CHEMICAL BANK - MI

Moderator: Michelle Pilaske
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Operator: Good day and welcome to the Chemical Financial Corporation's Earnings Call. Today's conference is being recorded. At this time I'd like to turn the call over to Ms. Michelle Pilaske. Please go ahead.

Michelle Pilaske: Thank you very much. As a reminder, a copy of today's earnings release can be accessed by logging on to Chemical Bank dot com, and selecting the Investor Info tab at the top of the Web site. We've also included a slide presentation on our Investor Info page, with supplemental information that will be referenced in today's call.

With me today are David Ramaker, CEO and President of Chemical Financial Corporation; and Dennis Klaeser, Executive Vice President and Chief Financial Officer. After brief comments from management, we'll open the call to your questions.

Before we begin, I'd like to caution listeners that this conference call may contain forward-looking statements about Chemical, its businesses, strategies, and prospects.

Please refer to our forward-looking statements disclaimer and the other information on Pages 2 through 4 of the slide presentation, for a description of risks and uncertainties that could cause actual results to differ materially from those reflected in forward-looking statements. And now I'd like to turn the call over to David Ramaker.

David Ramaker: Thanks, Michelle, and good morning, everyone. Thank you for joining us on today's call. As you can see on Slides 5 and 6, and in alignment with my remarks in our earnings release, our fourth quarter financial results, after adjusting for significant items, reflect both a solid finish to a milestone year, and a strong base from which Chemical Financial Corporation will move forward.

Let me address the solid finish. In the fourth quarter, from an operational perspective, the key achievement was completion of the integration of Talmer Bank into Chemical Bank, our fourth successful integration over the past two years.

Given the size and complexity, I feel that the Talmer integration has gone extremely well. Notwithstanding the considerable amount of time and effort dedicated to bringing our two organizations into alignment, our team of customer-focused bankers did not miss a beat.

Continued stable economic conditions in our core markets facilitated significant organic loan growth during the quarter. And we believe we have an attractive pipeline as we look forward to 2017. Asset quality remains high.

Admittedly, there is a great deal of noise in this quarter's income numbers. Our reported GAAP net income in 2016's fourth quarter was $47.2 million, or 66 cents per diluted share, compared to 2016 third quarter net income of $11.5 million, or 23 cents per diluted share; and 2015 fourth quarter net income of $25.5 million, or 66 cents per diluted share.

After excluding transaction expenses and other significant items, which are delineated in the press release and detailed in the appendices to this presentation, net income for the fourth quarter of 2016 was $49.9 million, or 70 cents per share, compared to $37.4 million, or 75 cents per diluted share; and $26.9 million, or 70 cents per diluted share, in the third quarter of 2016 and the fourth quarter of 2015, respectively.

At the year end, our total assets were roughly $17.4 billion, and our total loans were approaching $13 billion. Dennis will provide a more thorough review of our financial results in just a moment.

To put this in the larger context of strategic growth, since year-end 2014 we have more than doubled our asset base, expanded our delivery network -- the 249 locations concentrated in Michigan, northeast Ohio, and northern Indiana -- and increased our team of highly qualified customer-focused Chemical bankers to more than 3400 strong.

We have paired a targeted, acquisitive growth strategy with attractive organic growth across the Chemical franchise to achieve these results, never losing sight of our primary goal of creating experiences that are relationship-focused, with individualized solutions, and rapid local response -- all hallmarks of a community bank.

I'll comment a bit more on our general outlook at the end of the call, but I do want to mention that while I believe we are very well-positioned as we move forward, there are obviously some areas of uncertainty on the horizon as we transition from the current economic conditions and a low interest rate environment, into the future.

Obviously our focus will be to continue to build on our momentum of growth over the long term, while realizing ongoing synergies as a result of the Talmer merger.

In anticipation of the question, I will note that we are on track to achieve the $52 million of cost saves identified when we announced the Talmer merger one year ago. With incremental savings yet to be realized in 2017, we expect to push our efficiency ratio into the low 50s by the year-end 2017. With that, I'll turn it over to Dennis to walk through the financial highlights. Dennis?

