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

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**John A. Howard, CFA**  
**October 26, 2021**

<b>Price:</b>	\$61.10	<b>Diluted EPS 2020A:</b>	\$ 6.59	<b>P/E 2020A:</b>	9.3x
<b>52 Wk. Range:</b>	\$43.00 - \$65.00	(FY: DEC) <b>2021E:</b>	\$7.35	<b>2021E:</b>	8.3x
<b>Div/Div Yld: *</b>	\$1.88/3.1%	<b>2022E:</b>	\$6.80	<b>2022E:</b>	9.0x
<b>Shrs/Mkt Cap:</b>	4.4 mm / \$268 mm	<b>Book Value: **</b>	\$52.88	<b>Price/Book Value: **</b>	1.16x

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

\*\* Tangible book value is \$44.51.

### 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 September 30, 2021, the Company had total assets of approximately \$2.0 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. (“Midcoast”) in April 2020. The Company currently has offices in Tioga, Bradford, Potter, Clinton, Union, Lebanon, Berks, Schuylkill, Lancaster, Chester and Centre counties in Pennsylvania and one location in Wellsville (Allegany 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 three 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.

### Third Quarter of 2021 Earnings Surpassed Projections

As was expected, Citizens Financial Services reported a drop in third quarter earnings relative to the year-ago quarter, though results were actually a good bit better than we had been anticipating. There was a fair amount of “noise” in the quarterly comparisons, such as year-ago gains on the payoff of credit-impaired loans that were purchased in the FNB acquisition, as well as derivative income, neither of which were present in 2021’s third quarter results. Moreover, the year-ago quarter was unusually strong from a mortgage banking standpoint. Nevertheless, there were still a number of positives to the quarter, one being that EPS exceeded our forecast by \$0.16 per share, leading us to increase our earnings projection for the year. Based on that level of earnings, Citizens Financial’s profitability and efficiency measures remain impressive and were better than the majority of the Company’s peers. Balance sheet growth was also commendable. Finally, asset quality was good, with nonperforming assets in a favorable trend.

Net income in 2021’s third quarter was \$7.1 million, or \$1.79 per diluted share, as compared to \$8.0 million, \$2.02 per diluted share, in the year-ago quarter. Net interest income was up 1% to \$16.6 million in 2021’s third quarter from \$16.5 million in the year-ago quarter. Higher average earning assets (which grew 12% over the past year) essentially offset a 41-basis point decline in the net interest margin (which was 3.47% in 2021’s third quarter versus 3.88% in the year-ago quarter). Excluding derivative income and security gains, noninterest income totaled \$2.6 million for the third quarter of

**SYMBOL: CZFS**

**TOTAL ASSETS: \$2.0 BB**

**HQ: MANSFIELD, PA**

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

**EARNINGS WERE \$0.16 PER SHARE ABOVE EXPECTATIONS**

**EPS: \$1.79 vs. \$2.02**

**NET INTEREST INCOME GREW ABOUT 1%**

**AVERAGE EARNING ASSETS WERE UP ABOUT 12%, WHICH OFFSET PRESSURE ON MARGINS**

**NONINTEREST EXPENSE WAS UP 7%, DUE TO HIGHER SALARIES AND BENEFITS**

**THE COMPANY'S ROAA AND ROAE WERE BETTER COMPARED TO THE MAJORITY OF PA PEERS**

**THE ROAA WAS THE SIXTH HIGHEST OF THE PEER GROUP**

**THE NET INTEREST MARGIN WAS 36 BASIS POINTS ABOVE THE PEER GROUP MEDIAN, AND EFFICIENCY MEASURES WERE SUPERIOR AS WELL**

**FIRST NINE MONTHS HIGHLIGHTS:**

**EPS: \$5.62 vs. \$4.69**

**BALANCE SHEET GROWTH WAS FAIRLY STRONG AS WELL**

**EQUITY/ASSETS: 10.2%**

**NPAs/ASSETS: 0.50% vs. 0.84% AT THE YEAR-AGO DATE**

**RESERVES/LOANS: 1.20%**

**EPS:  
2020A: \$6.59  
2021E: \$7.35  
2022E: \$6.80**

2021, as compared to \$2.9 million in the year-ago quarter, with most that shortfall attributable to the previously alluded to drop in mortgage-related income. Noninterest expense was \$10.4 million in 2021's third quarter, up 7% from \$9.7 million in the year-ago quarter, while the provision for loan losses totaled \$400,000 versus \$550,000 in the year-ago quarter.

