

AVAILABLE ON THE WEB AT [WWW.EQUITYRESEARCH.COM](http://www.equityresearch.com)

## Citizens Financial Services, Inc. (CZFS – OTC Pink)

107 Windel Dr., Suite 211

Raleigh  
North Carolina  
27609

919-876-8868 ph

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

**John A. Howard, CFA**  
**July 30, 2020**

<b>Price:</b>	\$48.75	<b>Diluted EPS 2018A:</b>	\$ 5.09	<b>P/E 2018A:</b>	9.6x
<b>52 Wk. Range:</b>	\$36.00 - \$69.99	(FY: DEC) <b>2019A:</b>	\$5.53	<b>2019A:</b>	8.8x
<b>Div/Div Yld: *</b>	\$1.80/3.7%	<b>2020E:</b>	\$5.55	<b>2020E:</b>	8.8x
<b>Shrs/Mkt Cap:</b>	4.0 mm / \$194 mm	<b>Book Value: **</b>	\$46.35	<b>Price/Book Value: **</b>	1.05x

\* Cash dividend is most recent regular quarterly dividend (annualized), does not include special dividends.

\*\* Tangible book value is \$37.54.

### Background

Citizens Financial Services, Inc. (“the Company”) of Mansfield, Pennsylvania, is a financial holding company for First Citizens Community Bank, a full-service community bank. First Citizens Community Bank (the “Bank”) was founded in 1872, and as of June 30, 2020, the Company had total assets of approximately \$1.8 billion. The Company has completed various acquisitions, such as the acquisition of The First National Bank of Fredericksburg (“FNB”) in 2015, the S&T Bank branch located in State College, PA in December of 2017 and MidCoast Community Bancorp, Inc. in April 2020. The Company currently has offices in Tioga, Bradford, Potter, Clinton, Union, Lebanon, Berks, Schuylkill, Lancaster and Centre counties in Pennsylvania and one location in Wellsville (Allegheny County), New York. It also has offices in Wilmington and Dover, DE. The region has a diverse economic base, and has benefited from the Marcellus Shale, an area throughout much of Appalachia that contains significant untapped natural gas reserves. Citizens Financial Services, through its subsidiaries, focuses on highly personalized service and offers a variety of products and services to individuals and small- to medium-sized businesses. According to the American Bankers Association, it is the number two agricultural lender in Pennsylvania, and it is a key element of serving the ag-rich regions of Lebanon and Lancaster. Through its Investment and Trust Services division, a variety of brokerage services are offered, such as professional asset management, estate planning, mutual funds and annuities, as well as life insurance, mineral management services, financial planning and trust administration. The Company’s stock is traded on the OTC Pink market under the symbol “CZFS.”

### Earnings Exceeded Projections, Pretax “Normalized” Earnings Were Up 32%

Citizens Financial Services, Inc. reported a great quarter in the three months ended June 30, 2020. First, it completed the acquisition of MidCoast Community Bancorp (“MidCoast”), the Wilmington, DE based bank with roughly \$260 million in assets. (The transaction closed on April 17, 2020, so most of its operations were included in 2020’s second quarter results.) As we have mentioned in previous reports, this transaction expands the Company’s footprint, significantly grows its balance sheet and provides for compelling cost savings opportunities. It was also a commendable quarter in that the Company continued to actively participate in the SBA’s Paycheck Protection Program (“PPP”), funding 570 loans (totaling \$53.7 million) as of June 30, 2020. These loans will generate more than \$2 million in fees over their respective lives. Finally, it was a great quarter from an earnings standpoint. Despite \$1.8 million in merger-related costs, quarterly earnings were higher (EPS increased 2%) than in the year-ago quarter. In fact, when we exclude the merger-related expenses, as well as the provision and nonrecurring items, we see the adjusted pretax income was more than \$8.0 million in the quarter, well above \$6.1 million in the year-ago quarter.