Dennis Klaeser: Thank you, David. Moving on to Slide 7, you can see that net income has nearly doubled compared to a year ago, the year-ago quarter, and more than tripled compared to the fourth quarter of 2014. Clearly the company has achieved sustained growth through a combined impact of acquisitions and strong organic growth.

Diluted earnings per share, excluding transaction expenses and other significant items, were 70 cents per diluted share in the fourth quarter, down from 75 cents in the third quarter and 70 cents in the fourth quarter of 2015.

Comparisons to the prior quarter are difficult, given that the Talmer merger closed in the middle of the third quarter. But the primary reasons for the decrease from the third quarter are due to seasonally lower mortgage banking revenue in the fourth quarter, a slight decrease in the net interest margin, and an unusually low tax rate in the third quarter of 2016.

The year-over-year comparison’s impacted by the fact that the net interest margin was 8 basis points wider one year ago, and the provision expense was proportionately higher in the fourth quarter of 2016, given our very strong organic loan growth.

As shown on the top of Slide 8, year over year our total loan portfolio has grown by $5.7 billion, to just under $13 billion at year-end 2016. The overall composition of our loan portfolio has remained relatively similar year over year, with about 58% of our loans to commercial borrowers, and 42% to consumer borrowers.

Turning to Slide 9, we achieved $275 million of loan growth in the fourth quarter, reflecting a full quarter benefit from the merger with Talmer. The $275 million loan growth in the fourth quarter is an annualized loan growth rate of 8.7%.

We feel very good about this pace of growth, given that fourth quarter is usually a seasonally slower growth quarter, and given all the distractions during the quarter as we worked through all of our major technology and process integrations associated with the consolidation of Talmer and Chemical.

Since we are getting a fair number of questions about the specific sources of our organic loan growth, we added a new slide, Slide 10, on the net impact of loan growth in the originated loan portfolio, versus the acquired loan portfolios.

From this slide you can see that our $275 million of net loan growth for the quarter is a result of $702 million of growth in our originated loan portfolio, offset by $427 million run-off in the acquired loan portfolios. This information is helpful for analysts and investors to understand why our fourth quarter 2016 loan loss provision of $6.3 million seems relatively high given our overall net loan growth of $275 million.

For analysts and investors who understand the technical accounting issues, they know that for most banks when loans run off the balance sheet, the income statement gets an immediate benefit from the release of loan loss reserves that are associated with those loans.

However for Chemical, since we account for all of our acquired loans under the accounting convention ASC 310-30, run off of the acquired loans does not result in an immediate benefit to our loan loss provision, but rather is only realized over the longer period of time through a likely modest benefit to our net interest margin.

Moving on to deposits as you can see in Slide 11, overall organic deposit growth was relatively muted in 2016. However, this muted overall growth hides significant progress in that during the quarter we increased customer deposits by roughly $463 million by letting $385 million in broker deposits run off our balance sheet. At year end, broker deposits had fallen to just $226 million.

Our average cost of deposits during the fourth quarter of this year increased modestly to 27 basis points, up from 24 basis points in the prior quarter, with most of this growth due to the inclusion of Talmer deposits for the full quarter.

Looking at overall funding on Slide 12, largely due to the increase in the cost of wholesale borrowings, our average cost of funds has increased 8 basis points during the fourth quarter to 33 basis points, from 25 basis points in the third quarter.

Again, most all this increase is due to the impact of the Talmer merger for the ((inaudible)) in the numbers for the full quarter, and due to the fact that purchase accounting impacts have reduced the impact of Talmer's wholesale borrowing cost in the third quarter. As David mentioned, asset quality remains very high.

Turning to Slide 13, net losses in the fourth quarter of 2016 were in line with the second and third quarters of the year, despite the substantial growth in the originated loan portfolios for those periods of time.

While $6.3 million of loan loss provision seems relatively high for the quarter, please note that the provision expense is driven by the strong $702 million in growth in the originated loan portfolio during the fourth quarter, without there being any provision expense offset from the run-off of our acquired loan portfolios.

Our ratio of non-performing loans to total loans was a low 34 basis points at year end, fairly close to where it was in the prior quarter, and a very substantial improvement from 86 basis points at year end 2015.

