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## Chesapeake Financial Shares, Inc. (CPKF – OTCQB)

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May 7, 2019

<b>Price:</b>	\$ 26.80	<b>Diluted EPS 2017A:</b> *	\$2.25	<b>P/E 2017A:</b>	11.9 x
<b>52 Wk. Range:</b>	\$22.85 - \$32.25	(FY: DEC) <b>2018A:</b>	\$2.61	<b>2018A:</b>	10.3 x
<b>Div/Div Yld:</b>	\$0.58 /2.2%	<b>2019E:</b>	\$2.70	<b>2019E:</b>	9.9 x
<b>Shrs/Mkt Cap:</b>	4.1 mm/ \$110 mm	<b>Book Value:</b>	\$23.80	<b>Price/Book Value:</b>	1.13 x

• EPS excludes deferred tax charge of \$0.08 per share.

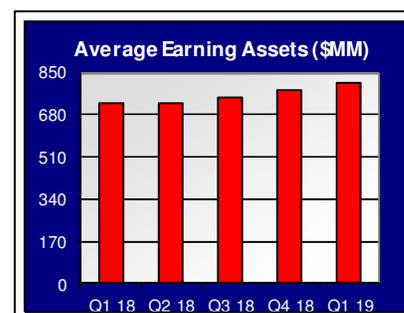
### Background

Chesapeake Financial Shares, Inc. is a one-bank holding company originally chartered in 1900 and is based in Kilmarnock, VA. As of March 31, 2019, the Company had \$893 million in total assets. The holding company operates two subsidiaries, Chesapeake Bank and Chesapeake Wealth Management, Inc. Chesapeake Bank is primarily a lender to small businesses. Personal and business products and services offered include checking, savings, CDs, mortgages, mobile and online banking, e-services comprising an internet branch, and a business cash management program. The Bank currently operates 15 branches; four in the Northern Neck, three in the Middle Peninsula, five in Williamsburg and three in Richmond. There is also a loan production office in Richmond. The Bank also offers merchant processing services for credit and debit card transactions. Chesapeake Wealth Management is an independent wealth management firm which offers investment, wealth management and trust services. Chesapeake Financial Shares, Inc.'s stock trades on the over-the-counter market (OTCQB) under the symbol "CPKF." The Company's Chairman, President, and CEO, Jeffrey M. Szyperki, is a former Chairman of the Virginia Bankers Association. He was also appointed in 2014 to the ABA Board of Directors for a three-year term and was subsequently elected to be Chairman. Finally, for the 11<sup>th</sup> consecutive year, Chesapeake Financial Shares was included in *America Banker* magazine's "Top 200 Community Banks" in the U.S. In the most recent issue, it was ranked 97<sup>th</sup>, up from 123<sup>rd</sup> last year.

### Earnings on the First Quarter of 2019 Exceeded Projections

Chesapeake Financial Shares reported better than anticipated earnings in the first quarter of 2019, thanks in part to better than expected expense containment. It was actually a fairly stable quarter, with commendable but modest increases in most areas of the income statement. Nevertheless, the bottom line EPS figures were about \$0.08 above our estimates, so we were pleased with the results and, based on those results, have revised upwards our earnings estimates for the full year. Profitability ratios were also high and balance sheet growth was commendable, with loans and deposits growing in the double-digits. Asset quality also held up well. Finally, we would note that the Board of Directors increased the Company's cash quarterly dividend, maintaining a record of 28 consecutive years of increases.

In terms of specific results, net income was \$2,975,000, or \$0.72 per diluted share, in the first quarter of 2019, versus \$2,917,000, or \$0.70 per diluted share, in the year-ago quarter. Net interest income was up 1% to \$6,769,000 in 2019's first quarter from \$6,679,000 in the year-ago quarter. Margins have been under some pressure over the past year, although growth in average earning assets (which was 11% over the past year) has more than offset the effects of the margin compression. Noninterest income, excluding security gains, was essentially flat at \$4,416,000 in the first quarter of 2019 compared to \$4,408,000 in the year-ago quarter, though fiduciary and wealth management, Merchant Card, ATM and Cash management income had increases in the



**SYMBOL: CPKF**

**ASSETS: \$893 MM**

**HQ: KILMARNOCK, VA**

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**1<sup>ST</sup> QUARTER HIGHLIGHTS:**

