

First Community Corporation

OUTPERFORM
FCCO (NASDAQ)
Price \$22.05
Price target \$25.00

Joseph Fenech
(312) 386-5909
jfenech@hovdegroup.com

Market Data

Market Cap (\$M)	\$147.7
Price / Tang. Book	1.83x
52-Week Range	\$14.80 - \$23.55
3-Mo. Avg. Daily Volume	5,299
Dividends	\$0.36
Dividend Yield	1.63%
Shares Outstanding (M)	6.7
Institutional Ownership	46.5%
Insider Ownership	7.9%

Financial Summary

As of September 30, 2017

Assets (\$M)	\$914.2
Tangible Book Value	\$12.02
Tang. Common Eq. / Tang. Assets	8.9%
ROA	0.94%
ROE	10.6%
Net Interest Margin	3.52%

Price Performance



Company Description

First Community Corporation stock trades on the NASDAQ Capital Market under the symbol "FCCO" and is the holding company for First Community Bank, a local community bank based in the Midlands of South Carolina. First Community Bank operates banking offices located in the Midlands, Aiken, Augusta, Georgia, and Greenville. In addition, two other lines of business, First Community Bank Mortgage and First Community Financial Consultants, a financial planning/investment advisory division.

3Q17 Earnings Review: A Strong Quarter Ahead Of Merger Close; Increasing Estimates; Maintain OUTPERFORM

EPS ESTIMATES

	Mar	Jun	Sep	Dec	Year	Growth	Est. Change	P/E
2017E	\$0.24A	\$0.26A	\$0.31A	\$0.30	\$1.11	16.8%	\$0.04	19.9x
2018E	\$0.30	\$0.33	\$0.34	\$0.34	\$1.31	18.0%	\$0.03	16.8x
2019E	\$0.34	\$0.35	\$0.36	\$0.37	\$1.42	8.4%	\$0.05	15.5x

Reported EPS	\$0.28
Core EPS	\$0.31
Consensus Estimate	\$0.28
Hovde Estimate	\$0.29

Core EPS ahead of us and consensus. FCCO reported 3Q17 EPS of \$0.28. We estimate core EPS of roughly \$0.31. Our core EPS estimate adjusts for (a) merger costs (\$228K or \$0.03 per share after-tax); (b) the net impact of a loss on early extinguishment of debt (\$165K or \$0.02); (c) a portion of reported securities gains, which were above trend this qtr (\$124K of \$0.01); and (d) asset sale gains (\$40K or \$0.01).

A strong quarter ahead of Cornerstone merger close. FCCO reported a solid quarter pretty much across the board, with no discernible weaknesses of note, and ahead of the completion of its acquisition of Cornerstone, which closed last Friday, 10/20. There were several takeaways from the release and our conversation with the company (FCCO does not hold a conference call).

- **First, loan growth was very healthy, at 11% annualized, reversing the one disappointing aspect of last qtr's results** (linked qtr decline in loan balances). The company continues to be impacted by payoff and paydown activity, which was about level with last quarter, but overall production levels picked up noticeably, particularly on the commercial side (\$49 mil., up from \$35 mil.), which translated to a stronger pace of net loan growth. Our sense was that loan growth probably isn't sustainable at quite the 3Q pace over the balance of the year, with some softness noted in the pipeline on our call, though management pointed to trailing 12 months loan growth of just shy of 9% as a more reasonable expectation (which is a bit higher than the 8% ann'l growth we had modeled).

Important Disclosures regarding Price Target Risks, Valuation Methodology, Regulation Analyst Certification, Investment Banking, Ratings Definitions, and any potential conflicts of interest begin on page 4 of this report. Past performance is no guarantee of future results.