As shown on Slide 14, a full quarter of Talmer results helped drive net interest income to $132.4 million in the fourth quarter, up from $96.8 million in the third quarter. The net interest margin, on a tax equivalent basis, was 3.56% in the fourth quarter, down from 3.58% in the third quarter, and from 3.64% in the fourth quarter of 2015.

Excluding purchase accounting accretion, the net interest margin declined by about 4 basis points quarter over quarter, again mostly due to the impact of the purchase accounting effect of the Talmer wholesale borrowings. On a truly core basis, my view is that our margin was relatively stable quarter over quarter.

Moving on to non-interest income on Slide 15, driven by the inclusion of Talmer for the full quarter and by $13.7 million of significant items, non-interest income jumped to $54.3 million in the fourth quarter of 2016. This equates to $40.6 million, excluding significant items in the fourth quarter, up from $29 million before significant items in the third quarter.

While hard to make quarter-over-quarter comparisons, given that Talmer was only included for one month in the third quarter, our core mortgage banking revenue was down given seasonality, and our deposit fee income was lower given the temporary impact of the technology and systems integration that occurred during the fourth quarter.

As seen on Slide 16, operating expenses, excluding transaction expenses, grew to $96.3 million in the fourth quarter of 2016, which suggest a current annualized operating expense run rate of about $385 million.

I should point out that when we announced the Talmer merger one year ago, the consolidated estimated 2017 operating expenses was about $433 million, which is about $48 million more than our current annualized operating expense run rate of about $385 million.

With some incremental savings yet to come out of our quarterly expense run rate, we should be able to achieve the $52 million of targeted expense saves that David mentioned in his introductory remarks.

Our adjusted efficiency ratio, which excludes transaction expenses and other significant items, was 53.7% in the fourth quarter, compared to 52.6% in the third quarter, and 55.8% in the fourth quarter of 2015.

As we look forward to 2017, our goal is to drive our efficiency ratio to the lower 50% range due to the combined impact of revenue growth, further merger efficiencies gains, offset by prudent investment in our infrastructure to position us for sustained growth over the longer term.

Turning to Slide 17, we ended the year with tangible book value of $20.20, which represents 7.5% growth in our tangible book value compared to year end 2015. I think this is an impressive amount of growth in our tangible book value, given that the corporation paid $1.06 of dividends, and absorbed the modestly diluted impact of the Talmer merger.

Our TCE to total assets ratio remains very strong at 8.8% at year end. And our regulatory capital ratios are strong at an estimated 10.7% for the Tier 1 capital ratio, and 11.5% for our total risk based capital ratio. Okay, with that I will turn it back to David for some closing remarks.

David Ramaker: Thank you, Dennis. Let me close with a brief comment on some larger macro factors that may impact our business as we move forward in 2017 and beyond. Once again there is a broader market expectation that the Fed will act to increase interest rates gradually over the course of the year, which may create a softening in mortgage originations.

On the other hand, we believe many of our business customers to remain cautiously optimistic over the intermediate term, which should tilt positively for continued commercial loan growth in 2017.

With last week's Inauguration, we have a new Administration. And while expectations for near-term changes are elevated, the timing of and the extent to which these changes -- if and when actually passed -- will impact either the banking industry or our core markets, is uncertain.

Notwithstanding these concerns, we continue to execute on our strategy of being the community bank of choice in the Midwest markets we serve. We believe that our combination of market focus, balance sheet strength, talent, and convenience provide the compelling choice to consumers and businesses alike.

Our strong organic growth, as well as our solid financial performance, is suggestive not only of the attractiveness of our strategy, but also of our team's ability to execute.

We can't control the macroeconomic environment. However, we believe that the key to translating our organic and acquisitive growth into shareholder value is to remain focused on the things that we can control.

Three key ingredients will drive future earnings success: revenue growth, cost discipline and realization of the remaining estimated cost saves associated with the Talmer acquisition. As always, we appreciate your time and interest in Chemical Financial Corporation.

On that note, (Ryan), let's open up the call for questions.

Operator: Thank you. If you'd like to signal for a question, please press Star 1. And we'll pause for a moment to allow everyone an opportunity to signal.

And once again, as a reminder, that's Start 1 to signal.

We'll go first to Scott Siefers with Sandler O'Neill and Partners.

Scott Siefers: Good morning, guys.

David Ramaker: Morning, Scott.

