Alpine Banks of Colorado

RATINGS

Alpine Banks of Colorado	
Action: Affirmed	5/27/2022
Outlook/Watch LTR	**Stable**
Senior Unsecured Debt	**BBB**
Subordinated Debt	**BBB-**
Short-Term Debt	**K3**

Alpine Bank	
Action: Affirmed	5/27/2022
Outlook/Watch LTR	**Stable**
Deposit	**BBB+**
Senior Unsecured Debt	**BBB+**
Subordinated Debt	**BBB**
Short-Term Deposit	**K2**
Short-Term Debt	**K2**

FINANCIAL SNAPSHOT

ALPIB (%)	1Q22	YE21
Total Assets ($B)	6.2	6.2
ROAA	0.80	1.03
NIM	2.93	3.09
NCO Ratio	0.06	(0.00)
NPA Ratio	0.20	0.13
TCE Ratio	6.2	6.5
CET1 Ratio	10.4	10.4
Loans/Core Dep	61	61

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Company Profile

- Alpine Banks of Colorado ("Alpine" or "the company") is the bank holding company for Alpine Bank (founded in 1973), whose private Class A voting stock remains majority-owned by a combination of the bank's two founders (one of whom remains Chairman), along with other directors and employees, including a 23% Class A stake owned by the company's ESOP that was created in 1983. Alpine's non-voting Class B shares are thinly traded (OTC: ALPIB).
- With the leading and organically based deposit share position in Western Slope (CO) markets through 26 branches, Alpine expanded east to the Front Range (Denver & Boulder MSAs) beginning in 2014 and currently has nearly $500 million of deposits in 5 area branches. The company is also opening branches in both Fort Collins and Colorado Springs in 4Q22.
- A real estate-oriented lender at its core, Alpine balances a not insignificant C&D exposure (13% of loans; 79% of TRBC at 1Q22) and a $740 million investor CRE portfolio (208% of TRBC), with a meaningful prime residential mortgage book that totaled $1.4 billion, or 42% of loans, at 1Q22. Having begun developing commercial lending capabilities in 2017, as a result of more perceived opportunities in the particularly vibrant greater-Denver market, the now modest traditional C&I book ($632 million including owner occupied CRE) is currently expected to grow to represent a greater proportion of the loan portfolio.

Key Credit Considerations

- Alpine's ratings are supported by an extremely low-cost and plentiful core deposit base that has highlighted its balance sheet profile for many years. The company has reflected among the lowest deposit costs in the industry throughout multiple interest rate cycles, including peak interest-bearing deposit costs of 15 bps in 2019. Moreover, while many banks liquidity positions have benefitted from government stimulus and the Fed's actions throughout the pandemic, we believe Alpine will continue to reflect a favorable liquidity position in less conducive operating environments. The high touch, relationship-based banking model has been instrumental in growing and maintaining the leading deposit market share in the Western Slope, while organic growth has been supplemented in recent years by successful de novo expansion into the Front Range markets.
- The company's low-cost deposit base has helped support a healthy NIM historically, which tracked well above 4.0% prior to the pandemic. However, given lingering excess liquidity, with 39% of assets in cash & securities, Alpine's NIM is currently below average. This, combined with decreasing fee income, primarily due to the normalization in mortgage banking, has resulted in lower returns compared to historical levels.
- Credit quality has remained pristine, with Alpine's NPA ratio being amongst the lowest in its peer group, while NCOs have remained negligible averaging just 3 bps since YE16. The sound credit performance has been supported by minimal exposure to COVID vulnerable lending segments, and management's disciplined loan underwriting, which in our view emanates from a significant level of insider ownership and lessons learned from the global financial crisis.
- KBRA also recognizes the modestly below average capital ratios, as well as Alpine's concentrated operating footprint compared to higher rated peers.

Rating Sensitivities

+ Improved core capital, further revenue diversification, and continued stability with credit quality metrics could facilitate a positive, intermediate-term ratings trend.

– Any unexpected deterioration in asset quality, leading to operating losses or lower core capital, or a more aggressive stance with liquidity management could pressure the ratings.

KBRA Bank & Bank Holding Company Global Rating Methodology November 8, 2021. KBRA ESG Global Rating Methodology June 16, 2021.

