

North State Bancorp (Not Publicly Traded)

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ASSETS: \$1.2 BB

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4TH QUARTER HIGHLIGHTS:

**EARNINGS WERE MUCH
STRONGER THAN ANTICIPATED**

EPS: \$1.06 vs. \$0.51

**EARNINGS BENEFITTED FROM
STRONG MORTGAGE
OPERATIONS AND INCLUDED
\$1.8 MILLION IN FEES FROM
PPP LOANS THAT WERE REPAID**

**PARTIALLY OFFSETTING THESE
WINDFALLS WERE A HIGHER
PROVISION, HIGHER
CHARITABLE EXPENSES AND A
NEGATIVE SWING IN MERCHANT
AND OTHER LOAN FEES**

**ROAA, ROAE AND THE
EFFICIENCY RATIO ALL
IMPROVED SIGNIFICANTLY**

**ANNUALIZED ROAE REACHED
44%**

Price: *	\$16.00	EPS	2019A:	\$1.95	P/E	2019A:	8.2x
52 Wk. Range:	N/A	(FY: DEC)	2020A:	\$2.53		2020A:	6.3x
Distributions (Estimated):	\$1.65		2021E:	\$2.30		2021E:	7.0x
Shares:	6.1 mm	Book Value:		\$9.72	Price/Book Value:		1.65x

* Stock is not actively traded. Last known trade. Tangible book value is \$9.38.

Background

North State Bancorp (the “Company”) is a single bank holding company headquartered in Raleigh, North Carolina with approximately \$1.2 billion in assets as of December 31, 2020. Its bank subsidiary is North State Bank, a commercial bank that began operations on June 1, 2000. North State Bancorp serves Wake and New Hanover Counties through seven full-service offices. The Company focuses on serving the total banking needs of small businesses and individuals, professional firms, professionals, property management companies, churches, non-profits and any others who value a mutually beneficial banking relationship. Market areas include Raleigh, Garner, greater Wake County and New Hanover County. The Company is an S-Corporation for tax purposes.

Fourth Quarter EPS Beat Projections, Net Income More Than Doubled

For the fourth quarter of 2020, North State Bancorp reported excellent results, with earnings that more than doubled and EPS that exceeded projections by \$0.67 per share. This solid growth was largely due to the strength in the mortgage operation and the recognition of net PPP fees, and was achieved despite a higher provision for loan losses. Balance sheet momentum remained strong with especially good growth in deposits. Finally, nonperforming assets declined for the second quarter in a row, and asset quality remains quite good.

Net income was \$6,400,000, or \$1.06 per share, in the fourth quarter of 2020, more than double the \$3,025,000, or \$0.51 per share, earned in the year-ago quarter. The main drivers of the higher earnings were: 1) a surge in mortgage volume, leading to a sharp increase in fees from the mortgage operation and 2) the accretion of roughly \$1.8 million in net fees from PPP loans (some of which was normal accretion, some of which was accelerated due to loan forgiveness). Offsetting these two windfalls were: a much higher provision for loan losses (\$1,100,000 in 2020’s fourth quarter, versus no provision in the year-ago quarter) and higher charitable contributions in 2020’s fourth quarter (they were \$706,000 in 2020’s fourth quarter versus \$113,000 in the year-ago quarter.) Excluding all of these factors (even the net PPP fees), pretax income before the provision more than doubled to \$6.4 million from \$3.0 million. The Company’s profitability ratios were also unusually high, as can be seen in the adjacent table. In particular, we would note the annualized ROAE, which was 44% in 2020’s fourth quarter, up from 23% in the year-ago quarter. The net interest margin continued to face compression due to the lower interest rate environment, and was 3.41% in the fourth quarter of 2020, versus 4.06% in the year-ago quarter.

	ANNUALIZED PROFITABILITY RATIOS (%)		
	Q4 19	Q4 20	NC Peer Group Median
ROAA	1.28	2.10	0.76
ROAE	23.43	44.32	8.32
Net Int. Mrgn.	4.06	3.41	3.33
Efficiency Ratio	74.6	56.8	69.9

Net interest income grew 10% to \$9,977,000 in 2020’s fourth quarter from \$9,041,000 in 2019’s fourth quarter, with higher average earning assets (up 27%) more than offsetting the margin drop, as well as benefitting from the PPP fees. While the increase in net interest income boosted earnings, the real