Scott Siefers: Let's see. Dennis, maybe the first question is for you. So I guess hopefully the fourth quarter was sort of the last one with noise in the margin as we got the Talmer funding kind of baked in there.

Do you think, you know, if we're at sort of a steady pure margin, do you think that can sort of hold firm here as we continue to move forward?

And then sort of segueing from that, what's your sense for the value of the benefit from the December rate hike that we could expect going forward?

Dennis Klaeser: Yes, so if you look at the margin excluding the benefit from purchase accounting, we're at 342. And you're right, we've sort of shaken out the impact of the - having Talmer in for the full quarter.

I think that 342 baseline number is - should be a stable number and there should be a little bit upward movement to that. And I think I saw a little bit of that as we progressed through the fourth quarter.

The benefit of purchase accounting at 14 basis points was a little bit higher than what I had originally expected and that has to do exclusively with improvement in expected cash flows of the acquisitions that Chemical did prior to the acquisition of Talmer where those portfolios have been performing quite well.

So I think, you know, with the Fed move and with the additional Fed moves expected later this year, that should help with making a stable margin, if not maybe having a little positive bias, upward bias to the margin.

Scott Siefers: Okay, perfect. And then maybe switching gears just a little, so on the credit cost side you have pretty good clarity on what drove the higher provision this quarter, meaning just very strong organic growth and not necessarily a ton of benefit from some of the loans - some of the acquired loans running off.

Was - that all will continue though, I imagine, right? So as long as the loan pipeline is pretty strong, is it reasonable to expect that we're going to be in sort of a kind of, you know, $5, 6 million per quarter provision? Or how would you have us think about that dynamic?

Dennis Klaeser: You know, I think you should think of it in that range now. Occasionally that's benefit from recoveries of previous charge-offs and we hope those things occur with this continuing great healthy economy.

But yes, that's the good news dragged to our earnings momentum here with the short term because we do have the situation where, you know, of our $13 billion, you know, loan portfolio, $5-plus billion is acquired. And we're going to be very cautious about managing that off-balance sheet reserve and that - for that loan portfolio.

And just the accounting is that even if there's a release of that effective reserve, that release basically trickles in over the remaining life of the portfolio.

So I think when you look at that benefit of purchase accounting, I think you should look at it in that context that in effect that is what - for the normal bank that is an offset that runs through the release of the provision expense but for us, it's an offset that runs through the margin over a period of time.

Scott Siefers: Yes, okay. That's great. Thank you.

Operator: And we'll go next to Terry McEvoy with Stephens.

Terry McEvoy: Hi, good morning.

David Ramaker: Good morning, Terry.

Terry McEvoy: Just circling back to slide ten again and follow-up on Scott's question. The acquired portfolio that's running off, how much of that has been moved or was moved into the originated portfolio?

And I'm trying to think about the loss net interest income if all of that leads relative to then booking new loan and the benefits of those new loans going forward.

Dennis Klaeser: Sure. So little, if any, would have flown into the originated portfolio.

The way the purchase accounting works is that once you're accounting - accounted for as a purchase loan given our accounting convention, it has to be a fairly material re-underwriting of the loan, a change in the loan terms, for it to flow out of the acquired bucket into the originated bucket.

So there’s very little of that that’s feeding into the originated portfolio so most of that payoff is true principal paydowns or a loan being paid off. If a loan is being refinanced, it is likely staying within that acquired bucket.

What I saw in the fourth quarter is that the pre-payment speed within the Talmer portfolio seemed a bit higher than what I had estimated. It was roughly an annualized rate of around 30%. The legacy acquisitions were more in the low-20% range.

And so with rates the way they’ve moved, I think what happened is that we spiked up a little bit in terms of pre-payment speeds with for example CRE loans and residential loans. And my hope is that as we move into 2017 that overall pre-payment rate of those acquired loan portfolios will slow down.

And any slowdown within that pre-payment rate obviously has a very positive benefit to the overall net growth of the loan portfolio.

David Ramaker: Yes, Terry, I would agree with Dennis’ comments. I mean, one of the strategies obviously for us in 2017 is truly working to manage that runoff and reduce the speed of that runoff. So it is a focus of ours and something that we’re working to capture and make sure that we’re managing appropriately.