**SYMBOL: CZFS**

**TOTAL ASSETS: \$1.8 BB**

**HQ: MANSFIELD, PA**

**CONTACT:**  
**GINA BOOR**  
**(570) 662-2121**

#### 2<sup>ND</sup> QUARTER HIGHLIGHTS:

**THE SECOND QUARTER OF 2020 WAS SIGNIFICANT IN THAT:**

- **MIDCOAST DEAL CLOSED**
- **THERE WAS ACTIVE PPP PARTICIPATION**
- **STRONG OPERATING PERFORMANCE**

**570 PPP LOANS WERE FUNDED AMOUNTING TO \$53.7 MILLION**

**PRETAX INCOME BEFORE THE PROVISION AND NONRECURRING ITEMS WAS UP 32%**

Quarterly Results (\$000s)	2019			2020	
	Q2	Q3	Q4	Q1	Q2
<b>Net Income</b>	<b>4,846</b>	<b>5,196</b>	<b>5,043</b>	<b>4,531</b>	<b>5,338</b>
Pretax Income	5,776	6,262	6,046	5,420	6,392
Eliminate:					
Provision	350	400	525	400	550
Payoff - Purch. Credit Imp. Loan	-	-	-	-	(600)
Merger/Nonrecurring expenses	-	275	191	376	1,803
Security Gains/Losses	(30)	(37)	(66)	254	(128)
<b>Adjusted Pretax Earnings</b>	<b>6,096</b>	<b>6,900</b>	<b>6,696</b>	<b>6,450</b>	<b>8,017</b>

**EPS: \$1.39 vs. \$1.36**

**THE PROVISION INCREASED SUBSTANTIALLY AND THERE WERE \$1.8 MILLION IN MERGER EXPENSES IN Q2 2020**

**NONINTEREST INCOME, EXCLUDING SECURITY GAINS, WAS DOWN MODESTLY**

**ROAA AND ROAE (BEFORE MERGER COSTS) INCREASED AND WERE SUPERIOR TO THE PA PEER GROUP MEDIAN**

**FIRST HALF HIGHLIGHTS:**

**NET INCOME GREW 7%, ADJUSTED PRETAX INCOME WAS UP 29%**

**EPS: \$2.67 vs. \$2.60**

**BALANCE SHEET GROWTH BENEFITED FROM MIDCOAST ACQUISITION**

**THE ACQUISITION ADDED THREE BRANCHES IN DELAWARE TO CITIZEN'S FRANCHISE**

**CITIZENS FINANCIAL HAS AN EXCELLENT OPPORTUNITY TO CONTINUE ITS ACQUISITION STRATEGY**

**NPAS WERE DOWN 2% FROM 3/31/20 AND 14% FROM 6/30/19**

**NPAS/ASSETS: 0.79%**

**RESERVES/LOANS: 1.09%**

**EPS:**

**2018A: \$5.09**

**2019A: \$5.53**

**2020E: \$5.55**

In terms of specific results, net income was \$5.3 million, or \$1.39 per diluted share, for the second quarter of 2020, which was up from \$4,846,000, or \$1.36 per diluted share, in the year-ago quarter. Net interest income was quite strong, increasing 32% to \$16,286,000 from \$12,336,000 in the year-ago quarter. Most of that increase obviously came from the inclusion of MidCoast. Partly offsetting some

(% , ANNUALIZED)				
	Q2 19	Q2 20	Excluding Merger Costs Q2 20	Pennsylvania Bank Peer Median (Core)
<b>ROAA</b>	1.34	1.25	1.58	0.85
<b>ROAE</b>	13.09	12.28	15.56	7.67

of this growth was a \$200,000 increase in the provision for loan losses from \$350,000 to \$550,000. Noninterest income (excluding net security gains) was down 3% to \$1,941,000 in the second quarter of 2020 from \$1,997,000 in the year-ago quarter, while noninterest expense (excluding merger costs) totaled \$9,610,000, up 17% from \$8,237,000 over this period. Profitability ratios remained excellent. Excluding merger-related costs, ROAA and ROAE both improved from the year-ago quarter, as can be seen from the adjacent chart. Moreover, the profitability ratios were far superior to the median ratios for the Company's peer group, which included 53 Pennsylvania banks with assets between \$250 million and \$3 billion.