- **Second, the quality of the funding profile and the robustness of the credit culture – the two hallmarks of the company in our view – continued to shine through in 3Q,** and the outlook suggests more of the same. FCCO reported a fifth consecutive quarter of core NIM expansion – up 3 bps linked qtr in 3Q, to 3.52%. The company's low cost deposit base (interest bearing liabilities cost at 0.44%, up 1 bp linked qtr), and balance sheet positioning (75% loan to deposit ratio, implying room to get more loaned up), leave it just about as well positioned for the next leg of the interest rate cycle as any company we cover. To date, management hasn't seen any real pressure on funding costs, and our sense was that it was unlikely to materialize near-term. Moreover, the acquisition of Cornerstone – with an estimated \$2 mil. loan mark, and slightly higher loan yields than FCCO – should be slightly accretive to NIM, which when coupled with our projection for slight core NIM expansion for the legacy company should translate to continued steady margin improvement. On the credit front, there just isn't all that much to discuss. The company has a nominal level of problem assets, at just under \$4 mil., and reported net recoveries in 3Q, while the classified loan ratio stood at just over 7% of regulatory capital. Provision was a little higher than we modeled in 3Q, but this was due to loan growth (which is a trade-off we'll gladly accept), and helped keep the allowance ratio flat at right around 1% of loans. With loan growth expected to slow a bit, we're modeling for provision between 2Q and 3Q (but closer to 3Q levels).
- **Third, costs were well-controlled, and represented the main positive variance in the quarter relative to our forecast.** Operating expenses fell just over 8% linked qtr (not annualized), due to the expected absence of one-off costs in 2Q related to the conversion to a new bank operating system, and to a lesser extent, a significantly lower level of marketing-related expenses (which is expected to normalize next quarter). Thus, on a stand-alone basis, we see costs migrating to about the midpoint of the 2Q and 3Q levels (about \$6.9 mil. quarterly). For 2018, there are a few important dynamics to consider. Most notably, the Cornerstone deal gets layered in for the full year. Also, the company is looking to supplement its expansion into new markets with additional full service offices. Specifically, the company is still looking to add an office in Greenville and hopes to find a site shortly, while it also recently received approval to add a branch in downtown Augusta. We estimate the combined annual cost of these new offices at around \$500K, with a payback period obviously attached to that investment – we are assuming these costs get layered in at some point next year, though we're not certain of exact timing at this point.
- **Fourth, core fee income came in right in line with our forecast, on higher deposit and investment advisory fees, partially offset by an expected pullback in mortgage banking.** Still, management noted on our call that 3Q was still the second-best quarterly result in mortgage since 2014 (2Q was by far the strongest), and cited the restructuring of that business, and the addition of new talent (mortgage banker in Greenville, with another one likely on the way soon in Augusta). Bottom line, there is reason to be enthused about the company's longer-term prospects in mortgage, with the caveat that 4Q is likely to evidence normal seasonal fluctuations.

Increasing estimates; Maintain OUTPERFORM rating. Our estimates move higher today – 2017 is up \$0.04 to \$1.11, 2018 is up \$0.03 to \$1.31, and 2019 is up \$0.05 to \$1.42. All in all, FCCO is a steady, high quality performer, with increasing scarcity value to the franchise in a consolidating Carolinas marketplace (we've made the point in the past that there are now just 5 banks with over \$1 bil. in assets in South Carolina). The acquisition of Cornerstone should add another favorable element to the story, and also propels the company over the \$1 bil. asset threshold that should help it to garner more attention from institutional investors, and puts the stock at least within striking distance of inclusion in the Russell (if not in 2018, then perhaps the following year). In short, there is lot to like about the story, and in our view, the stock. With Cornerstone now closed, we see M&A as more of a back burner issue at this point – the company seems well prepared to embark on another opportunity, particularly in the Upstate SC region – but the clear focus is to continue to organically build out the presence in newer markets (Augusta, GA; Greenville, SC). Valuation screens attractive, at 16.3x our 2018 estimate and 15.0x our 2019 forecast, but particularly on TBV, at 1.78x – the quality of the deposit franchise coupled with the scarcity factor and the pending cross of the \$1 bil. threshold suggests to us that it's only a matter of time before the stock garners a 2x handle on the TBV multiple. With about 17% upside to our target, we maintain our OUTPERFORM rating, and FCCO remains among our Top Ideas.

[Latest FCCO Company Report](#)