Financial Metrics

Figure 1: Summary Financial Highlights

ALPINE BANKS OF COLORADO										
	1Q22	4Q21	3Q21	2Q21	1Q21	2021	2020	2019	2018	2017
Balance Sheet ($ millions)										
Loans (HFI)	3,404	3,387	3,288	3,363	3,334	3,387	3,220	2,667	2,430	2,264
Average Earning Assets	6,087	5,961	5,737	5,450	5,132	5,570	4,287	3,536	3,398	3,112
Total Assets	6,184	6,219	6,111	5,792	5,643	6,219	5,178	3,868	3,710	3,483
Core Deposits	5,572	5,581	5,460	5,152	5,005	5,581	4,539	3,325	3,232	2,942
Total Deposits	5,599	5,608	5,491	5,184	5,043	5,608	4,581	3,360	3,271	3,071
Total Equity	398	418	412	400	386	418	376	342	297	258
Tangible Common (TCE)	380	400	394	382	368	400	359	325	279	241
Income Statement ($ millions)										
Net Interest Income	43.1	43.6	43.3	41.7	43.5	172.1	159.6	157.4	144.7	126.1
Noninterest Income	11.0	12.5	12.1	11.5	12.5	48.6	46.7	40.2	34.8	31.0
Noninterest Expense	35.8	38.8	35.2	32.9	34.2	141.1	132.8	127.9	113.3	102.6
Provision for Loan Losses	-	-	-	1.1	4.1	5.2	12.1	-	-	(1.1)
Net Income	12.7	13.6	16.2	15.7	14.1	59.6	51.1	58.0	54.8	33.6
Performance Measures (%)										
Return on Average Assets	0.80%	0.88%	1.09%	1.11%	1.05%	1.03%	1.13%	1.55%	1.54%	1.03%
Return on Average Equity	12.1%	13.1%	16.0%	16.0%	14.7%	14.9%	14.3%	18.2%	19.9%	13.5%
Risk Weighted ROA	1.25%	1.41%	1.81%	1.79%	1.74%	1.68%	1.65%	2.07%	2.07%	1.37%
Net Interest Margin (TE*)	2.93%	2.93%	3.02%	3.06%	3.39%	3.09%	3.72%	4.45%	4.40%	4.31%
Average Loan Yield	4.31%	4.54%	4.61%	4.47%	4.88%	4.62%	4.78%	5.52%	5.31%	4.98%
Cost of Interest-Bearing Deposits	0.03%	0.04%	0.04%	0.04%	0.06%	0.04%	0.09%	0.15%	0.10%	0.08%
Loans / Earning Assets	56%	56%	58%	62%	64%	60%	71%	70%	69%	69%
Noninterest Income / Op. Revenue	20%	22%	22%	22%	22%	22%	23%	20%	19%	20%
Efficiency Ratio	66%	69%	63%	62%	61%	64%	64%	65%	63%	65%
Asset Quality (%)										
NPA / Loans + OREO	0.20%	0.13%	0.14%	0.20%	0.21%	0.13%	0.23%	0.16%	0.32%	0.57%
LLR / Loans (HFI)	1.23%	1.25%	1.29%	1.25%	1.23%	1.25%	1.15%	0.98%	1.17%	1.27%
LLR / NPL	757%	1339%	1167%	738%	697%	1339%	600%	915%	493%	359%
NCO / Average Loans	0.06%	0.01%	(0.02%)	(0.01%)	0.00%	(0.00%)	0.04%	0.10%	0.01%	(0.02%)
Provision / NCO (x)	-	-	N/A	N/A	125.2	(72.6)	9.6	-	-	2.4
NPA Change Rate	55%	(10%)	(30%)	(4%)	(4%)	(42%)	73%	(46%)	(40%)	(16%)
Capital (%)										
TCE Ratio	6.2%	6.5%	6.5%	6.6%	6.5%	6.5%	6.9%	8.4%	7.6%	6.9%
Leverage Ratio	7.6%	7.7%	7.8%	8.0%	8.2%	7.7%	8.4%	10.3%	9.6%	8.9%
CET 1 Ratio	10.4%	10.4%	10.7%	10.7%	10.8%	10.4%	10.7%	10.9%	10.3%	9.2%
Tier 1 Ratio	12.1%	12.1%	12.5%	12.6%	12.8%	12.1%	12.7%	13.2%	12.7%	11.5%
Total Capital Ratio	14.4%	14.5%	15.0%	15.2%	15.5%	14.5%	15.3%	14.1%	13.8%	12.9%
Leverage & Funding (%)										
Loans / Deposits	61%	61%	60%	65%	67%	61%	71%	80%	74%	74%
Loans / Core Deposits	61%	61%	61%	66%	67%	61%	72%	81%	75%	77%
Core Deposits / Total Funding	97%	97%	97%	97%	97%	97%	97%	97%	97%	94%
Double Leverage (Incl TRuPS)	105%	105%	105%	105%	105%	105%	105%	97%	97%	96%
RWA / Total Assets	65%	63%	60%	62%	60%	63%	65%	77%	73%	75%

Sources: KBRA Research, Company Reports, Y9C

Figure 2:

LOAN COMPOSITION

($ millions)	1Q22	2021	2020	2019	2018
Construction & Development	453	429	395	375	335
Owner Occupied CRE	419	415	358	346	337
Non-Owner Occupied CRE	642	617	555	488	430
Residential Mortgage	1,420	1,443	1,371	1,133	1,023
Commercial & Industrial	214	237	338	126	118
Consumer	36	36	43	37	32
Multi-Family Loans	98	95	86	52	59
Leases	6	6	6	4	4
Agriculture	42	40	67	67	65
Other	91	90	38	58	37
Total Loans	3,410	3,399	3,246	2,682	2,435
Loans Held for Sale (HFS)	6	12	27	15	5
Loans Held for Investment (HFI)	3,404	3,387	3,220	2,667	2,430
Annual Loan Growth	2%	5%	21%	10%	7%
Investor CRE / Total Loans	35%	34%	32%	34%	34%
C&D / Risk-Based Capital	79%	76%	77%	90%	89%
Investor CRE / Risk-Based Capital	208%	202%	202%	219%	219%

Loan Composition

Agriculture 1%
Other 3%
Construction & Development 13%
Owner Occupied CRE 12%
Non-Owner Occupied CRE 19%
Residential Mortgage 42%
Commercial & Industrial 6%
Consumer...
Multi-Family Loans 3%

