

Community Shores Bank Corp.

OTC BB: CSHB - \$8.00
www.communityshores.com

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3Q02 Results

Undervalued Bank Posts Record EPS Growth, Gains Market Share

Current Data		EPS (FYE: December)		P/E
Current Price	\$ 8.00	2001	\$ 0.37	21.9
52-Week Range	9.49-5.9	2002E	\$ 0.61	13.2
Shares Out (Mill)	1.27	2003E	\$ 0.59	13.6
Ave Vol. LTM (Actl.)	800	Valuation		This Qtr
Market Cap.	\$ 10.2	P/E	10.74	35-18
Equity/Totl Assets	6.0%	P/B	0.98	1.1-0.7
Institutional Hldgs	na	Operating Data		This Qtr
Insiders Hldgs	31.5%	Net Int. Inc. Growth	20.1%	20.1%
Book Value	\$ 8.18	Net Interest Margin	3.40%	3.39%
10Yr Bond	3.94%	Net Inc. Growth	42.9%	218.8%

Note: CSHB commenced operations January 1999.



Source: Big Charts

Key Investment Points

- EPS was \$0.19 versus \$0.14 in 3Q01 and \$0.14 in 2Q02.
- 8th consecutive quarter of profitability and record EPS.
- Guidance increased for 2003.
- Efficiency ratio improved to 0.76 compared to 0.80 in 3Q01.
- 12-18 month target price reduced to \$11.00 from of \$11.40 to reflect impact of taxes on EPS.

Company Description

Based in Muskegon, Michigan, Community Shores Bank Corporation (“CSHB”) is the holding company for Community Shores Bank (“Bank”), a Michigan chartered bank with FDIC coverage. The Bank commenced operations on January 18, 1999 and had about \$175 million in assets at September 30, 2002. CSHB serves the greater Muskegon market from two locations in Muskegon (including the headquarters location), and one in Grand Haven (Northern Ottawa County), Michigan, as well as personal Internet banking services and business Internet services (to be released in the fall).

Please read the important disclosures at the end of this report.

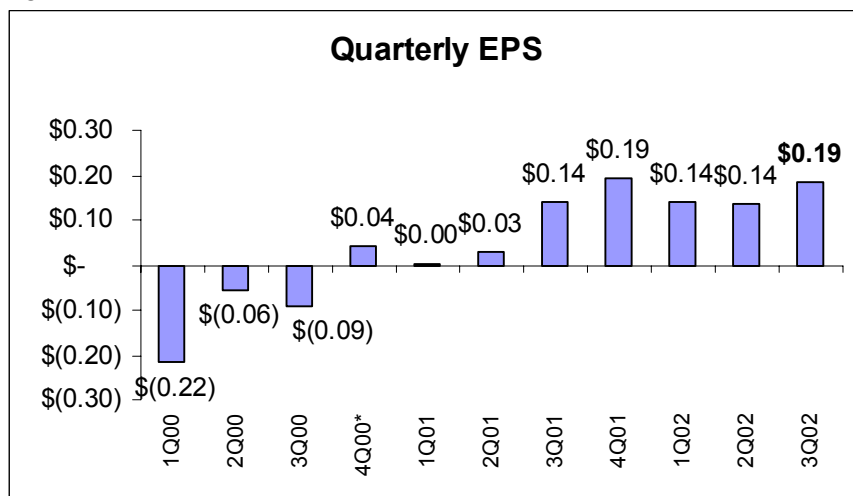
The Bottom Line:

CSHB continues to prove that there is money to be made in community banking. This young de novo bank has posted steadily improving quarterly EPS since opening its doors in early 1999. While EPS are expected to dip in 2003 (as the result of having to start paying taxes) we expect CSHB to outperform its competition in the long run. Our 12-18 month target price is \$11.00.

