Camden National Corp.

Fourth Quarter 2015 Earnings Conference Call

February 5, 2016 at 11:00 a.m. Eastern

CORPORATE PARTICIPANTS

Greg Dufour – *President, Chief Executive Officer and Director*

Deborah Jordan – *Chief Operating Officer and Chief Financial Officer*

PRESENTATION

Operator
Good morning and welcome to the Camden National Corporation Fourth Quarter 2015 Earnings Conference Call. All participants will be in listen-only mode. Later, we will conduct a question and answer session. If you require operator assistance, please press star then zero. Please note this event is being recorded.

Please note that this presentation contains forward-looking statements which involve significant risks and uncertainties. Actual results could differ materially from the results discussed. The risk factors are described in the Company's Annual Report on Form 10-K and in other filings with the SEC.

Today's call presenters are Greg Dufour, President, Chief Executive Officer and Director; and Deborah Jordan, Chief Operating Officer and Chief Financial Officer.

Our first presenter is Greg Dufour. Please go ahead.

Greg Dufour
Thank you. Good morning and welcome to our fourth quarter earnings conference call. We are very pleased that in addition to closing on the acquisition of SBM Financial, the parent company of the Bank of Maine, that we are also reporting record core operating earnings of $28.2 million for 2015, with a core return on tangible equity of 13.2% and core return on assets of 0.94%.

In a few moments, Debbie will walk you through our fourth quarter results as well as various accounting adjustments related to the acquisition, but from a high level, our core earnings performance excludes one-time acquisition costs, but does include the impact of two and a half months of earnings from SBM Financial.

Last quarter's conference call was only a few days after the closing of the transaction and conversion of the systems of SBM, and I reported that a very successful conversion of systems, resources and people occurred. I am pleased to say as of today that initial success was sustained allowing us to focus on wrapping up 2015 and laying the groundwork to deliver on the commitments made when we announced the transaction.

You'll hear from Debbie momentarily that we're on target to achieve the cost savings targets in 2016, and we're within range of our estimates of one-time costs associated with the transaction.

As we have gotten to know each other better, we worked together to address some strategic matters that we feel will properly align current and future resources. We performed initial review of our branch network, and even though we consolidated four branches in October, we recently announced that we will consolidate the former Camden National Bank, Milk Street Portland Maine branch into our new location at 2 Canal Plaza in Portland that we acquired during the acquisition.

Existing staff will be reassigned to fill vacant positions, and while we'll utilize existing branch space to help house our growing Portland-based presence, we'll have a small amount of cost savings as we consolidate two branches that were just a few blocks from each other.

We also reviewed the Health Professional Funding Corporation, or HPFC, which is a wholly-owned subsidiary of the Bank of Maine. After an extensive analysis, it was determined that at this time the capital and operational resources required to allow HPFC to scale up to its full potential did not align with our need to focus on ensuring that we meet the profitability targets of the merger.

Operations at HPFC will be discontinued during the first quarter of 2016. The Company will continue to earn revenues from the HPFC loan portfolio as it naturally runs off over the next 5 to 10 years. Many of the costs to close HPFC, including severance, were recorded in our 2015 results.

Today, we're a $3.7 billion financial institution, with a broad set of products and services ranging from consumer and loan-related products, commercial products that can serve micro and small businesses all the way to complex commercial lending transactions. We have brokerage and wealth management services, cash manager and treasury services and a comprehensive residential mortgage platform.

We're delivering these services through 64 banking centers; 85 ATM locations; Acadia Trust based in Portland, Maine; our commercial loan production office in Manchester, New Hampshire; and a mortgage origination office based outside of Boston, Massachusetts. Our scale allows us to provide similar products equivalent to larger organizations, while our network of banking centers and offices, along with empowering our people in the field, allow us to further our capabilities in a genuine local-based fashion.

Since the acquisition, any run off of customers have been well within our due diligence estimates, which I attribute to the hard work of the people at Camden National as well as loyal customers of both organizations. Even though markets remain highly competitive, the impact of the acquisition did not stop us from seeing significant growth.

I'll now hand the meeting over to Debbie.