Sources: Company Reports, KBRA Research

DEPOSIT COMPOSITION

($ millions)	1Q22	2021	2020	2019	2018
Domestic Deposits					
Demand Deposits	2,355	2,238	1,745	335	287
NOW & ATS	1,267	1,245	1,037	87	91
MMDA & Savings	1,867	2,013	1,659	2,800	2,745
Time Deposits					
Retail Time (<$250,000)	83	85	98	103	109
Jumbo Time (>$250,000)	27	26	42	36	39
Foreign Deposits	0	0	0	0	0
Total Deposits	5,599	5,608	4,581	3,360	3,271
Total Core Deposits	5,572	5,581	4,539	3,325	3,232
Total Noninterest Bearing Deposits	2,355	2,238	1,745	1,248	1,166
Annual Core Deposit Growth Rate	11%	23%	37%	3%	10%

Deposit Composition

Retail Time (<$250,000) 2%
Demand Deposits 42%
NOW & ATS 23%
MMDA & Savings 33%

Sources: Company Reports, KBRA Research

Sources: KBRA Research, Company Reports, Y9C

Comparative Statistics

Figure 3:

Peer Comparison Trends

Time Period	ALPINE BANKS OF COLORADO 1Q22	Benchmark $1-$10BN 1Q22	KBRA Peers BBB 1Q22	ALPINE BANKS OF COLORADO 2021	Benchmark $1-$10BN 2021	KBRA Peers BBB 2021	ALPINE BANKS OF COLORADO 2020	Benchmark $1-$10BN 2020	KBRA Peers BBB 2020
Balance Sheet ($ in mlns)									
Total Assets	6,184	4,918	6,870	6,219	4,967	6,730	5,178	4,547	6,325
Total Risk Weighted Assets	3,990	3,602	5,289	3,897	3,585	5,080	3,350	3,285	4,575
Loans (HFI)	3,404	3,091	4,822	3,387	3,118	4,682	3,220	3,056	4,674
Total Deposits	5,599	4,152	5,760	5,608	3,749	5,687	4,581	3,126	5,082
Average Loans / Average Earning Assets	55.6%	59.6%	67.3%	59.8%	69.5%	74.9%	71.0%	75.6%	80.3%
Performance Measures (%)									
Return on Average Assets	0.82%	1.25%	1.15%	1.03%	1.39%	1.23%	1.13%	1.10%	0.76%
Return on Average Equity	12.2%	11.9%	12.0%	14.9%	12.8%	12.8%	14.3%	9.9%	8.0%
Return Weighted ROA	1.31%	1.68%	1.53%	1.67%	1.98%	1.76%	1.63%	1.49%	1.02%
Net Interest Margin (TE*)	2.94%	3.16%	3.25%	3.15%	3.18%	3.20%	3.80%	3.32%	3.33%
Average Loan Yield	4.37%	4.52%	4.28%	4.62%	4.51%	4.28%	4.78%	4.63%	4.47%
Cost of Interest Bearing Deposits	0.04%	0.25%	0.25%	0.04%	0.30%	0.31%	0.09%	0.65%	0.69%
Noninterest Income / Op. Revenue	20.4%	25.0%	20.1%	22.0%	26.3%	21.4%	22.6%	26.2%	22.5%
Efficiency Ratio	66.1%	62.7%	61.4%	63.9%	61.1%	60.3%	64.4%	62.3%	65.8%
Asset Quality (%)									
NPA / Loans + OREO	0.20%	0.56%	0.46%	0.13%	0.60%	0.50%	0.23%	0.80%	0.69%
LLR / Loans(HFI)	1.23%	1.38%	1.10%	1.25%	1.41%	1.15%	1.15%	1.44%	1.32%
LLR / NPL	757%	916%	3816%	1339%	758%	760%	600%	386%	394%
NCO / Average Loans	0.06%	0.13%	0.01%	0.00%	0.13%	0.10%	0.04%	0.20%	0.15%
Capital (%)									
TCE Ratio	6.2%	8.8%	7.9%	6.5%	9.6%	8.5%	6.9%	10.0%	8.5%
Leverage Ratio	7.6%	10.1%	9.3%	7.7%	10.3%	9.2%	8.4%	10.4%	9.0%
CET 1 Ratio	10.4%	13.0%	11.1%	10.4%	13.1%	11.4%	10.7%	13.2%	11.3%
Tier 1 Ratio	12.1%	13.6%	11.9%	12.1%	13.8%	12.2%	12.7%	14.0%	12.1%
Total Capital Ratio	14.4%	15.6%	14.5%	14.5%	15.8%	14.9%	15.3%	16.0%	15.1%
Leverage & Funding (%)									
Noninterest Bearing / Total Dep.	42.1%	28.9%	30.6%	39.9%	29.0%	30.8%	38.1%	26.4%	27.6%
Loans / Deposits	60.9%	75.8%	84.2%	60.6%	76.7%	82.3%	70.9%	84.3%	91.1%
Loans / Core Deposits	61.2%	81.7%	91.1%	60.9%	81.8%	88.0%	71.5%	92.9%	102.3%
RWA / Total Assets	64.5%	71.8%	75.9%	62.7%	71.0%	74.0%	64.7%	71.0%	72.8%
Double Leverage (Incl TruPS)	104.9%	101.4%	106.0%	104.8%	101.0%	106.5%	105.0%	100.4%	105.9%
Loan Portfolio (%)									
C&I Loans / Total Loans	6.3%	16.4%	15.8%	7.0%	17.3%	15.7%	10.4%	20.9%	19.4%
Investor CRE / Total Loans	35.0%	33.9%	38.8%	33.6%	35.2%	41.6%	31.9%	32.4%	37.9%
Investor CRE / Risk-Based Capital	208%	206%	260%	202%	213%	267%	202%	211%	260%
C&D Loans / Total Loans	13.3%	7.7%	8.2%	12.6%	7.5%	8.3%	12.2%	6.9%	7.2%
C&D Loans / Risk-Based Capital	78.9%	43.3%	46.6%	75.9%	45.0%	50.5%	77.2%	44.1%	46.8%

