First National Corporation (FXNC)

Updated November 11th, 2024 by Nikolaos Sismanis

Key Metrics

Current Price:	$22.45	**5 Year CAGR Estimate:**	2.7%	**Market Cap:**	$201.2 M
Fair Value Price:	$16.50	**5 Year Growth Estimate:**	6.0%	**Ex-Dividend Date:**	11/22/2024[1]
% Fair Value:	136%	**5 Year Valuation Multiple Estimate:**	-6.0%	**Dividend Payment Date:**	12/09/2024
Dividend Yield:	2.7%	**5 Year Price Target**	$22.08	**Years Of Dividend Growth:**	9
Dividend Risk Score:	D	**Retirement Suitability Score:**	D	**Rating:**	Sell

Overview & Current Events

First National Corporation is a bank holding company that primarily operates through its wholly-owned subsidiary, First Bank. The bank provides a broad range of financial products and services, including traditional banking offerings like checking and savings accounts, commercial and consumer loans, residential mortgages, home equity lines, and wealth management services. In addition to its core banking activities, the company also offers estate planning, investment management, and trustee services. First Bank operates 20 branch offices, mainly in Virginia's Shenandoah Valley, Roanoke Valley, and Richmond regions, delivering its services through physical branches, a mobile banking platform, and a network of ATMs. The company's market cap stands at about $201 million.

On October 1st, 2024, First National Corporation completed the acquisition of Touchstone Bankshares.

On November 1st, 2024, the company posted its Q3 results for the period ending September 30th, 2024. The bank posted net income of $2.2 million, or $0.36 per share, compared to $3.1 million, or $0.50 per share, last year. Adjusted net income, which excludes $219K in merger-related expenses, was $2.4 million, or $0.39 per share. The bank's net interest margin (NIM) improved to 3.43%, up from 3.40% sequentially due to stronger loan yields and deposit management.

Noninterest income totaled $3.2 million, up from $2.7 million in Q3 2023, mainly due to increases in all other divisions such as in wealth management and brokerage services. Noninterest expenses fell 2% sequentially to $10.5 million, due to lower legal and merger-related costs. We believe First National is set to achieve EPS of about $1.65 this year.

Growth on a Per-Share Basis

Year	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023	2024	2029
EPS	$1.32	$0.31	$1.20	$1.30	$2.05	$1.92	$1.82	$1.87	$2.69	$1.54	***$1.65***	***$2.21***
DPS	$0.08	$0.10	$0.12	$0.14	$0.20	$0.36	$0.44	$0.48	$0.56	$0.60	***$0.60***	***$0.80***
Shares[2]	4.9	4.9	4.9	4.9	5.0	5.0	4.9	5.6	6.3	6.3	***6.3***	***6.3***

Over the past decade, First National's EPS has seen fluctuations, reflecting both strong performance and challenges. In 2014, EPS stood at $1.32, but it dropped significantly to $0.31 in 2015. This decline was primarily due to a combination of factors, including a $6.8 million surge in noninterest expenses, largely due to acquisition-related costs and expansion efforts. Additionally, the bank reported a substantially lower recovery of loan losses in 2015 compared to the previous year, contributing to the earnings drop.

In 2016, EPS rebounded to $1.20, due to improved cost management and steady loan growth. This recovery continued in 2017, with EPS rising to $1.30, driven by stronger loan demand and better financial performance. In 2018, EPS surged to $2.05, due to higher net interest income and the impact of federal tax reforms, which boosted profitability. Regardless, EPS dipped slightly to $1.92 in 2019, as noninterest expenses rose due to the bank's investment in expanding its market footprint. Despite these higher costs, First National demonstrated resilience during the COVID-19 pandemic in 2020, with EPS only dipping to $1.82, as it managed to maintain a stable loan portfolio.

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[1] Estimated dated based on past dividend dates.

[2] Share count is in millions.

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By 2021, EPS recovered to $1.87, with the bank benefiting from strong loan demand and the successful acquisition of The Bank of Fincastle, which expanded its presence in the Roanoke market. In 2022, EPS peaked at $2.69, driven by robust loan growth and favorable interest rates. However, in 2023, EPS declined to $1.54, primarily due to substantial charge-offs related to weaknesses in a purchased loan portfolio and increased provisions for credit losses. The bank's NIM slightly fell to 3.41% from 3.44% in 2022 as rising deposit costs put pressure on earnings.

Moving forward, we believe First National will be able to deliver more consistent EPS growth, with our medium-term estimate standing at 6%. We have applied the same rate to our dividend growth forecast, with First National having increased its dividend for nine consecutive years thus far.

Valuation Analysis

Year	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023	Now	2029
Avg. P/E	4.7	---	7.7	9.2	8.2	10.2	9.6	9.6	7.4	11.2	***13.6***	***10.0***
Avg. Yld.	1.3%	1.3%	1.3%	1.2%	1.2%	1.8%	2.5%	2.7%	2.8%	3.5%	***2.7%***	***3.6%***

In recent years, First National has consistently traded at a P/E ratio in the high-single digits to low teens, aligning with the typical range for regional banks. Currently, the stock is trading at just 13.6 times our projected EPS for the year—a multiple we believe overvalues the stock. We see the stock's yield of 2.7% advancing higher following a P/E contraction.