Terry McEvoy: Thank you. And then as a follow-up, in the prepared remarks, (Dave), I thought I heard you say “incremental cost saves in 2017” to get to that low 50% efficiency ratio. I just want to make sure I understood you correctly. Those incremental meaning above and beyond what had been identified with the Talmer transaction? And if so, where are those coming from?

And then just on the expense side, is the full run rate of crossing $10 billion, is that in the current expense rate today that we just saw for 4Q?

David Ramaker: Well, I think that incremental is, yes, we - first of all, we still have, as Dennis indicated, there are still some synergies to wring out in the fourth quarter - or excuse me, in the first quarter.

But there is an emphasis on our part to continue to look at how we can better efficiently manage the - especially the back rooms of our - in the shops. And so I think from that perspective it's a focus for us to continue to make improvements in those areas and help to drive that number down. As it relates to the...

Dennis Klaeser: Terry, just another comment on that is obviously you likely have a very good revenue projection for the company given the growth trends that we've guided to and that you're assuming so you can, you know, back into sort of what a low 50% efficiency ratio means in terms of annual operating expenses.

So the incremental expense saves is looking at that quarterly operating expense run rate of $96 million that we currently have. We hope to pull that down a little bit farther.

In the first quarter obviously there's a normal expense build that you have with, you know, annual salary increases, higher seasonality in terms of payroll taxes and things like that, so you won't see much, if any, stepdown in the first quarter because of that offset build of expenses that naturally occurs in the first quarter.

But then as we move into the latter part of the year we hope to have that quarterly run rate step down a bit. Of course, there's a lot of moving parts there because, you know, long term we want to not - we're going to be focused on opportunities to build our foundation, to hire additional bankers, to exploit longer-term growth opportunities. So that's not going to be the key, you know, driver.

The key driver for us is sustaining the longer-term growth of the company. But we do feel pretty confident that based on our outlook that that efficiency ratio could be managed down to the lower 50% range.

Terry McEvoy: Thanks, guys.

Operator: And we'll go next to Andy Stapp with Hilliard Lyons.

Andy Stapp: Good morning.

David Ramaker: Good morning, Andy.

Dennis Klaeser: Morning.

Andy Stapp: I had little technical difficulties with the call earlier but - so excuse me if I'm redundant with a question. But is the loan loss provision a good starting point with future provisioning being pretty much a function of loan growth and net charge-offs?

Dennis Klaeser: Yes, I think you're looking at a reasonable run rate there and if you're assuming 700-plus million of growth of the originated loan portfolio. We do expect that overall net growth of the loan portfolio over the course of '17 is going to be in that high single-digit range, similar to the guidance that we've given before.

Andy Stapp: Okay.

Dennis Klaeser: And again, if the pace of runoff of the acquired loan portfolio slows a little bit, the - and - so there is a chance that we achieve, you know, higher levels of loan growth just because of the pace of runoff slows down a little bit.

Andy Stapp: Okay. And what was the gain-up on sale component of mortgage banking in Q4?

Dennis Klaeser: You know, I don't have that particular number. So yes, I imagine 6.3 is the mortgage servicing, right, but I don't have that breakout for you right now. The margin came down a little bit between third and fourth quarter. And our production volume, you know, was seasonally down in the fourth quarter.

However, our pipelines look pretty good despite the tick up in interest rates. We're feeling pretty good about how the pipelines are looking as we go into the year here.

Andy Stapp: Okay. And I know these items tend to be lumpy but were there any unusual items impacting other non-interest income and other non-interest expense? Or do Q4 results represent pretty good run rates?

Dennis Klaeser: You're right, these items are sometimes difficult to predict and there's a variety of moving parts there.

The other non-interest income that you note is just under $8 million. That is benefitting from credit recoveries from some of the Talmer loan portfolios that had previously been fully charged off.

We hope those - that level sustains itself for quite a while though that might be a little higher than the normal run rate. But other than that, I think it's pretty consistent with where I see normalized run rates.

Andy Stapp: And the same thing for non-interest - their non-interest expense?

Dennis Klaeser: Yes.

Andy Stapp: Okay. I'll back into the queue. Thanks.

Dennis Klaeser: Sure.