Sources: Company Reports, KBRA Research, Y9C

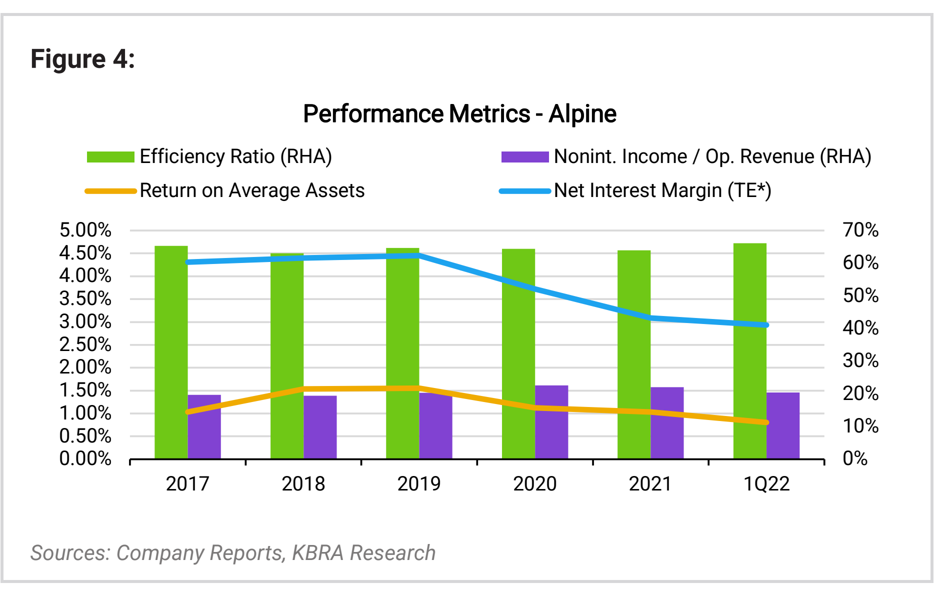
Key Quantitative Rating Determinants

The quantitative financial fundamentals of the bank are derived from the analysis of the bank's intrinsic financial strength and potential adjustments due to KBRA's stress testing as well as an analysis of current and historical financial metrics.

Performance

Alpine's profitability leading into the pandemic was very strong, with ROA exceeding 1.50% for 2018 and 2019, which was primarily due to a healthy NIM that tracked well above 4.00%. The company's NIM was reinforced by an exceptionally low-cost deposit base, with peak interest-bearing deposit costs of just 15 bps in 2019. With that said, earnings have trended much lower in recent years, with ROA tracking in between 1.00%-1.15% for 2020 and 2021, which was, in part, attributable to an increase in provision for loan losses due to the pandemic (ALPIB remains on the incurred loss method, though is adopting CECL in 2023). However, returns were also adversely impacted by significant NIM compression that was driven by the Fed's emergency rate cuts, as well as the significant inflow of deposits stemming from government stimulus and the Fed's quantitative easing. The NIM pressure can be further illustrated by the year-over-year changes, which fell to 3.09% for 2021 compared to 3.72% for 2020. During this time, excess liquidity lingered, with loans relative to earning assets falling to 60% for the year compared to 71% the year prior. Another headwind on profitability over the past year has been the decline in noninterest income, which decreased to 22% of total revenues (0.79% of average assets) for 2021 compared to 23% of total revenues (0.92% of average assets) for 2020, which was largely due to the normalization in mortgage banking activity. Despite the modest decline in fee income levels, we continue to positively view the diversity in revenues, which has averaged 21% of revenues from 2017-2021. Additionally, the fee income contributions are largely comprised of stable and recurring business lines, with gain-on-sale revenues averaging just 18% of noninterest income for the same period. Offsetting the pressure on revenues over the past year has been the more efficient operating model, with noninterest expenses to average assets decreasing to 2.44% for 2021 vs. 2.92% for 2020.

Figure 4:

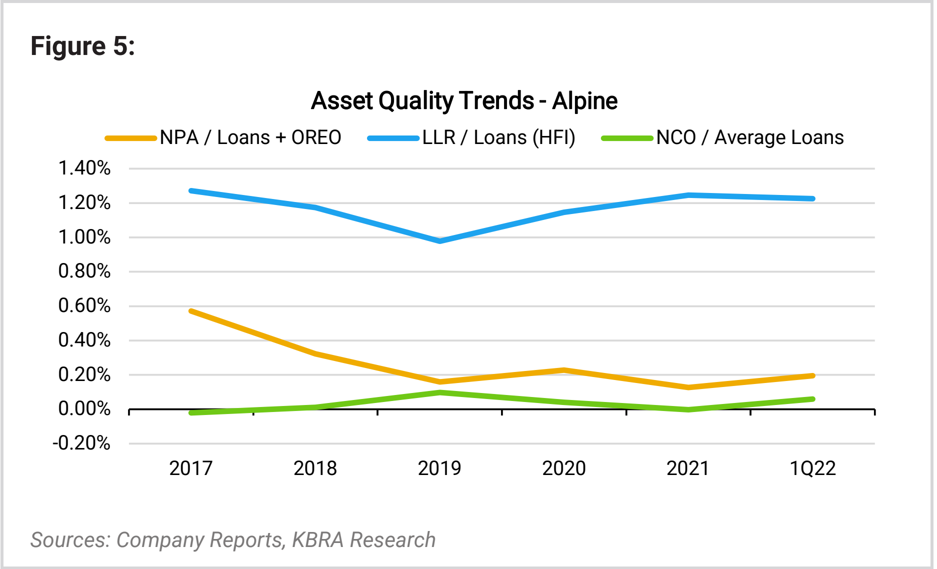


Sources: Company Reports, KBRA Research

While profitability has been below average in recent years, as well as for 1Q22, with ROA falling to 0.80%, which continues to be adversely affected by excess liquidity (56% of earning assets concentrated in loans; 39% of assets in cash and securities), with NIM decreasing to 2.93%, KBRA believes that earnings will improve significantly as liquidity levels normalize, and the company repositions the earning asset mix through loan growth. Additionally, Alpine is asset sensitive, and with the Fed increasing the target rate to 0.75%-1.00% through 2Q22, and the likelihood of further rate hikes, the company is expected to benefit from an NII perspective. Moreover, the company has not recorded any provision for loan losses the last three quarters, and management anticipates no provisions for the remainder of 2022. The lack of credit costs will also help support a turnaround in profitability. Fee income levels (20% of revenues; 0.70% of average assets for 1Q22) have likely troughed and are not expected to change meaningfully over the near term. Additionally, expense levels are already relatively below average (2.26% of average assets) and will continue to be pressured by investments into technology, as well as inflationary issues and worker shortages. Altogether, despite the decline, we believe ALPIB's earnings profile is sound and should return closer to pre-pandemic levels over time. Additionally, when factoring in the lower level of risk-weighted assets, the company's risk-adjusted returns or return on risk-weighted assets ratio is rather strong, averaging 1.77% from 2017-2021.

Asset Quality

Figure 5:



Sources: Company Reports, KBRA Research

Alpine's credit quality metrics, following substantial improvements following the global financial crisis (GFC), have remained pristine despite the challenging operating environment stemming from the COVID-19 pandemic. The NPA ratio has continued to track below 0.25% throughout 2021 and 1Q22 compared to an average of 0.32% for 2017-2020. Meanwhile the NCO ratio has remained negligible, averaging

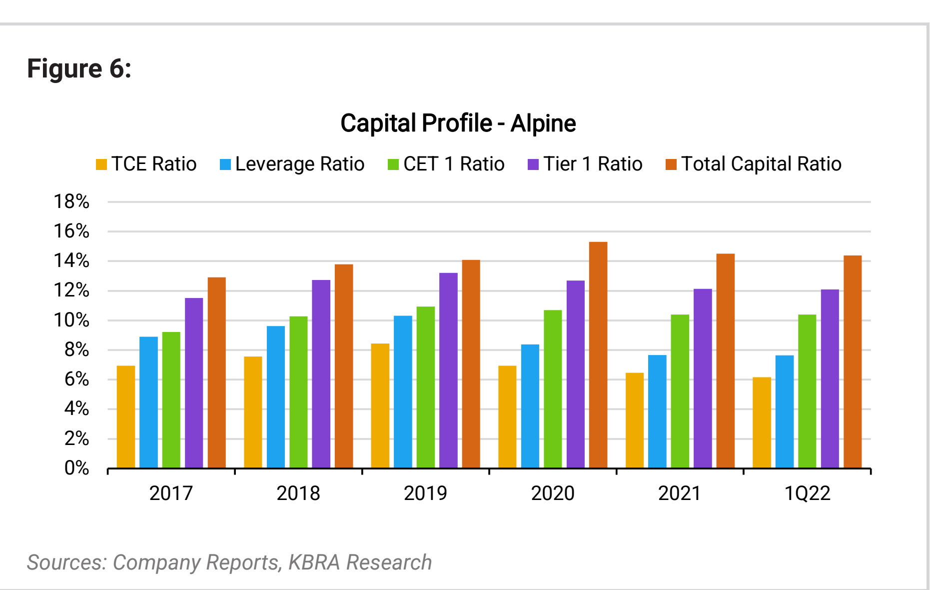
just 1 bp over the past five quarters, which is relatively in line with the favorable performance in prior years, which averaged a modest 3 bps from 2017-2020. KBRA notes that the more prudent approach with regard to C&D lending that currently reflects a greater underwriting discipline and a more conservative approach to credit assessment, including an explainable emphasis on loan segment concentration risk management, as well as the strong economic conditions in the Colorado markets, as supporting factors to the sound credit metrics thus far. Additionally, Alpine's diverse commercial loan book, which includes a minimal exposure to COVID-19 vulnerable lending segments, have also helped facilitate the outperformance. However, the massive amounts of government

