Speaker 1: Good morning, and welcome to the Premier Financial Corp third quarter 2022 earnings conference call. At this time, all participants will be in listen-only mode. After today's presentation, there will be an opportunity to ask questions. If you'd like to ask a question, please press *1 on your telephone keypad at any time. Please note, this event is being recorded. I would now like to turn the conference over to Paul Nungester with Premier Financial Corp. Please go ahead, sir.

Paul Nungester: Thank you. Good morning, everyone, and thank you for joining us for today's third quarter 2022 earnings conference call. This call is also being webcast, and the audio replay will be available at the Premier Financial Corp Website at premierfincorp.com. Following our prepared comments on the company's strategy and performance, we will be available to take your questions. Before we begin, I'd like to remind you that during the conference call today, including during the question and answer period, you may hear forward-looking statements related to future financial results and business operations for Premier Financial Corp. Actually results may differ materially from current management forecasts and projections, as a result of factors over which the company has no control. Information on these risk factors and additional information on forward-looking statements are included in the news release and in the company's reports on file with the Securities and Exchange Commission. And I'll turn the call over to Gary for his opening comments.

Gary Small: Thank you, Paul, and good morning, I appreciate your joining us today. I am very pleased to report Premier's third quarter earnings of $28.2 million, or 79 cents per share. That's a good outcome from our perspective, over a difficult operating environment. Pre-tax provision income was up 13% over the prior quarter, and total revenue growth for the quarter was 8.9%, which enabled us to post a very strong positive operating leverage figure, and that's a key metric for our organization.

The team posted another quarter of strong loan and deposit growth, as has been the case over the course of the year. So again, good growth in all three categories: commercial, consumer, and residential. We are extremely pleased with our quarterly commercial growth of 4%, as it follows an extremely strong second quarter, very encouraged and it really reflects the organization's ability to expand its client base. As Matt will share with us, our mix of C&I business continues to climb.

Our customer deposit growth for the quarter was 9% annualized, and I assure you we're working hard to keep pace with the loan growth. Business deposits continue to grow, with our commercial treasury and branch teams doing an excellent job on the deposit acquisition front. September non-interest-bearing deposits for the year were up 10% over September of the prior year.

Moving on to the consumer side, consumer spending is feeding our non-interest income for the quarter. Deposit and interchange fees were up 7.8% over the same period last year, and it's helping to offset the continued difficulty that we are experiencing in the residential mortgage market, where gain on sales under pressure with the secondary market sales due to a lag in volume and pricing challenges.

Our insurance business is benefiting from the inflationary environment from a renewal- revenue perspective, and our wealth team is having more value-added conversations with its clients than ever before, they're really leading through, again, a turbulent market environment. Expenses are right on expectation, and that's while we are also absorbing a mid-year compensation adjustment that we made again to mitigate to some degree some of the inflationary pressures we see.

In summary, it was an excellent asset growth period, with good, strong net interest income growth, with deposit-gathering and beta management being the issues of the day. And Paul and Matt will share some more details. Paul?

Paul Nungester: Thank you, Gary. I'll review our second quarter results- sorry, third quarter results, and start by highlighting another strong quarter of growth. Total loans, including those held for sale, increased by 301 million during the quarter, representing 20% annualized growth, or 16% year over year growth. Once again, we saw growth in all categories, including commercial, residential, and consumer.

We also had another good quarter in deposit growth, which increased 146 million or 9% annualized, excluding 70 million of broker deposits. Both non-interest-bearing and interest-bearing deposits each had strong 9% annualized growth. Our loans to deposits ratio was approximately 92% at 9/30, and we expect to remain in the low 90s near-term. This growth, in concert with the rising rate environment, drove improved net interest income and margin expansion. Net interest income increased 7% on a linked quarter basis, and 11% from the prior year, while core margin, excluding PPP and acquisition marks accretion, increased four basis points from second quarter 2022 and nine basis points from third quarter 2021.

This was primarily due to loan growth and higher loan yields, which increased 30 basis points from 2Q to 4.24%, excluding PPP and acquisition marks accretion. Largely offsetting this was an increase in average cost of funds, which rose 31 basis points on a linked quarter basis to 0.55%. This was primarily due to an increase in average deposit cost, which grew 24 basis points on a linked quarter basis to 0.39%, excluding acquisition marks accretion and broker deposits, as well as continued increased costs on FHLB borrowing.

Our loan yield expansion in 3Q represented a 21% beta compared to the change in the average effective federal funds rate for the quarter. While our total deposit beta, excluding marks and broker deposits, was 17%. We would expect this general trend to continue in 4Q and early 2023. That in combination with utilization of higher costs, high beta FHLB borrowings, that have supported our recent loan growth in excess of deposit growth, means we would expect our near-term NIM trend to be generally consistent with 3Q.