Operator: And we'll go next to Chris McGratty with KBW.

David Ramaker: Morning, Chris.

Chris McGratty: Hey, good morning. Thanks for taking the question. Maybe just starting with a modeling question, Dennis. The effective tax rate, obviously you've had some noise with one-time charges but as we look into '17 and '18, can you help us with the effective tax rate we should be getting?

Dennis Klaeser: Sure. So the effective tax rate going forward is going to be a little more volatile because of the change in accounting convention related to options and restrictive stocks.

So as those things vest and our options are exercised, we now get an immediate tax benefit that runs through the income tax line item. The former accounting convention was that just affected - went directly to equity.

So because we have a fair bit of options outstanding, we could have periods where we - the effective tax rate, you know, drops significantly based on that benefit that we get.

But in a normalized quarter, given sort of the mix of taxable revenues that we have and non-taxable revenues -- primarily from municipal bonds and municipal lending business -- the normalized tax rate for us should be, you know, around 30%, maybe a little less than 30%.

Chris McGratty: Okay, that's helpful. Maybe a question (David), on capital. Obviously your capital rates all look good. You spoke to a pretty good organic growth outlook. I think in the past you've talked about, you know, using the first half of the year to integrate into - to get the cultures aligned.

But can you help us with how you're thinking about capital planning, either, you know, a pre-emptive capital raise like you've done in the past and kind of M&A aspirations, you know, in the back half of the year?

David Ramaker: Well, there are a couple of hidden questions in there too, Chris, as I hear it.

But obviously we think our capital levels are more than sufficient to sustain the growth in the portfolio or the growth of the company. Obviously the income that will be generated will help assist that growth.

Now if we see significantly more increases in the growth of the portfolios, we may need to go out and augment our capital. But as it sits today, and I'll -- you know, you're pretty consistent in asking me the question about when we're going to get back in the game -- our focus is truly on those management controls or risk management controls that we need to implement and further enhance and quite frankly push into our (defast) modeling and monitoring and I would be extremely surprised if we - if from our regulatory standpoint whether we would need to have that (defast) program at least producing some initial results before I think that the regulators would be allowing us to move forward on that front.

So I think it's well into the year at this point in time because we need to build out all of those systems.

Chris McGratty: That's helpful, thanks a lot. Just a final one Dennis for you, with the earning assets, can you help us with the investment portfolio strategy? It's around a $1.9 billion and you've got a few hundred million of cash. How should we be thinking about those trends over the course of the year?

Dennis Klaeser: Yes, with the rate environment that we expect we do see a modest build in that securities portfolio. It's going to grow much more slowly than the loan portfolio but we could see the securities portfolio growing $150 million or so depending on the pace of growth in the overall interest rate environment and depending on overall liquidity position.

So the proportionate size of the securities portfolio we would not want to drop much further than its current proportion size in the balance sheet.

Chris McGratty: Okay, it's helpful. And the last one, do you have the mix of mortgage origination volume purchases ((inaudible))?

Male: No, I did not pull that stat for you. Sorry about that, I don't have that.

Chris McGratty: That's okay, we can follow up, that's great. Thanks for taking the question.

Operator: We'll go next to (Scott Beard) with ((inaudible)).

(Scott Beard): Good morning guys.

(Crosstalk)

Male: Morning.

(Scott Beard): So two quick questions, first off, I guess on period end deposits were down about $400 million quarter-over-quarter. I was curious, do you know what the amount was that was driven by the branch sale?

Male: Sure, zero. It's - so it's a very interesting question, and I'm glad you brought it up. The - in the branch sale, sorry, we did lose about $200 million of deposits in Chicago, sorry about $100 million of deposits in Chicago and about $70 million in Las Vegas but organic growth within the Michigan franchise and Northern Ohio franchise rebuilt that very quickly. So, we didn't miss a beat with the loss of those deposits. When you do look at our deposits there was about $400 million of shrinkage quarter for quarter and that's driven by two components, $250 million of that is driven by our basically running off a bit higher costing broker deposits. We ran off about a $250 million of broker deposits and those are basically rolled into (FHLB) borrowings. In the current environment (FHLB) borrowings are about ten basis points or so cheaper at all points in the yield curve versus broker. So it just made rational sense for us to run out those brokers and roll them into (FHLB).