stimulus, PPP loans, loan deferrals, and Fed's monetary policies have certainly helped reinforce sound credit quality as well. Moving forward, with the potential of a global slowdown amid rising interest rates and inflation, we believe Alpine is in a relatively solid position, with a below average exposure to investor CRE (208% of total capital) and a manageable C&D concentration (79% of total capital) compared to the GFC. The largest concentration in the loan portfolio continues to be residential mortgage at 42% of loans, which is predominantly first lien mortgages, followed by home equity lines of credit (HELOC), and investor properties. Despite the potential for a bubble in the housing market, which has been supported by a lack of inventory nationwide and extremely low interest rates, we believe Alpine's residential mortgage portfolio is relatively insulated, in part, due to the markets where these homes are owned – the Western Slope, which has weathered economic downturns fairly well historically. Additionally, despite some "chunkiness" in the residential mortgage book, with an average loan size of $577k, and the top 10 loans accounting for $67 million, the underwriting is conservative. The top 10 loans average LTV is 62%. Moreover, the top 10 HELOCs account for $41 million, with an average LTV of 55%. The commercial loan portfolio, with investor CRE comprising 22% of loans (including multifamily) and C&I (18% of loans including owner-occupied CRE), do not represent any meaningful concentration risks, with retail, hotel/motel, industrial/warehouse, and office being the largest exposures. Management remains in constant discussion with borrowers given the potential for a recession and to deal with any lingering effects from the pandemic. Altogether, this portfolio reflects disciplined underwriting criteria as well, with an average LTV of 47% on the investor CRE portfolio, and an average DSCR of 1.96x. Moreover, most of the new loan production has been in the Front Range markets, which has reflected favorable underlying demographics, including very low unemployment rates and strong population growth. That, combined with the lack of inventory, and desirability of the Western Slope markets, we believe the company's operating footprint should be rather resilient throughout any economic downturn. Moreover, if any unforeseen issues were to arise, Alpine continues to reflect a solid reserve position, with the allowance for loan losses at 1.23% of total loans (7.6x total NPAs), as well as an adequate capital position.

Capital

Alpine's core capital ratios continued to trend lower over the past year, which remains adversely impacted by significant balance sheet growth largely related to the continued inflow of deposits. The TCE ratio decreased to 6.2% as of 1Q22 compared to 6.9% at YE20, while the CET1 ratio fell to 10.4% vs. 10.7% for the same period. While the substantial balance sheet

Figure 6:



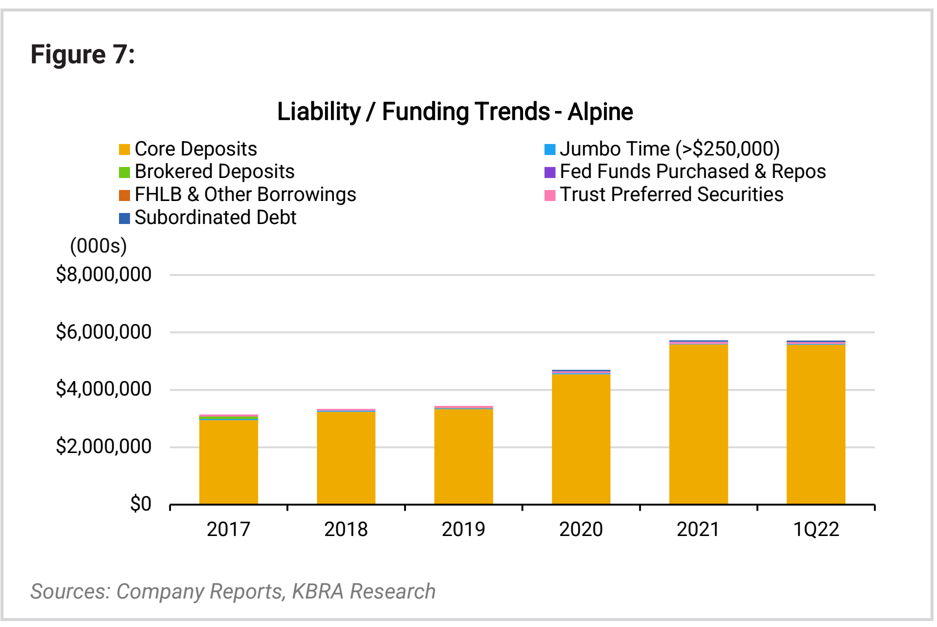
Sources: Company Reports, KBRA Research

growth (19% since YE20) has been the main driver of the reduced capital ratios, there has also been a negative effect from rising interest rates and the impact on the AFS securities portfolio that resulted in an accumulated other comprehensive loss of $30.3 million in 1Q22, though this solely impacted the TCE ratio as ALPIB opted out of counting AOCI adjustments to regulatory capital ratios. Altogether, the company's capital ratios are slightly below average, though still remain adequate for the rating category. Moreover, we believe capital ratios will rise as the balance sheet normalizes and growth rates slow. Management's longer-term capital targets for the TCE and CET1 are in the mid-8% and mid-10% range, respectively, which is viewed as comfortable for the rating group. Internal capital generation, which should improve as well as earnings trend closer to pre-pandemic levels, will be offset by Alpine's rather modest dividend payout (recently increased to $0.18 per Class B shares and $27 per Class A shares), with a payout ratio targeted for 20% of total net income (22% based on 1Q22 net income). Also included in the capital stack is a meaningful amount of legacy trust preferreds (TruPS) at $69 million, which helps support the regulatory capital ratios, with a Tier 1 risk-based ratio of 12.1% as of 1Q22. Additionally, Alpine issued $50 million of subordinated debt in 2Q20 at 5.875% (10NC5), which helped reinforce the total risk-based capital ratio (14.4% as of 1Q22). Despite the issuance, the double leverage remains minimal at just 105%. Moreover, Alpine reflected $27.8 million of holding company cash and equivalents at 1Q22, which covers nearly nine years of holding company debt service requirements.