	\$0.24		\$0.26		\$0.31		\$0.30		\$1.11	\$0.30		\$0.33		\$0.34		\$0.34		\$1.31		\$1.42		
	1Q17A		2Q17A		3Q17A		4Q17E		2017E	1Q18E		2Q18E		3Q18E		4Q18E		2018E		2019E		
	% Δ	Actual	% Δ	Actual	% Δ	Actual	% Δ	Est.	% Δ	Est.	% Δ	Est.	% Δ	Est.	% Δ	Est.	% Δ	Est.	% Δ	Est.	% Δ	
NET INTEREST INCOME ASSUMPTIONS																						
Avg Loans	3.8%	557.5	0.2%	558.4	2.0%	569.5	2.0%	636.2	580.4	12.8%	2.0%	664.5	2.0%	677.8	2.0%	691.4	2.0%	705.2	684.7	18.0%	741.2	8.2%
Avg Securities and CDs	-4.8%	268.1	-2.0%	262.8	-3.2%	254.4	0.0%	289.0	268.6	-5.3%	0.0%	298.8	0.0%	298.8	1.0%	301.8	1.0%	304.8	301.0	12.1%	312.5	3.8%
Avg Other Earning Assets	-5.6%	12.9	2.7%	13.2	11.4%	14.7	0.0%	23.7	16.1	-7.5%	0.0%	26.2	0.0%	26.2	0.0%	26.2	0.0%	26.2	26.2	62.6%	26.2	0.0%
Average Earning Assets	0.8%	838.5	-0.5%	834.4	0.5%	838.6	13.2%	948.9	865.1	6.1%	4.3%	989.5	1.3%	1,002.8	1.6%	1,019.4	1.7%	1,036.2	1,012.0	17.0%	1,079.9	6.7%
Average Assets	0.8%	912.7	-0.4%	908.7	0.3%	911.2	13.2%	1,031.1	940.9	5.9%	4.3%	1,075.2	1.3%	1,089.7	1.6%	1,107.7	1.7%	1,126.0	1,099.6	16.9%	1,173.4	6.7%
Net Interest Margin		3.52%		3.49%		3.52%		3.55%	3.52%			3.56%		3.56%		3.57%		3.59%	3.57%		3.61%	
CREDIT ASSUMPTIONS																						
Provision / Avg Loans		0.08%		0.06%		0.12%		0.08%	0.08%	0		0.08%		0.13%		0.15%		0.15%	0.13%	1	0.15%	1
Net Charge-Off Ratio		-0.03%		0.00%		0.00%		0.05%	0.00%	0		0.05%		0.05%		0.08%		0.08%	0.06%	0	0.10%	1
Reserves / Loans		0.97%		0.99%		0.99%		0.98%	0.98%			0.97%		0.97%		0.97%		0.98%	0.98%		0.96%	
INCOME STATEMENT																						
Net Interest Income	3.8%	7,279	-0.2%	7,264	2.4%	7,436	13.9%	8,468	30,447	11.3%	3.4%	8,759	1.3%	8,876	3.1%	9,148	2.2%	9,351	36,134	18.7%	39,014	8.0%
Loan Loss Provision (Recovery)	-51.3%	116	-32.8%	78	112.8%	166	-28.1%	119	479	-38%	4.5%	125	70.0%	212	22.4%	259	2.0%	264	860	79%	1,112	29%
Deposit service charges	-6.2%	320	8.8%	348	8.9%	379	1.0%	383	1,430	1.8%	-6.5%	358	3.0%	369	2.0%	376	0.0%	376	1,479	3.4%	1,529	3.4%
Mortgage banking income	-22.7%	670	88.2%	1,261	-18.2%	1,032	-20.0%	826	3,789	12.0%	-2.5%	805	25.0%	1,006	7.5%	1,082	0.0%	1,082	3,974	4.9%	4,128	3.9%
Investment advisory fees	-2.3%	258	21.7%	314	7.0%	336	1.0%	339	1,247	9.9%	0.1%	340	0.1%	340	1.0%	343	1.0%	347	1,369	9.7%	1,493	9.1%
Other non-interest income	-1.5%	714	-																			

IMPORTANT DISCLOSURES:

Regulation Analyst Certification

I, Joseph Fenech, hereby certify the views expressed in this research report accurately reflect my personal views about the subject security(ies) or issuer(s). I further certify that no part of my compensation was, is, or will be, directly or indirectly, related to the specific recommendations or views expressed by me in this report.

Research Disclosures:

Hovde Group, LLC currently makes a market and/or will sell to or buy from customers on a principal basis, the securities of First Community Corporation

Analysts' Compensation: The equity research analysts responsible for the preparation of this report receive compensation based upon various factors, including the quality and accuracy of research, client feedback, competitive factors, and overall firm revenues, which include revenues from, among other business units, institutional equities and investment banking.

Hovde Group, LLC acted as financial advisor and provided investment banking services to First Community Corporation in connection with its merger with Cornerstone Bancorp.

Hovde Group, LLC expects to receive or intends to seek compensation for investment banking services from the following subject company in the next three months: First Community Corporation .

Hovde Group, LLC provided investment banking services for the following subject company within the past 12 months: First Community Corporation .

