%	0.27%	0.31%	0.25%
Allowance % loans	1.47%	1.81%	1.74%	1.56%	1.55%	1.47%	1.50%
NPAs % loans & related assets	2.08%	3.22%	4.24%	3.35%	2.29%	2.08%	1.72%
Allowance % NPAs	70%	56%	41%	46%	67%	70%	87%
Liquidity & Funding							
Liquid assets % purchased funds	78%	122%	178%	242%	230%	234%	186%
Core deposits % loans	59%	61%	72%	80%	88%	96%	96%
Liquid assets % assets	18%	23%	30%	32%	29%	26%	24%
Loans % assets	76%	70%	64%	61%	61%	61%	62%
Capital Adequacy							
Total equity % assets	5.64%	6.96%	7.13%	7.24%	6.71%	6.16%	5.31%
Tangible equity % assets	5.46%	6.79%	6.97%	7.09%	6.56%	5.96%	5.12%
Tier 1 capital ratio	8.36%	11.14%	12.12%	12.24%	11.27%	11.37%	
Total capital ratio	10.39%	12.52%	13.70%	13.84%	12.71%	12.76%	
Parent Company Statistics							
Interest coverage	3.1X	1.4X	0.7X	2.8X	5.5X	2.0X	2.0X
Interest & dividend coverage	1.8X	0.5X	0.3X	0.8X	1.4X	0.9X	1.4X
Short-term debt coverage	2.0X	N/A	N/A	N/A	N/A	N/A	N/A
Total debt coverage	0.2X	N/A	N/A	N/A	N/A	N/A	N/A
Double leverage	146.1%	133.4%	132.5%	128.9%	130.8%	130.2%	157.1%

QCR Holdings, Inc.

Income Statement and Balance Sheet

(Dollars in millions, except per share data)

	2012				2013			
Summary Financial Data	**Q1 A**	**Q2 A**	**Q3 A**	**Q4 A**	**Q1 A**	**Q2 A**	**Q3 A**	**Q4 P**
Net interest income	14.2	14.5	14.6	14.3	14.2	15.7	17.3	16.9
Non-interest income	4.0	4.1	4.1	4.5	5.2	7.0	5.9	7.7
Total net revenue	18.2	18.6	18.7	18.8	19.4	22.7	23.2	24.6
Loan loss provision	0.8	1.0	1.5	1.1	1.1	1.5	1.4	2.0
Non-interest expense	12.7	13.1	13.0	13.4	14.0	15.2	17.0	18.2
Income taxes & other	2.4	2.4	2.0	1.9	1.8	2.8	1.8	1.3
Zacks adjusted income before NRI	2.3	2.1	2.2	2.4	2.5	3.2	3.0	3.1
GAAP net income	2.3	2.1	2.2	2.4	2.5	3.2	3.0	3.1
Diluted EPS before NRI	0.48	0.44	0.44	0.49	0.49	0.59	0.51	0.50
Reported EPS	0.48	0.44	0.44	0.49	0.49	0.59	0.51	0.50
Dividends per share	-----	0.04	-----	0.04	-----	0.04	-----	0.04
Liquid assets	625.4	639.1	594.7	612.7	645.7	655.0	656.8	628.3
Loans & leases, gross	1,211.7	1,213.3	1,244.3	1,287.4	1,291.8	1,530.7	1,539.4	1,460.3
Total assets	1,993.0	2,043.4	2,023.9	2,093.7	2,144.0	2,446.8	2,485.7	2,395.0
Core deposits	1,052.2	1,070.9	1,098.7	1,129.5	1,175.9	1,467.1	1,492.2	1,397.3
Purchased funds	266.2	265.2	266.2	266.2	266.2	293.8	268.2	268.2
Long-term debt	354.4	357.5	349.0	355.0	358.0	348.7	369.8	395.8
Shareholders' equity	143.5	136.9	139.0	140.4	142.2	145.4	148.0	147.6
Profitability								
Return on avg assets*	0.65%	0.61%	0.60%	0.63%	0.62%	0.70%	0.62%	0.63%
Return on avg equity *	9.00%	8.54%	8.78%	9.28%	9.25%	11.03	10.44%	10.19%
Net interest margin	3.09%	3.16%	3.16%	3.02%	3.02%	2.99%	3.07%	3.04%
Loan loss provision % avg assets*	0.16%	0.21%	0.29%	0.22%	0.20%	0.26%	0.22%	0.33%
Noninterest income % avg assets*	0.79%	0.81%	0.81%	0.87%	0.99%	1.20%	0.97%	1.27%
Noninterest expense % avg assets*	2.54%	2.61%	2.57%	2.60%	2.65%	2.55%	2.77%	2.99%
Preprovision pretax inc.% avg assets*	1.08%	1.09%	1.13%	1.05%	1.03%	1.35%	1.01%	1.05%
Tangible efficiency ratio	70%	71%	70%	71%	72%	65%	75%	74%
Payout ratio	-----	9%	-----	8%	-----	7%	-----	8%
Asset Quality								
Net charge-offs % avg loans*	0.19%	0.44%	0.26%	0.17%	0.07%	0.32%	0.12%	0.71%
Allowance % loans	1.57%	1.54%	1.56%	1.55%	1.61%	1.38%	1.43%	1.47%
NPAs % loans & related assets	3.19%	2.98%	2.33%	2.29%	1.83%	2.22%	2.18%	2.08%
Allowance % NPAs	49%	51%	67%	67%	88%	62%	66%	70%
Liquidity & Funding								
Liquid assets % purchased funds	235%	241%	223%	230%	243%	223%	245%	234%
Core deposits % loans	87%	88%	88%	88%	91%	96%	97%	96%
Liquid assets % assets	31%	31%	29%	29%	30%	27%	26%	26%
Loans % assets	61%	59%	61%	61%	60%	63%	62%	61%
Capital Adequacy								
Total equity % assets	7.20%	6.70%	6.87%	6.71%	6.63%	5.94%	5.95%	6.16%
Tangible equity % assets	7.05%	6.55%	6.72%	6.56%	6.49%	5.69%	5.70%	5.96%
Tier 1 capital ratio	12.27%	11.52%	11.52%	11.27%	11.60%	10.82%	10.84%	11.37%
Total capital ratio	13.87%	13.14%	12.98%	12.71%	13.04%	12.20%	12.25%	12.76%