Funding & Liquidity

The company's funding and liquidity profile remain key credit strengths. Alpine has consistently reflected a more comfortable liquidity position compared to peers, with the loan-to-deposit ratio steadily tracking at or below 80% over the past +10 years despite the expansion into more robust operating markets. The prudent approach to liquidity management, as well as the company's leading deposit market share in the Western Slope markets, conservative organic growth via de novo branch expansion, and high touch relationship-based banking model has helped facilitate the healthy liquidity position and favorable deposit mix. Moreover, while many institutions have benefitted from the significant amount of government stimulus and the Fed's actions over the past few years, Alpine has consistently reflected a favorable liquidity position and below average deposit costs through multiple interest rate cycles. The company strives for full banking relationships, which helps support a

Figure 7:



Sources: Company Reports, KBRA Research

robust level of noninterest-bearing accounts, which totaled 42% of total deposits as of 1Q22. Moreover, this helps reinforce a granular deposit base, with the top 20 relationships accounting for just 7% of total balances. Given these factors, Alpine has one of the lowest cost deposit bases of all KBRA rated institutions. Additionally, as the Fed continues to increase its target rate, which is now at the 0.75%-1.00% range, the management team believes the deposit beta will lag the rest of the market and remain very low. Aside from core deposits, which account for 97% of total funding, the only other funding sources are the aforementioned capital instruments (subordinated debt and TruPS). Over the past year, deposit inflows have remained substantial, with deposit balances increasing over $1.0 billion (22% since YE20) and excess liquidity lingering on-balance sheet, with the loan-to-deposit ratio falling to 61% as of 1Q22. With that said, this has hampered profitability, and management is taking actions to deploy excess liquidity through further growth in the securities portfolio, which has increased to $1.7 billion (28% of assets) compared to $950 million the year prior (17% of assets), as well as loan growth, and allowing for certain reciprocal deposits to leave the bank (~$250 million one-way sell, though these relationships can be brought back whenever is needed). Over time, management would prefer to reposition the earning asset mix closer to pre-pandemic levels. Aside from traditional borrowing sources, including FHLB and FRB, which are currently untapped, nearly half of the securities portfolio is available for sale. Moreover, with regard to the composition of the securities portfolio, municipal bonds account for 51%, followed by U.S. treasuries and agency securities (24%), and RMBS (23%).

Key Qualitative Rating Determinants

The qualitative aspects of Alpine Banks of Colorado were assessed using a scorecard that focuses on four key factors: market strategy, risk management, liquidity management, and the operating environment. For the most part, the bank scored average for qualitative factors. For qualitative aspects, KBRA relies principally on discussions with management supplemented by publicly available data, regulatory filings and KBRA's view of the economic and regulatory environment. The following describes KBRA's qualitative assessment for Alpine Banks of Colorado:

Market Strategy

Alpine embodies the description "Community Bank" in most ways, having been founded in 1973, and growing organically since then, other than a relatively small-scale acquisition in 2006 that expanded the company into the Telluride market. More recently (in 2014), Alpine opened its first branch in Denver, and has made good progress with four branches in Front Range markets of Colorado, having grown over an $800 million loan book, as well as nearly $500 million of deposits at 1Q22 Additionally, the company just recently opened an LPO in the Fort Collins market in June 2020, which has generated $60 million of loans thus far. Moreover, a land lease has been finalized in Fort Collins, which should become a permanent branch in the near future (4Q22). Another market that the management team is targeting is Colorado Springs, in which they plan to open a branch in 4Q22 as well. Having initially considered the diversification of operating footprint into an economically vibrant Denver MSA, given its top

share position in its heritage Western Slope markets, the company's strategic expansion plans have been focused and are likely to remain exclusively on the Front Range.

Beyond its footprint, which has developed from its headquarters' market (Glenwood Springs), Alpine seems very well connected to the communities it operates in, reflecting an enviable corporate culture that starts with a tenured senior management team, each of whom has been with the company for a long time. A longstanding "high touch" customer delivery and service model remains at the core of Alpine's business model and culture. From a financial perspective, it has manifested itself most clearly in the company's extremely low-cost core deposit base, but according to management, also exists with respect to loan pricing. Beyond the most traditional lending, deposit and payment related services, Alpine reflects an attractive and growing wealth management operation, which recently surpasses $1 billion AUM ($1.1 billion as of 1Q22).

With significant demand for commercial and residential real estate, as well as comparatively limited attractive C&I lending opportunities in its core Western Slope markets, Alpine was deliberate in adding expertise in and infrastructure for the latter, until the opportunities became clearer in Front Range markets. While typically growing its management and senior staff internally through its operating history, Alpine aptly recognized the need to add C&I bankers as part of its successful Front Range expansion.

Risk Management

Substantial insider and employee ownership, as well as extensive management experience in its core markets, remain instrumental drivers of Alpine's approach and capabilities with respect to credit risk management, which, like most community banks, is the principal risk facing the institution. Part of this "experience", particularly with respect to credit risk management, was developed through knowledge gained in the challenging period surrounding the GFC. We consider this experience to have been instrumental in enhancing the credit culture at Alpine. In addition to a traditional credit review function, Alpine utilizes an outside CPA firm to conduct an independent quarterly review, primarily of its top 40 lending relationships.