3Q02 Results

CSHB posted its eighth consecutive quarter of profitability in 3Q02, despite a declining interest rate environment, as it continued to gain market share and control expenses. CSHB's net income rose 42.6% to \$235,712, or \$0.19 per share, from \$165,311, or \$0.14 per share, in 3Q01. Figure 1 illustrates the trend in quarterly EPS.

Figure 1



Among the quarter's highlights are the following:

- Total loans grew 14.1% from FYE01 and 18.4% from 3Q01. Since year-end 2001, commercial loans increased 14.8% while the retail portfolio grew 12.7%. CSHB's strategy remains focused on growing the commercial banking business but has expanded its efforts via increased installment and home equity loans.
- The net interest margin held steady at 3.51% despite a 125 basis point fall in the prime rate since last year.
- Deposits increased 24% vs. 3Q01.
- Non-interest income rose 75.2% as the result of service charge income, mortgage loan refinancing fees, and brokerage commissions.
- Non-interest expenses rose 20.6% to service its growing business. CSHB added 10 employees so far in 2002, increased spending in data processing (to service volume and for its internet initiative), and as insurance premiums increased 13%.
- Annualized return on Assets was 0.57% versus 0.47% in 3Q01.
- Return on Average Equity was 9.17% compared to 7.52% in 3Q01.

As expected, CSHB has reached its allowance for loan loss target level of 1.36% of total loans. Past due loans have been increasing, but this appears to be due more to the normal "aging" of a de novo bank's loan portfolio and some timing issues.

Table 1 compares 3Q results of 2002 with the same period in 2001.

Table 1: Quarter Comparison			
(\$Million)	3Q01	3Q02	Change
Net Interest Inc	1.171	1.407	20.1%
Loan Loss Prov	-0.101	-0.154	52.0%
Dep. Service Chrgs	0.054	0.138	154.5%
Othr Non-Int Inc	0.080	0.051	-36.0%
Tot. Non-Int Inc	0.134	0.235	75.5%
Comp & bennies	0.560	0.714	27.5%
% Tot Revs	42.9%	43.5%	1.3%
Occ & Equip	0.186	0.184	-0.9%
Other Non-Int Exp	0.293	0.354	20.9%
Tot. Non-Int Exp	1.038	1.252	20.6%
Net Before Taxes	0.165	0.236	42.8%
Taxes	0.000	0.000	na
Net After Tax	0.165	0.236	42.8%
EPS	\$ 0.14	\$ 0.19	31.6%
Eff Tax Rate	0.0%	0.0%	
Shares	1.170	1.269	8.5%
Net Int. Margin	3.52%	3.40%	
Ave Earning Assets	135.9	163.0	
ROAE	7.4%	9.2%	
Efficiency Ratio	0.796	0.762	
Allow./Total Loan	1.30%	1.36%	

Financial Condition

CSHB as a holding company remains well capitalized with a Tier 1 capital to risk-weighted assets ratio of 10.51%, versus the required 10.0% limit. In order to maintain the “well capitalized” status and fund future growth, CSHB sold 10,000 in restricted stock at \$8.00 per share during the quarter. The sale of restricted stock and the loan from the Board of Directors were needed to finance the bank’s rapid growth rate. If earnings start to outpace asset growth, we would expect the need for additional stock sales would decline.

Outlook

While our 2002 EPS forecast increased to \$0.61 from \$0.54, our 2003 estimate was reduced to \$0.59 from \$0.64. The reasons for the forecasted decline in 2003 EPS, despite the steady increase in net income, are: (1) paying taxes for the first time, and (2) the dilutive effect of stock sales required to maintain capital ratios.

Our other main assumptions are as follows:

- Earning assets expected to grow approximately 5% per quarter sequentially, resulting in 20% total growth in 2002, and about 19% growth in 2003. This is a slower growth rate than previously assumed and reflects the effects of the growing size of CSHB and, to a lesser extent, increased competition.
- Loans, as a percent of earning assets remain at 82.0%, a level in line with historical figures, by 3Q02, staying at that level throughout 2003, as the Bank makes new loans from its growing deposit base.