The other thing that happens with Chemical is that there's a fair bit of seasonality in its deposits from municipalities, municipalities typically build deposits in the first and third quarters of the year and then they use those deposits in the fourth and the second quarters of the year and with particularly significant seasonality around the third and fourth quarter.

So, there was about $200 million worth of municipal deposits that flowed out of our deposit base in the first, in the fourth, quarter. And basically those $200 million of deposits were substituted with a little bit higher costing (FHLB) advances and that's going to reverse course when we go into the first quarter, the municipals rebuild again and will let the (FHLB)'s run off.

So the loan and deposit ratio as of year-end is around 100%. It's a little higher than our normal targeted level but we're very comfortable with it because we know it's going to move back down to the mid to high 90% range as we go into the first quarter.

(Scott Beard): Right, okay. So that's very helpful and answered of my following questions I had kind of in this area. So I guess if we're looking at it then, you're looking at - if you add up those items and what was the seasonal outflows in the public funds, you know, the transfer into (FHLB) borrowings as well as what went out in the branch sales, the organic kind of run rate there, your quarter run rate, was something in the neighborhood of plus $220 million, does that sound about right in terms of adding deposits?

Male: I think you've got it just right, maybe a little bit higher than that but in that neighborhood, yes.

(Scott Beard): Okay, thanks, that's very helpful. Secondly, I was looking at on the fee income side, you know, I know that there's difficulties in some of the timing from when the merger closed last quarter, but in other fee income, it looks like you were up to right around just under $8 million where it was $2.5 million in the previous quarter. I was just wondering, you know, the delta was about $5 million there and change. If there was anything specific relative to the fourth quarter that was driving that?

Male: Yes, so, looking back over time, yes, $2.7 million in the third quarter but when you look back to the second quarter when it was just Chemical without ((inaudible)) it was only $700,000 and Chemical historically had been in that range, $700,000, $600,000. So in the third quarter we benefited very significantly in the month of September alone with the Talmer merger and what Talmer has is a steady flow of recoveries from previously charged off loans if you think of the history of Talmer it required a variety of banks that had various charge-offs of loans going back over time and it's a large pool of loans that provide a steady opportunity for additional recoveries.

So, that's a key driver just plus we're adding in various other components of ((inaudible)) other income. So in response to an earlier question I said that $7.9 is probably a little bit higher than the normalized run rate but it's a little bit difficult to predict because that's always a number that's a bit - that's a line item that is a bit more volatile because there's a number of different components that are driving it.

(Scott Beard): Sure, thank you. No, that's very helpful. Lastly and then I'll hop out, just real quick, are you expecting any material merger expenses or are we about wrapped up there with what we saw in the first quarter?

Male: The $18 million that we had in the fourth quarter was a little higher than I had predicted admittedly. We do expect a little bit more in the first quarter but it's going to be, you know, definitely in the lower to mid-single digit range as, you know, in the first quarter and maybe just a little bit of spill over into the second quarter.

(Scott Beard): Okay, thank you. Appreciate it.

Operator: And we do have a follow-up question from Scott Siefers with Sandler O'Neill & Partners.

Scott Siefers: Hi guys, just one sort of ticky-tack question just on the $52 million of cost saves and I apologize if I missed this earlier in the call but did you guys say specifically where you are as it relates to the $52 million total (annualized)?

Male: You know, it's hard to sort of exactly segregate where we are because of this flow of normal expense bills versus the pace of cost saves but we're well into that $52 million. There's two things yet that are hard for you to sort of see; one is that in the mortgage banking area we are in-sourcing the servicing of Talmer's $5 billion mortgage servicing portfolio and that occurred late in November. So previously we had been paying a firm called ((inaudible)), a firm based in Chicago approximately $5 million or a little less than $5 million annually to service that portfolio for us and we've now moved that servicing entirely in-house, we need to add some additional staff in our loan operations area to handle that but the - that expense currently is an expense that offsets the revenue in mortgage banking so $5 million on an annualized basis.