Deborah Jordan
Thank you, Greg and good morning, everyone. We are pleased to report a strong finish to the year with solid loan and deposit growth during the fourth quarter. When excluding non-core one-time merger costs, our core operating earnings of $7.7 million for the quarter increased 26% compared to the fourth quarter last year. Our fourth quarter results include the benefit of 2.5 months of the former Bank of Maine.

Core operating EPS of $0.78 per share for the fourth quarter declined 5% compared to the same period a year ago as a result of this issuing 2.7 million shares in connection with the acquisition as well as the timing of cost saves from combining the two organizations.

On a core operating basis, our return on average assets was 86 basis points and our return on average tangible equity was 11.96% for the quarter. As a result of the merger in mid-October, our revenue increased 37% over the fourth quarter of last year, while operating expenses were up 39% for the same period.

We are really pleased with the growth experienced on both the loan and deposit front during the fourth quarter. When excluding the acquired loans, our loan portfolio grew organically $45 million, which is an annualized growth rate of 10%.

Organic core deposits were up $75 million for the quarter or a 21% annualized rate, while CD and broker deposits declined 7% during the quarter.

We had a healthy fee income growth for the quarter, driven by mortgage banking income of over $1 million as we realized the benefit of an expanded mortgage origination platform with a network of originators in office locations in Falmouth, Maine and Braintree, Massachusetts.

In addition, we recorded customer loan derivative income of $861,000 during the quarter as we swapped longer-term fixed-rates on new commercial real estate transactions to LIBOR-based pricing. Our loan loss provision was slightly higher in the fourth quarter, primarily due to higher level of loan charge-offs resulting from the timing of options. For the quarter, our annualized net charge-off rate was 16 basis points bringing our annual charge-off rate to 10 basis points for the year.

Non-performing assets increased by $9 million since September 30th, as a result of the SBM acquisition as we designated $11 million of loans as non-accrual. In addition, we transferred $1 million into OREO in connection with former branch facilities that were closed and/or acquired. At year-end, non-performing assets represent just 66 basis points of total assets.

Operating costs were up 39% for the quarter after excluding merger expenses, with the increase related to 168 additional employees, 24 new locations and 55,000 new customers. We made significant progress in reducing costs and we remain on track to achieve our 37% cost save projections by the end of the second quarter of 2016.

In addition to the HPFC wind-down and one branch closure that Greg mentioned earlier, we are also closing one operation center.

Our efficiency ratio was slightly over 64% for the fourth quarter. We are forecasting the efficiency ratio to trend lower each quarter and feel confident of a 58% ratio for 2016.

As mentioned by Greg, we couldn't be more pleased with the execution of the Bank of Maine merger. There was limited customer impact and deposit attrition has been minimal with a 2% outflow of balances and a 6% account attrition rate.

During the fourth quarter, we took the opportunity to reduce our exposure to rising interest rates. This was achieved through a combination of the acquired loans and deposits, reducing borrowings, selling long-term fixed-rate mortgages and the continued CRE loan swap program.

Our investment portfolio currently stands at 23% of total assets, a decline from 29% just a quarter ago. Our income tax rate for 2015 was 32.1% and we expect it will increase slightly to 32.5% for 2016.

We are much in line with our projections related to the merger. Tangible common equity of 7.18% exceeds our 7% estimate and our total risk-based capital ratio of 12.98% is slightly below our 13% forecast. Total merger and acquisition costs are estimated to run 5% higher than the $15 million forecasted which includes $600,000 that will be incurred in the first half of 2016.

Goodwill and intangible assets are 6% lower than anticipated translating to lower tangible book value dilution of just 12% compared to our original estimate of 14%.

The lower goodwill amount relates to the deferred tax asset on the acquired net operating loss carry forward. In our original forecast, we established a valuation allowance of $10 million that we deemed wasn't necessary at year-end.

Earnings-per-share accretion for 2016 is anticipated at 11%, compared to our original estimate of 14%. This difference in EPS accretion is primarily related to the elimination of the deferred tax asset valuation allowance that was modeled to reverse into income each year.