Safety, Quality, Competitive Advantage, & Recession Resiliency

Year	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023	2024	2029
Payout	6%	32%	10%	11%	10%	19%	24%	26%	21%	39%	***36%***	***36%***

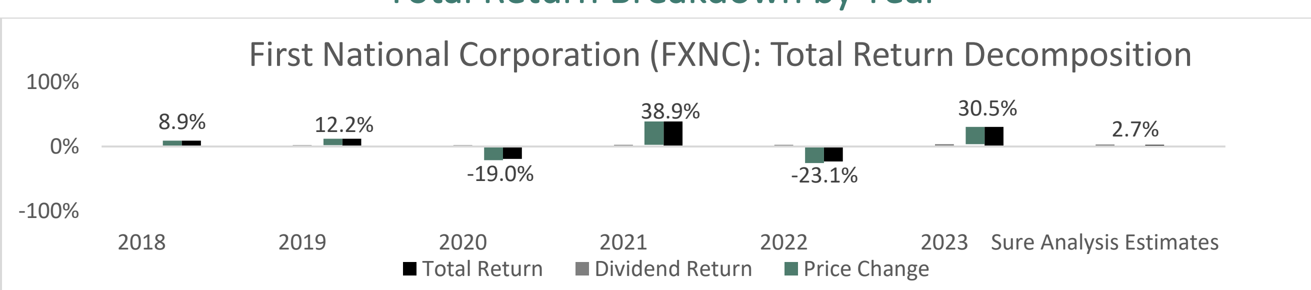
First National holds a number of competitive advantages, particularly when it comes to its long-standing community ties and commitment to customer service within its primary market areas, including the Shenandoah Valley, Roanoke Valley, and Central Virginia. Its solid local presence and customer relationships give it a competitive edge against larger national and regional banks, credit unions, and other financial institutions in the region. During challenging periods, such as the COVID-19 pandemic, First National remained resilient, maintaining profitability through prudent financial management and effective cost control. The bank's capital health remains robust, as reflected in its Common Equity Tier 1 capital ratio of 13.04% and Total Capital ratio of 14.29% at the end of the third quarter of 2024, both above minimum requirements.

Nevertheless, its smaller scale compared to larger institutions limits its ability to fully leverage economies of scale, which could make it more vulnerable during prolonged periods of economic stress. Also, the bank suffered in the aftermath of the Great Financial Crisis, with the bank facing a substantial increase in non-performing assets, and writing down a $6.4 million deferred tax asset. In any case, we believe the stock's dividend can be considered rather secure today.

Final Thoughts & Recommendation

First National's strong community ties make it a compelling choice for investors looking for exposure to a Virginia-based well-managed regional bank with a solid track record of EPS and DPS growth. Yet, we see annualized returns of just 2.7% through 2029, as valuation headwinds could offset returns from growth and the dividend. Thus, we rate the stock a sell.

Total Return Breakdown by Year



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Year	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023
Revenue	25	28	31	33	36	36	37	44	57	54
SG&A Exp.	12	16	15	14	14	14	14	19	22	23
D&A Exp.	1	2	2	2	2	2	1	1	2	2
Net Profit	8	3	6	6	10	10	9	10	17	10
Net Margin	30.0%	9.5%	19.1%	19.7%	28.2%	26.8%	24.1%	23.6%	29.5%	18.0%
Free Cash Flow	7	3	8	5	12	11	14	7	26	15
Income Tax	3	1	2	4	2	2	2	3	4	2

Balance Sheet Metrics

Year	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023
Total Assets	518	692	716	739	753	800	951	1,389	1,369	1,419
Cash & Equivalents	25	39	41	40	29	46	127	176	67	87
Accounts Receivable	1	2	2	2	2	2	3	4	5	5
Goodwill & Int. Ass.	0	2	2	1	0	0	0	3	3	3
Total Liabilities	459	646	664	681	686	723	866	1,272	1,261	1,303
Long-Term Debt	9	14	14	14	14	14	19	19	14	64
Shareholder's Equity	45	46	52	58	67	77	85	117	108	116
LTD/E Ratio	0.16	0.31	0.27	0.24	0.21	0.18	0.23	0.16	0.13	0.55

Profitability & Per Share Metrics

Year	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023
Return on Assets	1.5%	0.4%	0.8%	0.9%	1.4%	1.2%	1.0%	0.9%	1.2%	0.7%
Return on Equity	13.5%	5.0%	12.0%	11.7%	16.2%	13.3%	10.9%	10.3%	14.9%	8.6%
ROIC	11.1%	4.1%	9.3%	9.3%	13.2%	11.1%	9.1%	8.6%	13.0%	6.3%
Shares Out.	4.9	4.9	4.9	4.9	5.0	5.0	4.9	5.6	6.3	6.3
Revenue/Share	5.18	5.71	6.26	6.62	7.26	7.18	7.52	7.89	9.08	8.53
FCF/Share	1.33	0.53	1.62	1.11	2.46	2.18	2.91	1.27	4.09	2.31

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