*Annualized.

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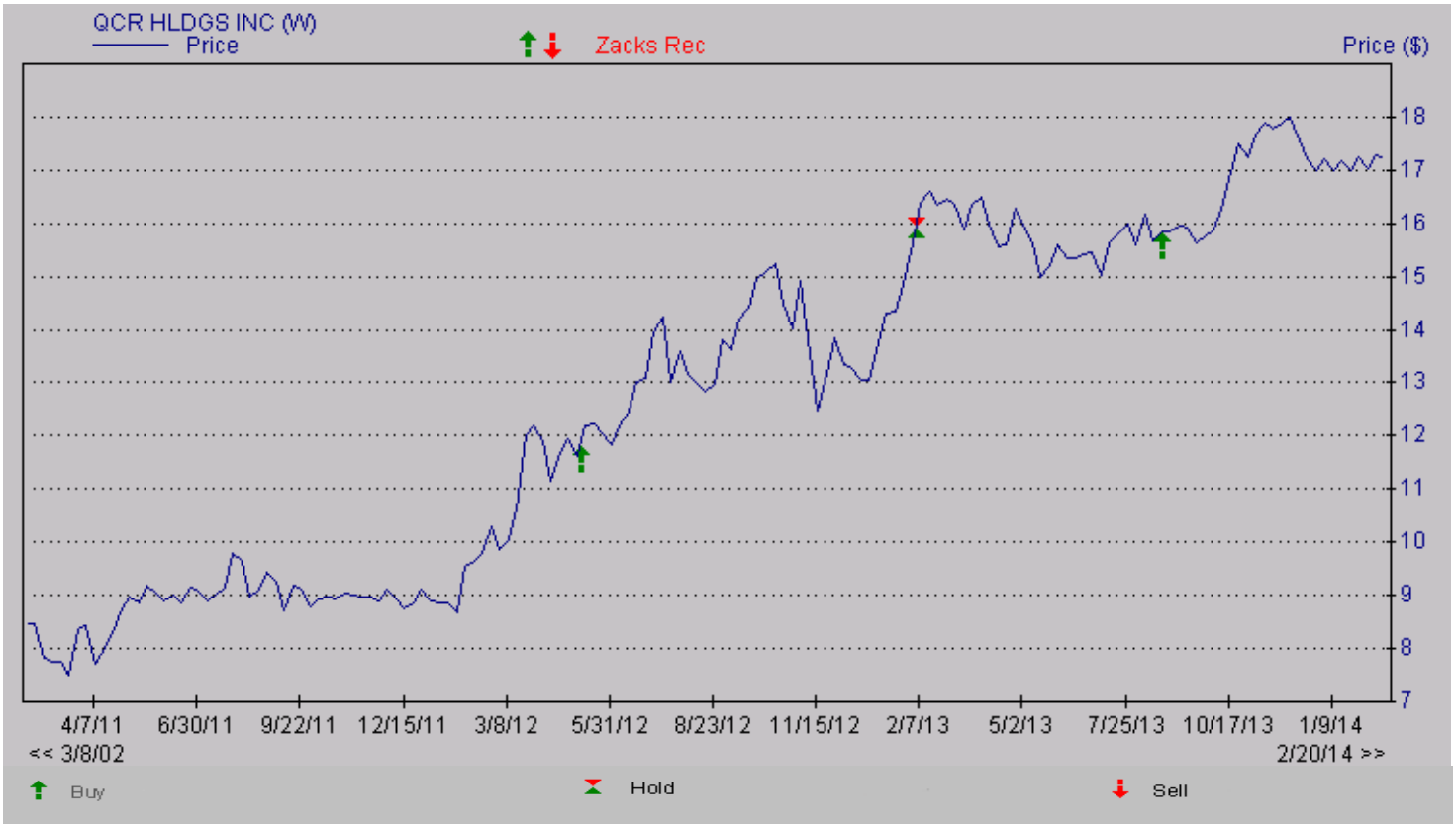

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