Our dilution earn back on the SBM transaction still stands at a five-year earn back. We just swapped lower tangible book value dilution for lower earnings per share accretion, but overall no material change in economics from what was originally modeled.

We remain confident in the importance of the SBM transaction and what we can accomplish as a combined organization with the added scale and market expansion.

That concludes my comments and we will now open up the call for questions.

QUESTIONS AND ANSWERS

Operator
We will now begin the question and answer section. To ask a question, you may press star then one on your touchtone phone. If you are using a speakerphone, please pick up your handset before pressing the keys. To withdraw your question, please press star then two. At this time, we will pause momentarily to assemble our roster.

Our first question comes from Matt Kelley of Piper Jaffray. Please go ahead.

Matt Kelley
Yes. Good morning.

Greg Dufour
Good morning.

Matt Kelley
Just a question on the cost saves in the SBM transaction. When I go back and look at what they were running at, they were running at about $7.5 million a quarter, so call it a $30 million annualized type of run rate, with 37% expenses should be $11 million in terms of the dollar amount of cost saves. Is that the right bogie from a dollar amount perspective?

Deborah Jordan
Yes, that is correct, Matt; $11 million is what we targeted as cost saves.

Matt Kelley
All right, I was just going to ask what is the dollar amount of cost savings from electing to discontinue HPFC closing the location on Milk Street, and then I think you said there was one other branch, I know you were closing on the Camden side. What is that combined cost save number for those three items?

Deborah Jordan
That will be—I'd have to do the math on those three combined.

Matt Kelley
Okay.

Deborah Jordan
We're targeting the HPFC wind-down in the first quarter. Some of that cost will still continue to be incurred as we support that business line in run-off mode. I'll have to get back you on that, Matt.

Matt Kelley
Okay. No worries. And then second item on the margin, on the 3.21% core margin you have reported this quarter ex-accretion, what would you expect the outlook to be in the current rate environment off of that 3.21%?

Deborah Jordan
Our core margin, as you said, was 3.21%. Our interest rate risk position changed quite a bit for the fourth quarter. As you know in our filings before, we had a rising rate exposure above 5% of our net interest income and now we are almost a neutral position. When we forward look at 2016, we see that core margin coming down slightly but not very much going forward.

Matt Kelley
Okay. Got you, and then on the accretion side, the 9 basis points you had this quarter, how quickly will that rundown? I mean, where will that be by fourth quarter of '16, any thoughts there?

Deborah Jordan
We estimate about 7 basis points coming from accretion for next year, for 2016.

Matt Kelley
Okay. Got it and last question on the securities portfolio, should we expect that to stay about the same level at $850 million or is that going to come down as you remix further?

Deborah Jordan
Yes. Our target has been 23% to 25% of total assets, and we're at 23% right now. As we grow total assets, we envision keeping that pretty consistent percentage of total assets going forward.

Matt Kelley
Okay. Thank you very much.

Deborah Jordan
Thanks, Matt.

Operator
Again, if you have a question, please press star then one. Our next question comes from Travis Lan of KBW. Please go ahead.

Travis Lan
Thanks. Good morning, everyone.

Greg Dufour
Good morning.

Travis Lan
If we think about the outlook for loan growth with the benefits of SBM included, you put up 6%

organic growth for the year and then 10% in the quarter. Is an outlook for 2016 kind of in between the two? Is that a reasonable expectation or is there anything that would kind to push it one way or the other?

Greg Dufour
Travis, I think your comment is between the two points that I would say that would be correct. The driver of it is two things. One, we just saw a very strong fourth quarter. How to maintain, call it within that range, really reflects our existing lending that we're doing through the legacy franchise. We not only expanded into Southern Maine, but we have a very seasoned, experienced team in the Portland market so there is not a ramp up of lenders, if you will. So that 6% to 10% should be achievable for us from what we see today.

Travis Lan
Okay. Good. That is helpful. On the provision, or, I guess, the outlook for the reserve, would you expect to be building reserve to loans going forward as kind of the acquired SBM loans runoff and are replaced with newly originated loans? How do you think about just the outlook for the reserve to loan ratio?

