First Farmers Financial Corporation (FFMR)

Updated April 15th, 2022 by Josh Arnold

Key Metrics

Current Price:	$54	**5 Year CAGR Estimate:**	6.0%	**Market Cap:**	$378 M
Fair Value Price:	$49	**5 Year Growth Estimate:**	5.0%	**Ex-Dividend Date:**	06/30/22[1]
% Fair Value:	110%	**5 Year Valuation Multiple Estimate:**	-1.9%	**Dividend Payment Date:**	07/15/22[1]
Dividend Yield:	3.0%	**5 Year Price Target**	$63	**Years Of Dividend Growth:**	31
Dividend Risk Score:	A	**Retirement Suitability Score:**	A	**Rating:**	Hold

Overview & Current Events

First Farmers Financial is a holding company for First Farmers Bank & Trust, which provides banking products and services to individuals, families, and commercial customers. It offers core checking and savings accounts, health savings accounts, business accounts, construction loans, auto loans, collateral loans, mortgages, and other services. The bank has 29 offices in Indiana and 6 offices in Illinois, so it is a very small community bank. First Farmers was founded in 1885, generates about $90 million in annual revenue, and trades with a market capitalization of $378 million. First Farmers also has a dividend streak of 31 years, meaning it qualifies to be a Dividend Champion.

First Farmers reported its 2021 results in late March 2022, capping what was a record year. The bank showed strong loan growth in 2021 once again, this time adding $157 million in net new loans to $1.7 billion at the end of the year. Total deposits grew at about double that rate, adding $350 million to end 2021 at $2.1 billion. First Farmers' loan-to-deposit ratio is still quite elevated by peer standards at 81%. However, it isn't elevated to the point where we believe it will pose a significant balance sheet risk, or crimp growth, so long as it continues to attract deposits.

Total revenue for the year rose from $83 million to $87 million, reflecting primarily the growth in loans. Paycheck Protection Program loans were a feature of 2020, but First Farmers almost completely wound that down in 2021. Revenue grew much more quickly than core operating expenses, which helped drive earnings-per-share to a new record of $5.11. We think that will be difficult to replicate in 2022, so our estimate for earnings-per-share for the current year is $4.90. That would still be the second best year in the company's history, but we think the perfect conditions of 2021 will be hard to replicate.

Growth on a Per-Share Basis

Year	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022	2027
EPS	$1.89	$2.22	$2.27	$2.35	$2.38	$3.03	$3.87	$4.13	$4.29	$5.11	***$4.90***	***$6.25***
DPS	$0.35	$0.40	$0.53	$0.59	$0.65	$0.69	$1.02	$1.22	$1.29	$1.39	***$1.60***	***$2.24***
Shares	7.1	7.1	7.1	7.1	7.2	7.2	7.2	7.1	7.1	7.1	***7.1***	***7.1***

First Farmers has grown its earnings-per-share at a rate of 10% annually since 2012, which is very impressive to say the least. However, we do not expect that sort of performance to continue given the bank's current balance sheet and profitability metrics. Note that First Farmers executed a 2-for-1 stock split in 2018, which the above numbers reflect.

We estimate 5% annual earnings-per-share growth for the next five years, as we see First Farmers continuing to maintain its elevated loan-to-deposit ratio, but with little room for growth there. At ~80%, First Farmers' loan-to-deposit ratio moved down since the end of 2020, improving balance sheet safety, as well as the runway for future lending growth. Even so, we think growth off of the very high base of earnings at present is going to be tough.

In addition to that, First Farmers has made a significant amount of loans while interest rates have been at or near historical lows. Rates have risen sharply in recent months, and if that move sticks, First Farmers may be caught in a

[1] Estimated date

situation where its deposit costs are rising while its loan yields are fixed. We note this hasn't happened yet, but it is a distinct possibility considering how First Farmers' balance sheet is constructed.

First Farmers does buy back stock, but it's quite minimal, so we don't see that as a significant factor in terms of powering earnings-per-share growth.

Valuation Analysis

Year	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021	Now	2027
Avg. P/E	---	---	14.3	14.9	17.5	15.5	10.9	11.3	10.2	8.8	***11.0***	***10.0***
Avg. Yld.	---	---	1.6%	1.7%	1.6%	1.5%	2.4%	2.6%	3.0%	3.1%	***3.0%***	***3.6%***

First Farmers has traded with an elevated P/E ratio in past years, generally trading around the mid-teens or higher. However, we see First Farmers as facing a number of growth challenges, as detailed above, and given that sector valuations are still quite low, we assess fair value at 10 times earnings. The stock trades for 11 times earnings today, so it is modestly ahead our estimate of fair value, implying a small headwind to total annual returns from the valuation.

We note that the valuation and consistent dividend raises have sent the current dividend yield to an impressive 3%, much higher than in past years. We expect the dividend to grow more quickly than earnings and the share price, and therefore see some upside to the yield in the years to come.