Downside risk here would most likely come from deposit runoff, and/or the deposit beta exceeding our loan beta. Next, non-interest income of 16.7 million for 3Q was up 2.3 million from the prior quarter, primarily due to mortgage banking and security gains. Mortgage banking income increased two million on a linked quarter basis, due to a $2.2 million increase in gains, offset by a 0.2 million lower MSR valuation gain.

Security gains were 43,000 in 3Q, from increased valuations on equity securities, compared to 1.2 million of losses in 2Q. These increases were partially offset by seasonal 0.8 million decrease in insurance commissions. Expenses of 41 million were up 5% on a linked quarter basis, as expected, primarily due to higher compensation and benefits. Fees increased 2.2 million, partly from lower deferred costs related to lower quarterly loan production, as well as higher base compensation, for mid-year adjustments we made related to a recent market compensation analysis.

Higher revenues helped improve our efficiency ratio, which declined to 51.3% for 3Q from 52.2% in 2Q. The net effect of higher revenues, offset partially by higher expenses, led to a 13% linked quarter increase in pre-tax, pre-provision income, of $39 million and a 1.9% return on average assets.

The allowance increased 3.6 million in 3Q due to 3.7 million of provision expense, all for loan growth offset slightly by only 154,000 of charge-offs. Our asset quality stats improved again during the quarter, with decreases for nonperforming assets and classified loans of five and 8%, respectively. At September 30, our allowance coverage of non-performing loans was 213%.

Finishing the balance sheet is capital, with a quarterly decrease primarily due to a $44 million negative evaluation adjustment on the available for sale securities portfolio. At September 30, our tangible equity ratio was 6.7%, down from 7.3% at 6/30. However, excluding AOCI, tangible equity would be 9.0% at 9/30, consistent with June 30. Additionally, our regulatory ratios are comfortably in excess of well-capitalized guidelines, with tier one capital at approximately 10.1%, and total capital at approximately 11.9% on a consolidated basis at 9/30. That completes my financial review, and I'll now turn the call over to Matt.

Matt Garrity: Thanks, Paul. We're pleased to report total loan growth net of PPP in excess of $316 million, for 5.44% for the third quarter. Our commercial business experienced another strong quarter of loan growth, with third quarter growth of approximately 3.8% or $151 million. Commercial loan growth was outstanding at 15.9%, for approximately $563 million on a year to date basis. C&I loan growth has been a significant contributor to our overall loan growth, as C&I balances grew during the third quarter by 5.48%, or approximately $54.2 million compared to the second quarter.

On a trailing four-quarter basis, C&I balance growth was 28.77% or approximately $232.6 million. Line utilization for the third quarter remained relatively unchanged from the second quarter, as utilization remains under 40%. For the fourth quarter, we expect commercial balance growth to be flatter in the low single-digit range, based on a combination of anticipated payoffs and lower pipeline levels caused by a higher rate environment and ongoing general economic uncertainty.

In our residential mortgage business, we saw meaningful improvement in total mortgage banking revenue during the third quarter of 2022 compared to the second quarter. Overall, industry conditions remain challenging, due to the combination of increasing rates and declining demand, resulting in third quarter 2022 mortgage banking income that was 36% lower than the third quarter of 2021.

Origination activity decreased approximately 15% in the third quarter of 2022 compared to the second quarter, a reflection of a softer overall market and our decision to increase pricing of our non-salable products in an effort to temper our use of the portfolio. Given the rate and demand challenges, as well as the fact that the fourth quarter is typically a seasonal period of lower demand, our outlook for the fourth quarter's origination activity is for a relatively soft quarter.

Consumer loan activity was very good in the third quarter, with balances growing 8.61% or $38.5 million compared to the second quarter. On a trailing four-quarter basis, our consumer portfolio has grown by 24.62%, for approximately $95.9 million. With respect to asset quality, we had another quarter of improvement, as third quarter levels of classified and criticized loans declined by 7.83% and 10.63% respectively, on a linked quarter basis. When comparing the third quarter of 2022 to the third quarter of 2021, levels of classified and criticized loans improved by 50.02% and 46.49% respectively. Nonperforming loan levels improved during the third quarter by 4.6% compared to the prior quarter, while net charge-offs for the third quarter were $154,000.

We continue to monitor our portfolio closely for signs of stress, given the ongoing volatility in interest rates, continued inflationary pressures, and overall economic uncertainty. Our outlook for asset quality remains stable. I'd now like to turn the call back over to Gary Small. Gary?