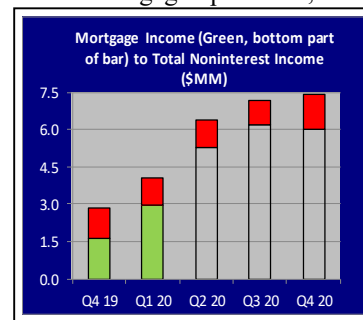
THE MARGIN REMAINED UNDER COMPRESSION

AVERAGE EARNING ASSETS INCREASED 27%

NET INTEREST INCOME WAS UP 10%, DUE TO VOLUME GROWTH OFFSETTING LOWER MARGINS

NONINTEREST INCOME MORE THAN DOUBLED, MOSTLY DUE TO GROWTH IN THE MORTGAGE AREA

driver, as was stated earlier, was the mortgage operation, which was spurred by residential purchase and refinance activities. As can be seen from the adjacent chart, fees from mortgage operations, which accounted for 81% of total noninterest income, increased to \$6,006,000 in 2020's fourth quarter from \$1,657,000 in the year-ago quarter, while total noninterest income totaled \$7,389,000 versus \$2,875,000 over the same period. While we expect some continuation of strong results for the mortgage operation, we do realize that at some point, the level of fees are likely to subside. The important thing to remember is that North State has a highly variable cost structure with its mortgage business, so if refinancing activities decelerate, expenses are likely to drop as well. Finally, noninterest expense was up 11% compared to the year-ago quarter, primarily due to higher salaries and employee benefits, reflecting the high mortgage origination activity.



Net Income for the Year 2020 Increased 31% from 2019

Earnings for the full year 2020 also were strong despite a higher provision, which increased to \$5,040,000 in 2020 from \$680,000 for the year 2019. Net income was \$15,248,000, or \$2.53 per share, for the twelve months ended December 31, 2020, up 31% from \$11,606,000, or \$1.95 per share, in the year-ago period. Net interest income increased 5%, noninterest income more than doubled and noninterest expense grew 17% compared to year 2019 figures. As was stated earlier, balance sheet growth has been excellent. While some of this came from the PPP loan originations, management expects many new long-term relationships from many of these borrowers. From December 31, 2019 to December 31, 2020, net loans increased 24%, deposits grew 27% and total assets were up 26%. Shareholders' equity totaled \$59.3 million, or 5.05% of total assets, at December 31, 2020.

FULL YEAR 2020 HIGHLIGHTS:

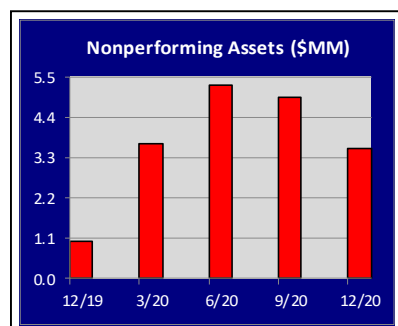
EPS: \$2.53 vs. \$1.95

CORE EARNINGS WERE QUITE STRONG

BALANCE SHEET GROWTH WAS IN THE 24% TO 27% RANGE OVER THE PAST YEAR

Nonperforming Assets Were Down 28% from September 30, 2020

As can be seen from the adjacent chart, North State's nonperforming assets have decreased for the two past consecutive quarters. Nonperforming assets ("NPAs", excluding restructured loans) totaled \$3.6 million, or 0.31% of total assets, at December 31, 2020, which was down from \$4.9 million, or 0.40% of total assets, at September 30, 2020, but was up from \$1.0 million, or 0.11% of total assets, at the year-ago date. All of the NPAs were nonaccrual loans. We would also note that of the loans that were granted deferments during the pandemic, the vast majority have since returned to normal payment terms. Finally, the allowance for loan losses was \$6.5 million, or 0.68% of total loans, at December 31, 2020, up from \$4.9 million, or 0.64% of total loans, at the year-ago date. The allowance as a percentage of non-PPP loans (PPP loans are guaranteed) was 0.76% as of December 31, 2020.



NPAS DECLINED FOR THE PAST TWO QUARTERS IN A ROW, AFTER TRENDING UP AT THE BEGINNING OF 2020

NPAS/ASSETS: 0.31% vs. 0.34% FOR THE NC PEER GROUP MEDIAN

RESERVES/LOANS: 0.68%

2021 Projections Introduced

We expect the provision to remain elevated for the next several quarters given the continued economic uncertainty, though fees from PPP loans are likely to offset this increase. While projections remain difficult to gauge, we are estimating 2021 earnings of \$14.0 million, or \$2.30 per share. As stated previously, actual earnings could vary substantially from these projections given the uncertainties of the COVID-19 crisis.

EPS:
2019A: \$1.95
2020A: \$2.53
2021E: \$2.30

ADDITIONAL INFORMATION UPON REQUEST

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