Safety, Quality, Competitive Advantage, & Recession Resiliency

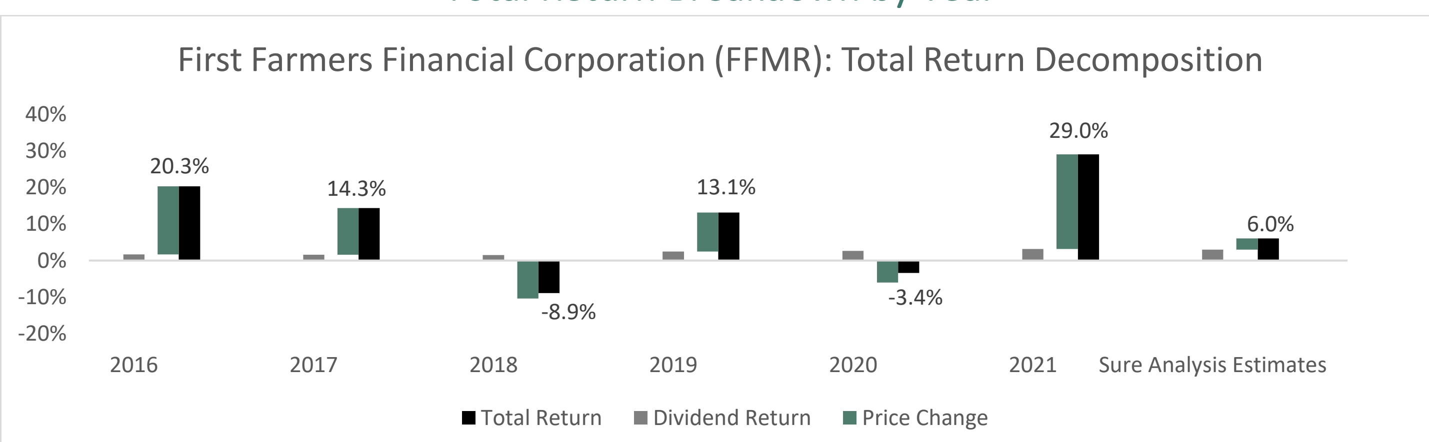
Year	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022	2027
Payout	19%	18%	23%	25%	27%	23%	26%	30%	30%	27%	***33%***	***36%***

First Farmers, like any other community bank, struggles for competitive advantages given that banking is a highly commoditized business with similar offerings from most players. That said, its performance during periods of low interest rates has been impressive, having grown its earnings consistently through periods of extremely low rates. We're keeping an eye on the bank's long-term debt, which is in excess of $200 million, but we expect First Farmers to hold up relatively well during the next recession. The bank's payout ratio is also quite manageable at just one-third of earnings, so we see the dividend as safe.

Final Thoughts & Recommendation

We see First Farmers as a slightly overvalued income stock among community banks. We forecast 6.0% total annual shareholder returns in the next five years, and with a 3%+ yield, the security earns a hold rating.

Total Return Breakdown by Year



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Disclosure: This analyst has no position in the security discussed in this research report, and no plans to initiate one in the next 72 hours.

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Income Statement Metrics

Year	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021
Revenue	---	---	56	63	68	74	81	85	103	96
SG&A Exp.	---	---	20	24	26	28	29	31	35	34
D&A Exp.	---	---	3	4	4	3	3	4	4	5
Net Profit	---	---	16	17	17	22	28	30	36	30
Net Margin	---	---	28.8%	26.5%	25.1%	29.4%	34.3%	34.7%	34.9%	31.9%
Free Cash Flow	---	---	18	16	22	27	36	30	65	25
Income Tax	---	---	6	6	6	5	5	5	7	6

Balance Sheet Metrics

Year	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021
Total Assets	---	---	1,340	1,480	1,616	1,677	1,749	1,916	2,439	2,214
Cash & Equivalents	---	---	80	53	111	88	52	60	221	191
Accounts Receivable	---	---	16	20	20	24	24	26	31	29
Goodwill & Int. Ass.	---	---	12	13	12	11	10	10	9	9
Total Liabilities	---	---	1,228	1,356	1,480	1,523	1,577	1,718	2,196	1,992
Accounts Payable	---	---	12	11	19	15	12	21	21	30
Long-Term Debt	---	---	114	120	140	173	158	173	81	209
Shareholder's Equity	---	---	112	125	136	154	172	198	243	222
D/E Ratio	---	---	1.02	0.96	1.03	1.13	0.92	0.87	0.33	0.94

Profitability & Per Share Metrics

Year	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021
Return on Assets	---	---	---	1.2%	1.1%	1.3%	1.6%	1.6%	1.6%	1.5%
Return on Equity	---	---	---	14.2%	13.1%	15.0%	17.0%	16.0%	15.5%	14.5%
ROIC	---	---	---	7.1%	6.5%	7.2%	8.4%	8.4%	9.6%	7.6%
Shares Out.	7.1	7.1	7.1	7.2	7.2	7.2	7.1	7.1	7.1	7.1
Revenue/Share	---	---	7.89	8.86	9.47	10.30	11.29	11.90	14.65	13.47
FCF/Share	---	---	2.48	2.28	3.10	3.75	5.02	4.22	9.28	3.54

Note: All figures in millions of U.S. Dollars unless per share or indicated otherwise.