Gary Small: Thanks, Matt, and now I'll give you some thoughts relevant to our performance expectations through the end of the year. From a balance sheet perspective, we're looking at modest earning asset growth, for the fourth quarter, somewhere in the 2% range. The commercial new business generation will continue to be strong, but a bit more moderate than it has been, over the last two quarters. And these will be offset by some specific exits of client companies, who have been recently acquired. We always have pay-downs in the fourth quarter and so forth. So more modest growth.

And on the consumer side, expect the portfolio to be relatively flat, versus Q3, up 24%, as Matt mentioned, for the year to date number. We're very pleased with our position, as we stand right now. Margin improvement will be leveling off as we remain very much focused on deposit acquisition in our tactical strategies on closing out our wholesale funding position and that will have some impact on our upside margin.

From a fee business perspective, consumer-banking fees will remain ahead of their original targets. Mortgage fee income will continue to be under stress and be hard-pressed to match the third quarter that we posted. Expenses, we're gonna stick with our original guidance that we updated last quarter at 163 million for the year, and we would see an efficiency ratio still in the 52% range for the full year.

From a credit perspective, as Paul was mentioning, provisions driven primarily by portfolio growth. That's very much consistent with CECL methodology. There could be some potential additional movement if the unemployment forecast moves substantially, that's another CECL variable. So some unknowns there. But generally speaking, pre-tax and pre-provision income for Q4 plus or minus a couple percent, will look very much the same as what we saw in Q3. From an equity standpoint, we have no specific plans regarding additional repurchase activity through the end of the year. And with that, I'll turn it back over to Sam, our operator, to take questions.

Speaker 1: Thank you, Gary, we will now begin the Q&A session. If you'd like to ask a question, again, it is *1 on your telephone keypad. If for any reason you'd like to remove that question, you may press *2. As a reminder, if you are using a speakerphone, please remember to pick up your handset before asking your question. Our first question comes from the line of Michael Perito with KBW. Michael, your line is now open.

Speaker 5: Hey guys, thanks for taking my question.

Gary Small: Morning, Mike.

Michael Perito: Appreciate the [inaudible] pretty specific commentary for next quarter, which is, you know, which I'm sure we all appreciate. Just as we look out to next year, though, understanding the environment's difficult, I'm not gonna ask you to, to give any type of, like, growth targets or anything like that. It's more of just like I guess a strategic question which is if we are in an environment where, you know, the Moody- the current Moody's forecast is accurate and, and fed funds remain in the, you know, pretty elevated, right, relative to where it's been historically, like, what do you guys, what's your appetite to grow beyond your ability to fund with deposits? Or maybe asked another way, you know, like if we're thinking about a growth rate for next year, I mean, is it a growth rate that, you know, will likely have to be funded by your deposit growth, or will you take on borrowings? Maybe just some refresh there would be helpful, 'cause it does

seem like you guys have some pretty good momentum on the loan side, but obviously, the deposit market continues to get more challenging.

Gary Small: I'll take a swing at that. Good question, and you're right. From a visibility standpoint, we can't be too specific, but I'll say this. Our loan growth next year will be very much in line and supported by our expected deposit growth, in support of that growth, and you wouldn't have as, I wouldn't expect as big a disconnect, if you will, as we have experienced this year. For all the right reasons, we're very pleased with the year that we posted, and that was purposeful.

At the same time, we have some other levers we're, be pulling, that we would expect to work our way in a favorable position relative to our existing federal home loan bank position. Typically it's not quite as punitive to be in that position on the portfolio as it is currently, and with the upside being unlimited, we share your enthusiasm for reducing that number in the near term. And it's one of the reasons our deposit margin our overall margin aspirations are more moderate, because we are going to be out, as we have been gathering new funds, and rate's a part of that equation, but it's gonna be such a more beneficial rate than the rate we're experiencing with the federal home loan bank, so ... A long answer to your question, but.

Michael Perito: No, no, that's helpful.

Gary Small: We'll fund our- we'll fund ourselves next year and we'll work off some of what we've got.

Michael Perito: Yeah. And so maybe just a follow-up to that for, for Paul, I mean, is like a three, three and a half margin year, plus or minus kind of where you think you'll trend over the next quarter or two? And then it sounds like, you know, if you guys are gonna grow, continue to grow, you know, there's probably not a ton of room to expand beyond that. I mean, without locking you in, do you think that's generally a fair way to, to be thinking about it at this point, just given where the, the forecast, the consensus forecast is for rates?