Deborah Jordan
When we look at the provision for 2016, we built it based on estimated charge-offs and then ramping up with the growth that we anticipate on the loan side, and so I would anticipate to start seeing that reserve increase for 2016.

Travis Lan
Okay. All right, that's helpful. And then the outlook for mortgage banking, will you kind of extend the SBM mortgage banking model across your legacy footprint as well? What do you kind of think about the potential momentum on the mortgage banking side?

Greg Dufour
The momentum is strong, not only from the origination side of it, which obviously SBM invested quite a bit in it. We have a very seasoned staff on the origination side. The real benefit of it will be as we take, the more sophisticated approach that SBM gets including their secondary sales process, that's what is going to be leveraged through our legacy areas through, not only originations within that legacy franchise, but also through the branch network.

Travis Lan
Okay. That's helpful. Then last one is just if you have a comment on deposit pricing pressure in the markets. If you have seen any kind of impact from Fed fund hike or if there is any kind of promotional pricing going on in the market?

Greg Dufour
It has been spotty so far, Travis. There is always pressure to increase deposit rates. What we're seeing is, it's competitive, but there's not at least a, a group of competitors that are kind of breaking out of the pack right now. Things seem to have settled down, especially after the Fed rate hike. How we do expect to grow deposits is really through the new product set that we rolled out, Promise Rewards, on the checking side post-merger and that was one of those things that we did in addition to acquiring an institution, we put out an all new consumer product set for us, and we also expect to see some return on our investments in treasury management services to help that growth there.

Travis Lan

Great. Okay. Thank you all very much.

Deborah Jordan
Thanks, Travis.

Operator
Our next question is a follow-up from Matt Kelley of Piper Jaffray. Please go ahead.

Matt Kelley
Just a quick one, I think you had said that the total deal charges is going to be 5% higher, so that would put it at $16 million, is that correct?

Deborah Jordan
Yes. Just under $16 million.

Matt Kelley
Okay. And so the remaining $7 million, will that occur in Q1 or is that spread over Q1 and Q2 or how should we expect that to play out?

Deborah Jordan
That total $16 million was actually recorded in several places. Some of it was recorded on SBM books before the opening balance sheet occurred. Some of it hit equity, some of it hit Camden National's P&L, so all that you'll see in the future is $600,000 that we expect in 2016.

Matt Kelley
Okay, so just $600,000 in Q1 I assume then?

Deborah Jordan
Yes.

Matt Kelley
Got it. Then on a core earnings basis, in the fourth quarter, if you just back out the $9 million charge, you're about $23 million. For the first quarter, will it be flat, up or down compared to that level?

Greg Dufour
Typically, we see a lot of—we're pausing, because we really, as you know, Matt, we don't get into specific estimates for the quarter, but I think what you do is if you probably go back and see the seasonality that we see by quarter, you'll see some impact and that can probably help you in your estimates or anybody in their estimates of what the first quarter will look like.

Matt Kelley
Sure.

Greg Dufour
I don't believe that the bringing in SBM would really change that seasonality that we've seen in the past.

Matt Kelley
Okay. I guess, another way to look at it is, that 58% efficiency ratio target, that's the full year. Correct?

Deborah Jordan
That is correct.

Matt Kelley
Full year 2016? Okay.

Greg Dufour
Yes. That is correct.

Matt Kelley
Okay. Thank you very much.

Greg Dufour
You're welcome.

Deborah Jordan
Thanks, Matt.

Operator
Again, if you have a question, please press star then one.

As we have no further questions, this concludes our question and answer session. I would like to turn the conference back over to Greg Dufour for any closing remarks.

CONCLUSION

Greg Dufour
Great. Well, thank you. First of all, I want to thank everybody for their interest and taking the time to sign on to the conference call. Needless to say, we've had a great quarter and a great year achieving really a transformation of the organization that really gives us the critical mass not only for 2016, but also beyond that. We're very excited about the future of the organization and we appreciate all your support.

Operator
The conference has now concluded. Thank you for attending today's presentation. You may now disconnect your line. Have a great day.