For the first half of 2020, Citizens reported net income of \$9,869,000, or \$2.67 per diluted share, which was up 7% from \$9,251,000, or \$2.60 per diluted share, in the first half of 2019. Results were likewise impacted by a higher provision, merger-related expenses and security gains/losses. Pretax income before the provision and nonrecurring items increased 29%. Net interest income grew 20%, noninterest income (excluding net security gains/losses) was up less than 1% and noninterest expense (excluding merger expenses) grew 10% compared to the year-ago period. Balance sheet growth was strong over the past year, benefiting from the recently completed acquisition. Specifically, from June 30, 2019 to June 30, 2020, total assets and loans grew 24%, while deposits were up 28%. Loan growth also benefited from the PPP obviously. (Not surprisingly, organic loan growth was negative due to early payoffs and low loan demand in the first half of 2020.) Citizens Financial remains well capitalized at June 30, 2020, with shareholders' equity of \$183 million, or 10.2% of total assets.

### **MidCoast Acquisition Completed During the Second Quarter of 2020**

As was stated previously, the acquisition of MidCoast was completed on April 17, 2020. The addition of MidCoast adds three branches to the franchise, which are located in Dover, DE, west of Wilmington, DE and North Wilmington, DE. As part of the transaction, the Company added loans of \$223 million and deposits of \$209 million. Based on the closing price on April 17, 2020, the deal value was approximately \$26.9 million, which was a modest premium to book value. We continue to believe Citizens Financial is in an excellent position to create long-term shareholder value by using its stock as a currency to acquire smaller institutions at attractive (lower) multiples. This opportunity is especially compelling given the disciplined cost containment and efficiency of Citizens Financial.

### **NPAs Were Down 14% from June 30, 2019**

The Company's nonperforming assets continued to decrease at the end of 2020's first half, with NPAs at \$14.2 million, or 0.79% of total assets, at June 30, 2020, down 2% from \$14.5 million, or 0.99% of total assets, at March 31, 2020, and down 14% from \$16.6 million, or 1.14% of total assets, at the year-ago date. NPAs mainly consisted of nonaccrual loans (\$11.3 million) followed by OREO (\$3.1 million). The allowance for loan losses was \$14.8 million, or 1.09% of total assets, at June 30, 2020, up 11% from \$13.3 million, or 1.21% of loans, at the year-ago date.

### **Projections**

Projections remain challenging to estimate accurately. However, we are tentatively projecting 2020 earnings of \$20.9 million, or \$5.55 per diluted share. As stated previously, actual earnings could vary substantially from these projections given the uncertainties of the COVID-19 crisis.

#### **ADDITIONAL INFORMATION UPON REQUEST**

Copyright © 2020 Equity Research Services, Inc. All rights reserved. This material is for your information only and is not a solicitation, or an offer, to buy or sell securities mentioned. Equity Research Services, Inc. ("ERS") is a firm involved in financial advisory, equity research, valuation and investor relations services. All reports generated by ERS for the purpose of investor relations are designated "Investor Relations Report," and ERS receives a fee (from the company whose securities are described) for producing such reports. ERS may also act in a financial advisory role to the company and the analyst may have an ownership in the shares of the company. The information contained herein has been obtained from sources we believe reliable but in no way is guaranteed by us. Furthermore, this report contains forward-looking statements and projections that are based on certain assumptions and expectations. Accordingly, actual results may differ considerably from those reflected in this report due to such factors as those which are listed in the Company's SEC filings. Any non-factual information in the report is our opinion and is subject to change without notice.