Paul Nungester: Good question, Mike. What I would say is kinda reiterate what we said during the call, that, you know, where we're at today is around where we expect to be, at least near-term, as we work through this deposit gathering strategy. So, you know, plus or minus a few bps from 3Q is, is where you can think at least for the next quarter or two, and from there, you know, we'll reassess as we finalize our plans coming out of 4Q and how successful we are on the deposit front.

Michael Perito: Got it. Helpful. And then just lastly for me and I'll step back, the 52% efficiency ratio range for the full year, you know, that kind of puts you generally flat with where you were this quarter, next quarter, right? Like around 51% as we exit '22 and look to '23. I guess just as we think about next year, investment rate Gary, you know, obviously there's some inflationary pressures that might be a bit more than normal, but beyond that, I mean, are there any technology-related or 10 billion in asset-related investments on the regulatory compliance or infrastructure side that that could potentially impact the growth rate or their off-sesh how are you kinda thinking about that as I'm sure you guys are starting the, the budgeting process around that for, for next year as we speak?

Gary Small: Well, you know, Mike, there's always, there's always things that are added to the plate and there are things that fall away as completed, and next year we will start to spend a little bit more on the, some of the features that need some time to mature, as we head into the whole 10 billion territory, there are initiatives that we will be a little bit more active on than we have in the past. And, we do foresee a good effort from a customer experience standpoint as we go to work on one of our systems there. But that's not inconsistent with the sort of activity that we would have every year, and there's other activity that we were engaged with this year that's completed, and we'll just redeploy those funds to that. So, there are those elements, but I wouldn't look for them to necessarily change the dynamic of our efficiency ratio.

Michael Perito: Yeah, so I was going to say so theoretically, right, if you're 52 for the full year, but you're 51 on the exit. So I mean, you should, as it stands today, you guys think some modest, some moderate, rather operating leverage isn't out of the question for '23?

Gary Small: Mm-hmm

Paul Nungester Yeah.

Michael Perito: Okay.

Gary Small: Yes.

Michael Perito: Um, great guys, thank you very much. I appreciate it.

Paul Nungester: Thanks, Mike.

Speaker 1: Thank you, Mr. Perito. The next question comes from the line of Brendan Nosal with Piper Sandler. Brendan, your line is now open.

Brendan Nosal: Hey, good morning, guys. How are you doing?

Gary Small: Morning.

Brendan Nosal: Um, maybe just to start off here on kind of deposit pricing. Um, was kinda hoping you could give us an updated beta outlook through the, through the cycle, I guess, you know, this quarter, [inaudible] around the 23, 24% sequential data, it sounds like you're gonna be actively gathering deposits to help fund your loan growth, and that certainly could come at a, an expense. I'm just kinda curious how you think about that.

Paul Nungester: Mm-hmm. Yeah, I can take that one, Brendan. Excuse me. Yeah, third quarter, uh, it obviously picked up pace, as we thought, in the low 20s there for, for deposits. Uh, we see that continuing, um, maybe taken up as we, focus even more on deposit-gathering, a- as Gary was, uh, just saying, to help with cutting into our FLHB position, things like that. And as it stands now, uh, we're still looking to come in around, uh, once the full cycle's [inaudible] around that low 30%, uh, beta that we previously talked about. You know, right now, to date, and you can think of that, you know, go back to 4Q before any Fed movement started in first quarter, and comparing to third quarter, we're in the mid-teens, low teens on total deposits from a beta perspective. So we've got a little room from the get-go, from the lags as everybody was kinda dragging heels, on the deposit side, but now it's gonna start picking up. Um, and we'll start feeling, most likely some more competitive pressure as everybody's starting to post loan growth, like we have for the past two quarters.

So, so yeah, it'll pick up, on the deposit beta specifically for the next quarter or two for sure, but still, once we get through all that, should come in on an average around the 30 to low 30s there.

Brendan Nosal: Okay. Fantastic, that- that's super helpful color, I appreciate it. Maybe turning to fee income for a moment, just kinda looking at that mortgage banking income line. I mean it, it was, even though it was down year over year, it was up quite substantially from the second quarter, which feels like more of an aberration, this earning season. Maybe just kinda discuss what allowed that line item to improve so much sequentially? And, you know, near-term expectations as we move through the balance of the year.

Matt Garrity: Brendan, this is Matt, and I'll answer that question. I think you're, you're spot on. It is a little bit of an aberration, it was a little bit of a timing issue regarding the recognition of that revenue, and our expectations for Q4 would be, I think relatively flat and a little bit, certainly down from the performance you saw in Q3.