So starting in the first quarter we'll no longer have that expense drag offsetting that mortgage banking revenue. And then we have frankly a few million worth of additional cost saves that are hitting in the first quarter as we now are getting a full quarters benefit from the (FPE) reductions that we had in the fourth quarter and we're getting additional benefit from reduced core operating expenses, fully benefiting our first quarter but some of those benefits are being offset by the (national) expense (bill) with salary increases and seasonal payroll taxes and we do have a little bit of headcount (bills) in the first quarter.

So that's why I was saying that on a run rate basis I was expecting it to be relatively flat, maybe down just a little bit in the first quarter, and then stepping down a little bit further in the second quarter.

We also have, for the first three quarters I should note, a bit of unusual high level of drag from these legacy Talmer restricted stock awards because those stock awards the best thing - divesting did not vest upon change of control but rather vested one year after the change of control and so there's a couple million quarterly expense drag that we get from that through August, a couple million quarterly expense drag on a quarterly basis through August of this year and then that dropped away to a very small amount after that.

Scott Siefers: All right, perfect. That's very helpful, thank you for the color.

Male: Sure.

Operator: And we'll go next to David Long with Raymond James.

Male: Morning David.

David Long: Morning guys. I wanted to follow-up with one of the earlier questions I think Terry McEvoy asked it about the acquired loans and Dennis you had said that once somebody acquired loans when they get refinanced will stay in that acquired loan bucket but when they get refinanced do you build the reserve out at that point?

Dennis Klaeser: Good question. No you don't rebuild the reserve however they're in a pool, we're accounting for these loans in pools and there's this off balance sheet credit market in that pool and so there's an assessment of is that off-balance sheet credit mark adequate. So very likely if you refinanced a loan odds are it has fully met your underwriting criteria and it would only need a sort of normalized provision expense so to say 1%.

In one of the presentations in the charts in the earnings release we show that the overall off-balance sheet credit mark for our acquired loan portfolio is 3.1%. So, in that particular example what likely happens is that you have this off balance sheet reserve, on average 3%, the new refinance loan really only requires 1% and so in the re-estimation of cash flows you then take that 2% and you say, we probably don't need that part of the reserve effectively and effectively then that reserve moves into the accreditable bucket and then gets accreted over the remaining life of the entire loan pool. That's a little complicated but I hope you followed my explanation there.

David Long: No, I got it, I got it. Thanks just wanted to make sure that I understood how that would work going forward. And then the other thing that I wanted to ask about was just we've talked a lot about the expense savings and rationalization. On the revenue side you guys hinted at that but are there any numbers that you can put to that or at least talk about and give us some color on what you're seeing or where you may be seeing some revenue synergies?

David Ramaker: Well, I think obviously the first thing is the amount of originated growth so we're truly seeing some significant and good opportunities for much larger loans in the market place and we're starting to, I would say, be a player in those types of credits and we're starting to win some of those and develop those relationships. So from a commercial perspective we're seeing the benefit of bringing the two companies together in the larger in-house limits that we can do.

From a consumer perspective as we've indicated in the past, that might be the easiest thing to start really pushing towards and we've signed up for roughly 13 dealers in Southeast Michigan and another four in Ohio at this point that will start to augment our indirect lending programs from that standpoint.

On the trust side, we're still building out the team. We - Talmer really didn't have a team in Southeast Michigan so we need to really build out that team in order to take advantage of potentially the 401K plans that are out in the marketplace from the customers that we currently already have. So maybe that one is probably going to lag a little bit more than the other two that I just talked about and then I think we are seeing some benefit, Dennis spoke a little bit about the - while we are seasonally down in mortgage originations or taking of applications, we're actually very pleased with that level and so I think on all four fronts we're hitting that pretty well.

David Long: Got it, thank you David.

David Ramaker: Yes.

Operator: And we'll go next to (Andy Stapp) with (Hillary Lyons).

Andy Stapp: Hi guys, my remaining questions were answered. Thanks.

Operator: And we have no further questions in the queue at this time. I would like to turn the conference back over to Mr. David Ramaker for any additional or closing remarks.

David Ramaker: Thank you (Ryan). Again, we appreciate your time and interest in Chemical Financial Corporation. We remain confident in our future prospects and believe we are well positioned to achieve additional competitive and market share gains as we move forward. Thanks and have a great day.

Operator: And that does conclude today's conference, thank you for your participation.

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