- The Loan loss provision (“LLP”) is expected to remain at 1.36% of loans through 2003, and then taper to 1.33%. The LLP was 1.30% of loans in 2001.
- Net interest margin remains relatively stable at current levels. We may be near the bottom of the interest rate cycle, but asset/liability management tools should allow the bank to maintain current NIM.
- Non-interest income growth should remain strong in 4Q02, driven by low rates and mortgage activity. In 2003 we expect the momentum to slow in 2003 as mortgage refi activity is expected to slow and interest rates start to rise.
- The growth of operating costs are expected to slow as CSHB emerges from its initial growth stage. Compensation and benefits (“C&B”) costs increase 21.4% and 15.2% in 2002 and 2003, respectively (versus a 30%+ rate in 2000 and 2001). Occupancy and equipment (“O&E”) costs are expected to rise 2.0% and 4.0% in 2002 and 2003 (versus 35% in 2000 and 20% in 2001, as a new branch was opened and employees were added).
- Other non-interest expense growth is expected to slow as no additional branches are expected to open until late 2003. This category (which consists of advertising, supplies, bank fees, outside services, loan expenses, directors’ fees, and non-sufficient fund losses) is expected to grow 16% in 2002 (in 2001 this category grew 25.3%) and grow 7.8% in 2003.
- The Bank will begin paying taxes in 2003, at a 34.0% effective rate.

As Table 2 shows, the growth in earning assets is expected to remain high throughout 2003, but earnings per share growth will dip in 2003 as the result of having to start paying income taxes (the bank will likely use up its net loss carry-forwards in mid-2003). Table 3 contains our quarterly forecast through 2003.

(\$Million)	1999	2000	2001	2002 e	2003 e
Net Interest Inc	1.458	3.095	4.420	5.399	6.154
Loan Loss Prov	-0.852	-0.505	-0.395	-0.586	-0.569
Dep. Service Chrgs	0.065	0.233	0.324	0.501	0.510
Othr Non-Int Inc	0.088	0.185	0.322	0.366	0.380
Tot. Non-Int Inc	0.153	0.418	0.646	0.866	0.890
Comp & bennies	1.425	1.855	2.249	2.730	3.145
% Tot Revs	88%	53%	44%	44%	45%
Occ & Equip	0.449	0.606	0.727	0.741	0.772
Other Non-Int Exp	0.687	0.926	1.267	1.460	1.400
Tot. Non-Int Exp	2.561	3.387	4.243	4.931	5.317
Net Before Taxes	-1.802	-0.378	0.428	0.748	1.158
Taxes	0.000	0.000	0.000	0.000	-0.394
Net After Tax	-1.802	-0.378	0.428	0.748	0.764
EPS	\$ (1.55)	\$ (0.32)	\$ 0.37	\$ 0.61	\$ 0.59
Eff Tax Rate	0%	0%	0%	0%	34%
Shares	1.16	1.17	1.17	1.23	1.30
Return/AEA	3.73%	3.13%	3.35%	3.27%	3.28%
Earning Assets	67.6	118.2	142.9	171.5	203.7
Growth		75%	21%	20%	19%

	1Q	2Q	3Q	4Q	FY
1999	\$ (0.52)	\$ (0.45)	\$ (0.26)	\$ (0.33)	\$ (1.55)
2000	\$ (0.22)	\$ (0.06)	\$ (0.09)	\$ 0.04	\$ (0.32)
2001	\$ 0.00	\$ 0.03	\$ 0.14	\$ 0.19	\$ 0.37
2002	\$ 0.14	\$ 0.14	\$ 0.19	\$ 0.14	\$ 0.61
2003	\$ 0.11	\$ 0.13	\$ 0.17	\$ 0.19	\$ 0.59
Boldfaced data are forecasts.					
Growth					
2001	101.6%	148.3%	256.0%	-375.4%	213.3%
2002	3988.6%	401.0%	31.8%	-26.9%	66.0%
2003	-23.9%	-5.5%	-10.1%	30.4%	-3.0%