Brendan Nosal: Okay, fantastic. One more for me before I step back. Just kind of curious, with, you know, organic growth returning to probably a more typical pace next year, and that being less of a call on capital, just would love to hear your updated thoughts on, on the M&A environment and, and your appetite, and based on some deals we've seen recently, obviously rate marks are highly punitive, but would love to just hear your, your updated thoughts.

Gary Small: Well, you know what I say, Brendan, is that it makes the conversations more interesting. Obviously with AOCI where it's at, you're have a ton of GAAP book dilution on a deal, and you have a ton of accretion coming back in over the short end. So academically, you should say it doesn't matter, but it surely does. And I think it slows the discussions from where they were in the first half of the year as the realization of the magnitude of the AOCIs are thought through, we may feel differently about it since you know, two or three quarters down the road, but I think both sides of the table there's a little less activity now than there was coming into the summer months, and, I think with certainty or familiarity, things will return back to their normal pace. But the numbers are, you know, out of the normal relative range and I think, has folks touching the breaks a little bit on the topic.

Brendan Nosal: Yep, yep, makes sense. All right, great. Thank you for taking my questions.

Speaker 1: Thank you Mr. Nosal. The next question comes from the line of Christopher Marinac with Janney Montgomery Scott. Christopher, your line is now open.

Christoper Marinac: Hey, thanks, good morning. Just wanted to go back to the deposit-gathering comments you made on the call, and in the Q&A. Do you have to, or can you incent your team to do more deposit-gathering? Do you have to do anything different than you may have done in, in the past? I'm just kinda curious on your experience even before this last, you know, experience with deposits the last two years.

Gary Small: Chris, I'll take a swing at that. You know, since we got together and became Premier Bank two and a half years ago, we have not had to be in a deposit-gathering mode, you know, once COVID was upon us and all the programs started in place, all the banking industry was benefiting from the money landing on the businesses and the households. So this is the first time as an organization of our combined size that we're flexing our muscle to see, to see how our eight or nine relative markets compete and where the pressures are.

Uh, in our pre-combination world, we had experience of being able to sit down and raise 5% deposits in our marketplace, and we knew the levers that worked, and we knew the magnitudes and betas that went with those, each organization did that. But this, this was our first time flexing as a combined organization in a pretty dynamic environment. So, we'll change the expectations and the goal-setting and so forth relative to that, as there's always a dynamic issue out with your team in the field, and pricing will help open that conversation up, and we will make adjustments as we see what's working well, what's working less well, combination of pricing, marketing, and the team in the field.

And as we look toward the next year, you would see more swings relative to how we reward the team. It could be the same scorecard, but just with a higher weighting on deposit gathering, perhaps, than on loan generation, as those are designed to flex with the needs of the organization.

Christoper Marinac: Great, that's really helpful feedback, thanks a lot for that. And I guess just to switch gears on credit quality, do you see anything in the horizon that changes the sorta ongoing positive trends in the special mention and the substandard, you know, classified numbers that you disclosed?

Matt Garrity: This is Matt. We, we don't and we are looking at credits robustly by sector, looking for some systemic issues, and we're not seeing it. It doesn't mean, you know, that something won't pop up as a result of a recession, but we're, we feel pretty good about where our portfolio's positioned, and how we will perform through a recession. And I think we got a quick peek of that during COVID, and how that, how well our portfolio performed.

Christoper Marinac: So is it fair though Matt that charge-offs could rise a little bit during a recession but still be relatively low compared to past history?

Matt Garrity: Oh of course, yes.

Christoper Marinac: Okay. Great. Thanks again for hosting us this morning.

Paul Nungester: Thanks Chris.

Speaker 1: Thank you Mr. Marinac. We have no further questions waiting at this time, so as a final reminder, to ask a question it is *1. We'll pause here very briefly. And we have no further questions waiting at this time, so I'd like to hand the call back over to Gary for any closing remarks.

Gary Small: Thank you, Sam. I'll just close in saying as I think I opened the call, strong growth, but our focus is 100% on deposit-gathering and managing our beta through that process, and that's gonna continue to be the, the, the theme for, I think, the next handful of quarters. For all our newness as an organization as far as having to go out and understand our markets, we wouldn't wanna lose sight of the actual performance for the year. We've had 7% year to date deposit growth, we're not in uncharted territory relative to what we need to do and is typically our case once we focus on an issue, we usually get it resolved. And this is a, the next issue that is in front of us, and we will get it resolved. So thank you all for joining us today.

Speaker 1: That concludes the Premier Financial Corp third quarter 2022 earnings conference call. Thank you all for your participation, you may now disconnect.