Price Target Risks & Related Risk Factors:

Investment risks associated with the achievement of the price target include, but are not limited to, a company's failure to achieve Hovde Group, LLC's earnings and revenue estimates; unforeseen macroeconomic and/or industry events that adversely affect demand for a company's products or services; product obsolescence; changes in investor sentiment regarding the specific company or industry; intense and rapidly changing competitive pressures; the continuing development of industry standards; the company's ability to recruit and retain competent personnel; and adverse market conditions.

Company Specific Risks:

Risks to the price target, rating, and EPS estimates include: (a) the announcing of a large acquisition that is dilutive to TBV/sh and/or implies considerable integration risk, (b) potential integration issues and/or delays in closing the company's pending acquisition, (c) the announcing of a large, dilutive capital raise, (d) the emergence of unanticipated credit deterioration, (e) NIM compression stemming from heightened deposit pricing competition amid rising ST rates and/or a flattening/inverted yield curve, (f) an economic downturn specific to the company's South Carolina footprint (likely slowing loan growth and pressuring credit quality), and (g) lower bank equity valuations.

Valuation Methodology:

Methodology for ratings and target prices includes both qualitative and quantitative factors including an assessment of industry size, structure, trends and overall sector attractiveness; management; competition; financial condition; and expected total return, among other factors. These factors are subject to change depending on overall economic conditions or industry or company-specific occurrences. Hovde Group, LLC analysts base valuations on a combination of forward looking earnings multiples and price-to-tangible book multiples. Hovde Group, LLC, believes this accurately reflects the strong absolute value of earnings, the strong earnings growth rate, the inherent profitability, and adjusted balance sheet factors. Additional company-specific valuation methodology is available through Hovde Group, LLC.

Company Specific Valuation:

Our price target of \$25.00 assumes the shares of First Community Corp. (FCCO) will trade at 17.6x our 2019 EPS est. one year out.

Definition of Investment Ratings:

OUTPERFORM: We expect the subject stock to outperform the industry benchmark (NASDAQ Bank) over the next 12 months.

MARKET PERFORM: We expect the subject stock will perform inline with the industry benchmark (NASDAQ Bank) over the next 12 months.

UNDERPERFORM: We expect the subject stock will underperform the industry benchmark (NASDAQ Bank) over the next 12 months.

Ratings Distribution:

Rating Category	Count	Percent	IB Serv./Past 12Mos.	
			Count	Percent
OUTPERFORM	25	34.72%	10	40.00%
MARKET PERFORM	47	65.28%	9	19.15%
UNDERPERFORM	0	0.00%	0	0.00%

For purposes only of FINRA ratings distribution rules, our Outperform rating falls into a buy rating category; our Market Perform rating falls into a hold rating category; and our Underperform rating falls into a sell rating category.

First Community Corporation Rating History as of 10/20/2017

powered by: BlueMatrix



ADDITIONAL INFORMATION AVAILABLE UPON REQUEST: Contact the Hovde Research Department at 1-855-559-6831, or write to 120 W. Madison Street, Suite 1200, Chicago, IL 60602.

For current company specific disclosures please see the most recently published company report, or contact the Hovde Group Research Department at the address or telephone number listed above. You may also access such disclosures, including price charts or other relevant disclosures, by visiting the following website: <https://hovdegrouppbluematrix.com/sellside/Disclosures.action>.

Other Disclosures:

This report has been prepared and issued by Hovde Group, LLC. The information contained in this report (except information regarding Hovde Group, LLC) was obtained from various sources which we believe to be reliable, but we do not guarantee its accuracy or completeness. Additional information is available upon request. The information, opinions or recommendations contained in this report speak only as of the date of this report and are subject to change without notice.

This report does not constitute an offer, or a solicitation of an offer, to buy or sell any securities or other financial instruments, including the securities of companies mentioned in this report. This report has been prepared and circulated for general information only and does not take into account the financial position or particular needs or investment objectives of any individual or entity. The securities or strategies discussed in this report may not be suitable for all investors. Investors must make their own determination of the appropriateness of an investment in any securities based on the legal, tax and accounting considerations applicable to such investors and their own investment strategy. Investors are cautioned that statements regarding future prospects may not be realized and that past performance is not necessarily indicative of future performance.

Hovde Group, LLC generally prohibits research analysts and members of their households from maintaining a financial interest in securities or options of any company that the analyst covers. This report or any portion thereof may not be reproduced or redistributed by any person for any purpose without the written consent of Hovde Group, LLC.

© Copyright 2017 Hovde Group, LLC. All rights reserved.