Alpine's institution wide credit culture is viewed favorably, and prior to the past year, the company was rather unique and did not have Chief Credit Officer by title. However, Alpine recently announced that Rachel Gerlach has taken on the title of Chief Credit Officer. Prior to this her title was the Chief Operations Officer, although her duties included those normally covered by a Chief Credit Officer. With that said, any deposit operations that she was previously in charge of has been moved to other areas and she is now solely focused on the credit side. Each credit executive has been an Alpine employee for more than 15 years, and like most of their respective teams, has experience both as a lender, as well in their current functions. The senior loan committee, through which Alpine approves all large credits and any potential exceptions to underwriting guidelines, is comprised of Senior Management and Credit executives.

In addition to Alpine's somewhat unique Credit Risk Management organizational structure, at least by corporate title, we would also offer some perspective on the company's somewhat less granular than typical commercial

exposure risk grading scale. Alpine has operated for years with a three-grade scale: (A) Pass, (B) Special Mention and (C) Substandard (and below). Even acknowledging that in a more common 10 grade scale, most of the Pass credits are typically in categories 4 and 5, all else equal, we still prefer a more granular risk rating scale than not. That said, we would always prefer a pervasive credit culture that encompasses the line lenders, than necessarily traditional department titles and/or standard commercial loan risk grading scales, and that is a characteristic that we believe Alpine reflects.

Liquidity Management

Alpine's liquidity management is obviously enhanced by the company's robust and low-cost core deposit base. Only since entering the Front Range markets, which offer greater lending opportunities has the company's loan-to-core deposit ratio moved upwards from the mid-70% range. While the lack of wholesale borrowings is not indicative of capacity, we are less enamored with the company's nearly exclusively municipal bond securities portfolio that, while consistent with much of the industry practice in its classification of holdings as HTM, is more concentrated in this bond class than peers. This is not to suggest that KBRA has any issues with respect to the credit quality associated with the portfolio. Moreover, holding company liquidity is managed conservatively in our view.

ESG Management

KBRA typically analyzes Environmental, Social, and Governance (ESG) factors through the lens of how management teams plan for and manage relevant ESG risks and opportunities. More information on KBRA's approach to ESG risk management in financial institution ratings can be found here. Over the medium-term, banks and other financial institutions will need to prioritize ESG risk management and disclosure with the likelihood of expansions in ESG-related regulation and rising investor focus on ESG issues.

Environmental Factors

Although near term climate-related risks are believed by KBRA to be well contained, we note the bank is currently in the process of introducing practices that are more sustainable and are geared toward decreasing its overall carbon footprint, among other initiatives. The bank and most of its peers do not yet estimate carbon emissions, but Scope 1 emissions are believed to be modest compared with many other types of industries. Calculating Scope 3, which primarily refers to the emissions banks finance across their portfolios, is a challenge across the sector, not only for smaller regional banks but for large multinational banks as well. Banks and other financial institutions will need to address increasing stakeholder pressure to improve disclosure of carbon and other greenhouse gas emissions, as well as prepare for the possibility of increased carbon regulation and/or carbon taxes. In common with most peers, the company's direct loan exposure to carbon-intensive industries is considered minimal relative to the total loan portfolio.

Social Factors

The bank has a strong social mission and is active in fostering economic development in its communities of operation, including small business lending and other lending, as well as other community banking services and Community Reinvestment Act (CRA) activities. Moreover, the bank received a satisfactory CRA rating during its last examination in January 2021.

Governance Factors

An ESG factor that has a meaningful impact on this rating is an effective risk management framework including conservative loan portfolio underwriting and rigorous portfolio monitoring. For supplementary information on risk management and other governance considerations including data security and cyber risk, please reference the qualitative rating determinants section beginning on page 7, most notably the Risk Management section.

Operating Environment

Overall, the U.S. banking system has a strong regulatory framework. Since the 2008 financial crisis, banking institutions have adjusted to additional rules and regulations resulting from the Dodd-Frank Wall Street Reform and Consumer Protection Act and Basel III standards. Despite some easing of regulatory burden, particularly for small to mid-sized banks in recent years, regulatory standards and oversight remain strong for the U.S. banking system. The latest research on this and other topics can be found here.

External Support

Pursuant to the 2010 Dodd-Frank Act, U.S. regulators created a resolution regime with the goal of preventing a systemic crisis if a systemically important bank fails. For non-systemically important depositories such as the bank, KBRA believes that uninsured depositors could benefit from some degree of extraordinary systemic support. However, KBRA does not foresee any regulatory support being extended to creditors or investors at the bank or its BHC. As the bank operates in the U.S. market, a well-developed economy with a AAA sovereign rating, there were no adjustments for country risk. In addition, the rating does not incorporate external support related to its ownership structure.

Ratings Approach

KBRA's ratings are supported by the following factors: i) a quantitative view of the bank's financial fundamentals, including stress testing, ii) a qualitative assessment of the bank's management and market strategy, and iii) the incorporation of potential external systemic support. KBRA's ratings for the bank holding company reflect the overall credit profile of the organization and the potential structural subordination of its liabilities to the liabilities

of its subsidiary in an event of default or regulatory intervention. KBRA's short-term ratings are derived from senior long-term bank ratings. Consistent with KBRA's typical notching practices, subordinated debt is rated one notch below senior unsecured debt.

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