Valuation Analysis

We lowered our 12-18 month target price to \$11.00 from \$11.40 due to the impact of dilution and taxes on our EPS forecast. The 2003 assumed P/E and P/B multiples are the averages of the peer group's historical P/B and P/E multiples and CSHB's historic and current multiples. We then used these multiples on our forecasts of book value and EPS. Our methodology is shown in Table 4

		Multiples				2003 Ests.	Price Range	
		Peers*		CSHB				
		LTM	LTM	Current	Assumed			
Price/Book	High	1.17	1.23	0.97	1.20	\$ 10.65	\$ 12.78	\$ 10.91
	Low	0.95	0.77		0.85		\$ 9.05	
P/E (LTM)	High	15.8	35.2	10.74	22.00	\$ 0.59	\$ 12.97	\$ 10.91
	Low	11.9	11.8		15.00		\$ 8.84	

* Michigan Peers: MSBF, DEAR, CCBD	Range	High	\$ 12.97
		Low	\$ 8.84
		Average	\$ 10.91

We think these are reasonable assumptions based upon peer group averages and CSHB's expected growth rate. Bank valuations center more on price/book ("P/B") than price/earnings ("P/E") ratios. Our assumed P/B multiple is below the peer average. We assumed a high P/E multiple (although it is within CSHB's historic range) because we expect earnings to continue growing at an above average rate. Table 5 compares CSHB and peer group valuations as of the end of October.

	TKR	Assets*	P/E	P/B	Price	LTM EPS	Book
COMMUNITY SHORES	CSHB	\$ 174.8	13.0	1.0	\$8.00	\$0.61	\$8.24
Peer Group average		186.0	15.4	1.1	\$16.25	\$1.14	\$14.73
Peer Group							
DEARBORN BANCORP	DEAR	296.9	17.3	1.30	\$15.55	\$0.90	\$11.40
COMMUNITY CENTRAL BK	CCBD	280.2	14.2	1.14	\$9.40	\$0.66	\$8.26
GLB BANCORP	GLBK	183.2	22.0	0.79	\$9.60	\$0.44	\$12.18
FIRST BANCORP IND	FBEI	182.2	18.6	0.79	\$14.30	\$0.77	\$18.81
HIGH COUNTRY BNCRP	HCBC	178.4	11.8	1.24	\$22.75	\$1.92	\$18.60
GREAT AMER BANCORP	GTPS	167.6	13.3	1.16	\$26.50	\$1.99	\$20.84
MAYFLOWER CO-OP BK	MFLR	167.2	14.0	1.49	\$14.70	\$1.05	\$8.96
BANK SOUTH CAROLINA	BKSC	166.1	18.0	1.60	\$12.24	\$0.68	\$7.65
FALMOUTH BANCORP	FCB	155.4	15.4	1.39	\$25.25	\$1.64	\$18.15
FIRST INDEPENDENCE	FFSL	153.0	10.8	0.96	\$14.97	\$1.38	\$15.29
LOGANSPORT FINANCIAL	LOGN	151.0	11.1	0.81	\$15.48	\$1.40	\$17.08
FIRST KANSAS FIN'L	FKAN	150.9	18.0	0.77	\$14.24	\$0.79	\$19.49

Source: Baseline *Million

Investment Risks

Investors need to consider the following risks when investing in these shares:

The Bank has only existed for three years and faces the challenges of building a brand name and reputation in a very competitive market. However, we have found that in banking, the community banks often succeed in the face of larger competitors.

The shares are not very liquid due to the high percentage of insider ownership and the lack of information on CSHB available to investors.

Operating results are dependent upon the economic health of the western Michigan market.

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