**EPS: \$0.72 vs. \$0.70**

**EPS WAS \$0.08 AHEAD OF PROJECTIONS**

**NET INTEREST INCOME WAS UP 1%**

**NONINTEREST INCOME EXCLUDING SECURITY GAINS GREW 1%**

**ROAA: 1.36% vs. 0.83% FOR THE VA PEER GROUP MEDIAN**

**ROAE: 12.49% vs. 9.67% FOR THE VA PEER GROUP MEDIAN**

**FROM 3/31/18 TO 3/31/19:**

**NET LOANS GREW 8%  
DEPOSITS INCREASED 14%  
TOTAL ASSETS WERE UP 12%**

**THE CAPITAL POSITION REMAINS STRONG**

**DIVIDENDS HAVE INCREASED AT OVER A 9% ANNUAL RATE OVER THE PAST 20 YEARS**

**IN THE PAST FIVE YEARS, DIVIDENDS HAVE ACCOUNTED FOR 20% OF THE 99% TOTAL RETURN ON THE STOCK**

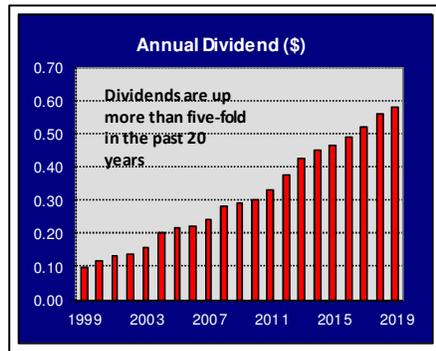
4% to 9% range. As was stated earlier, cost containment was also an encouraging aspect of the quarter, as noninterest expense increased less than 1% to \$7,667,000 in 2019's first quarter, versus \$7,598,000 in the year-ago quarter. Finally, the provision for loan losses was \$175,000 in the first quarter of 2019, unchanged from the first quarter of 2018. The Company's profitability ratios remained excellent and were superior to the majority of the Company's peers. Chesapeake Financial had an annualized ROAA of 1.36% versus 0.83% for its peer median and an annualized ROAE of 12.49% compared to 9.67% for the peer median.

### Balance Sheet Growth Was Led by Deposits

Chesapeake continues to experience excellent balance sheet growth. From March 31, 2018 to March 31, 2019, net loans were up 8%, deposits increased 14% and total assets grew 12%. Linked quarter growth (annualized) was likewise strong, with loans growing 9%, deposits up 17% and total assets increasing 18%. Chesapeake remains well capitalized, with shareholders' equity of \$98 million, or 10.95% of total assets, at March 31, 2019, which was up from \$87 million, or 10.91% of total assets, at the year-ago date. The Company's high ROAE (and its reasonable dividend payout ratio, which we view as a positive, as is discussed more fully below) has allowed its capital to expand at a relatively rapid rate.

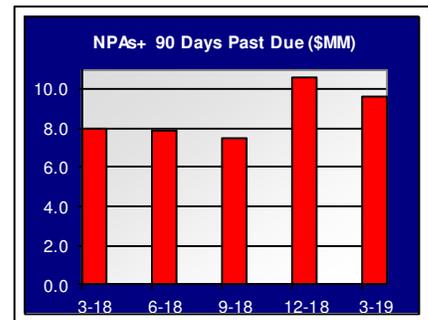
### Chesapeake's Cash Dividend Increased For 28<sup>th</sup> Year

As was stated previously, the Board of Directors recently increased the Company's quarterly cash dividend to \$0.145 per share, up from \$0.14 per share, which marks the 28th consecutive year the Company has increased its cash dividend. On an annualized level, the dividend increases have been quite impressive, with dividends increases more than five-fold over the past 20 years, or a annual growth rate of more than 9%. As we have stated in previous reports, a large amount of the long-term return from owning CPKF shares has come from cash dividends. For example, over the past five years the total return of CPKF shares has been 99%, of which 79% came from appreciation and 20% came from dividends (the median five-year total return for the VA peer group was 75%). Given the Company's strong capital position and reasonable payout ratio (i.e., the percentage of earnings used for dividends is about 20%, which is clearly sustainable), it is in excellent shape to maintain its growth in cash dividends over time, or even to pursue stock buybacks.



### NPAs Were Up From the Year-Ago Period But Decreased from Year-End 2018

Although nonperforming assets increased compared to the year-ago date, they declined compared to December 31, 2018. NPAs were \$9.6 million, or 1.08% of total assets, at March 31, 2019, versus \$10.6 million, or 1.24% of assets, at December 31, 2018, and \$7.9 million, or 0.99% of total assets, at March 31, 2018. Net charge-offs remained quite low in 2019's first quarter, and were about 0.03% of average loans. The allowance for loan losses was \$5.2 million, or 1.00% of gross loans, at March 31, 2019, up 11% from \$4.7 million, or 0.98% of loans, at the year-ago date.



**NPAS DECREASED 9% FROM 12/31/18**

**NPAS/ASSETS: 1.08%**

**RESERVES/LOANS: 1.00%**

**EPS:  
2017A: \$2.25 (EXCLUDING TAX RELATED CHARGE)  
2018A: \$2.61  
2019E: \$2.70**

### Projections Increased

We are increasing our 2019 earnings projections to \$11.1 million, or \$2.70 per diluted share, up from \$2.60 per share estimated previously. Note that these projections could vary widely based on the economy and credit conditions.

ADDITIONAL INFORMATION UPON REQUEST

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