### Profitability and Efficiency Ratios Remain Quite Impressive Relative to Peers

Citizens Financial remains one of the most profitable banks in the state of Pennsylvania. As can be seen from the adjacent chart, nearly all of its performance metrics were superior to the medians of its peer group, which includes publicly traded banks in Pennsylvania with assets between \$250 million and \$3 billion. For example, the Company's ROAA was 1.40% (the sixth best of the total of 51 banks in the peer group), versus 0.99% for the peer group median; the ROAE was 13.65% compared to 10.64% for the peer median, and Citizens Financial's margin was 36 basis points above the peer group median. The annualized return on average tangible equity also was superior. Not surprisingly, Citizens Financial's efficiency ratio was also much better, at 52.6%, versus 64.4% for the peer group median. Much of this higher profitability stems from the Company's tight cost controls, as evidenced by the low noninterest expense-to-average assets ratios (2.06% on an annualized basis versus 2.36% for the peer median).

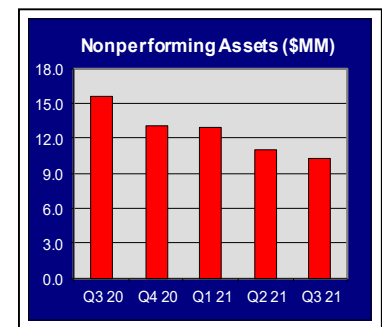
	PROFITABILITY AND EFFICIENCY RATIOS VS. PA PEERS (%)	
	CZFS	PA Peer Group Median
ROAA	1.40	0.99
ROAE	13.65	10.64
ROATE	16.25	11.50
Net Int. Mrgn.	3.47	3.11
Efficiency	52.6	64.4
Nonint. Exp./ Avg. Assets	2.06	2.36

### Year-to-Date Earnings Increased 24%

Earnings for the year-to-date period were likewise strong. Net income for the first nine months of 2021 was \$22.2 million, or \$5.62 per diluted share, up 24% from \$17.9 million, or \$4.69 per diluted share, in the year-ago quarter period. Both periods included nonrecurring items, such as \$2.2 million in expenses related to the acquisition of MidCoast in the year-ago period. But excluding the nonrecurring items (merger expense, life insurance proceeds, derivative income and nonrecurring gains and losses), pretax income before the provision increased 10%. Net interest income grew 8%, noninterest income (excluding security/derivative gains and losses) increased 27% and noninterest expense excluding merger expenses was up 10%. The provision for the first nine months of 2021 totaled \$1.6 million, up slightly from \$1.5 million in the year-ago period. In terms of the balance sheet, from September 30, 2020 to September 30, 2021, net loans grew 6%, deposits increased 12% and total assets were up 10%. Shareholders' equity was \$209 million, or 10.2% of total assets, at September 30, 2021.

### Asset Quality Trends Are Favorable

Nonperforming assets have dropped in each of the last five linked quarters, and totaled \$10.2 million, or 0.50% of total assets, at September 30, 2021, versus \$10.9 million, or 0.55% of total assets, at June 30, 2021, and \$15.6 million, or 0.84% of total assets, at the year-ago date. While NPAs declined, the allowance has continued to grow, and was \$17.3 million (1.20% of total loans) at September 30, 2021, up from \$15.2 million (1.11% of total loans), at the year-ago date.



### 2022 Projections Introduced

For the year 2021, we are estimating Citizens Financial will earn \$29.0 million, or \$7.35 per diluted share, up from \$7.05 projected previously. For 2022, we project net income of \$26.8 million, or \$6.80 per dilute share. The drop in earnings is expected due to the absence of fee accretion on PPP-related loans and the presence of \$1.2 million in life insurance proceeds paid in the first quarter of 2021.

### ADDITIONAL INFORMATION UPON REQUEST

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