Camden National Corporation

Q3 2019 Earnings Conference Call

Tuesday, October 29, 2019, 3:00 PM Eastern

CORPORATE PARTICIPANTS

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

Deborah Jordan – *Executive Vice President, Chief Operating Officer and Chief Financial Officer*

PRESENTATION

Operator
Good day and welcome to the Camden National Corporation's Third Quarter 2019 Earnings Conference Call. My name is Eilee and I will be your operator for today's call. All participants will be in a listen-only mode during today's presentation. Following the presentation, we will be conducting a question-and-answer session. If you require operator assistance at any time during the call, please press "*", then "0."

Please note that this presentation contains forward-looking statements, which involve significant risks and uncertainties that may cause actual results to vary materially from those projected in the forward-looking statements. Additional information concerning factors that could cause actual results to differ materially from those in such forward-looking statements are described in the company's earnings press release, the company's 2018 Annual Report on Form 10-K and other filings with the SEC.

The company does not undertake any obligation to update any forward-looking statements to reflect circumstances or events that occur after the forward-looking statements are made. Any references in today's presentation to non-GAAP financial measures are intended to provide meaningful insights and are reconciled with GAAP in your press release.

Today's presenters are Greg Dufour, President, Chief Executive Officer, and Director; and Deborah Jordan, Executive Vice President, Chief Operating Officer, and Chief Financial Officer. Please also note that this event is being recorded.

At this time, I would like to turn the conference over to Greg Dufour. Please go ahead, sir.

Greg Dufour
Good afternoon and welcome. Earlier today, we released our third quarter 2019 earnings of $14.5 million, which reflected a 3% increase over our third quarter 2018 earnings. Earnings per diluted share reached $0.94 for the quarter, a 4% increase over EPS for the third quarter of 2018.

The performance ratios for the quarter were strong with return on average assets of 1.29%, return on average equity of 12.26% and non-GAAP efficiency ratio of 55.32%. On a year-to-date basis, net income totaled $42 million, 7% increase over the same time period last year, and diluted earnings per share reached $2.70, 8% increase over that same time period.

Last quarter I expressed a caution regarding various pricing strategies we're experiencing in our markets. We still remain cautious regarding the competitive pricing for loans and deposits, as well as, what we're seeing in loan structure. Our focus remains, as it always has been, on the long-term performance of our company.

Over the past several years, we've discussed various strategic efforts we've undertaken, including our focus on deposits, small business lending, and shareholder performance. I'm pleased to share that over the past few months, we've reached several milestones and received recognition for our work in those areas.

Our focus on deposits is confirmed by the June 30, 2019, FDIC Summary of Deposits report, which shows Camden National with 11.4% of deposit market share across Maine, the largest of any Maine-based bank. We've been recognized by both the Finance Authority of Maine and the

Small Business Administration for our business lending programs. We've been named the large financial institution of the year by the Finance Authority of Maine for 2019, the 10th year in a row receiving this recognition. Also this quarter, the Maine district of the Small Business Administration has named Camden National its 2019 SBA District Director award recipient.

Finally, during the quarter, Camden National was named to Sandler O'Neill's Sm-All Stars list for 2019. We're one of 30 publicly traded banks and thrifts out of 400 in our size class, and the only bank headquartered in New England to be recognized. Camden National is thrilled to be selected for the Sandler O'Neill award from amongst the highest performing institutions nationwide. It's a testament to the success of our measured, balanced approach and to the outstanding dedication of our talented employees.

Based on our consistently strong performance and confidence we have in our business going forward, we returned over $31 million of capital to our shareholders through the repurchase of over 400,000 shares of our common stock and paid $14 million of dividends through the first nine months of this year.

Before I turn the discussion over to Debbie, I want to recognize and thank her for 11 years of service to the company. Last Friday, Debbie, announced her intention to retire in April 2020 after 27 years in banking. Her contributions to Camden National are significant and deeply appreciated to say the least.

I'm pleased she will be with us for a transition period. We expect to engage, or we have engaged I should say, a recruiting firm, Russell Reynolds, to assist us in the search for the Chief Financial Officer position, and Debbie's remaining responsibilities will be assessed in the context of the appropriate needs of the organization over the next several weeks.

I'd like to now turn it over to Debbie.

Deborah Jordan
Good afternoon everyone. As Greg mentioned, we are pleased with our third quarter results with net income up 3% over the same period last year, due to strong loan and deposit growth. When comparing results to the previous quarter, net income of $14.5 million increased $1.3 million, or 10% due to revenue growth of 3% combined with lower levels of loan loss provision and operating expenses.

On a linked-quarter basis, revenue increased $1.1 million, primarily due to a nice pickup in mortgage activity which drove an increase in mortgage banking fees of $926,000 between quarters. Our mortgage pipeline at September 30th reached $135 million, which includes a lift from the refinancing activity.

Net interest income grew $350,000 from the previous quarter, with average loan growth of 1% between periods, an average checking balance growth of 5%, primarily due to the seasonality of our customer base. Our net interest margin declined 2 basis points between periods with our asset yield declining 7 basis points and our funding cost decreasing 5 basis points.

The company's average cost of deposits was 0.85% for the third quarter, representing a 1 basis point decline on a linked-quarter basis. Deposit rates on interest checking and savings accounts re-priced lower between periods, whereas rates trended a little higher for money market and certificates of deposit. We anticipate lower rates across all deposit categories in the fourth quarter, both as indexed deposits reprice and through active management of deposit exception pricing.

We experienced modest loan growth during the quarter of $10.3 million, with residential mortgages being up $26.1 million for the quarter, while commercial real estate and commercial loans were down for the quarter by $16.3 million. Year-to-date loans have grown 3%, led by residential mortgages.

Commercial real estate loans are down 1% year-to-date, largely due to elevated prepayments we experienced in the first quarter of this year. Prepayment speeds for the last two quarters have normalized on the commercial real estate side. Although, we continue to review commercial real estate deals, we are being more selective on our appetite for certain transactions. We believe now is the time to maintain what has historically served us well--our strong credit and disciplined pricing culture.

In providing net interest margin expectations for 2020, our objective is to maintain a net interest margin of 3%. To accomplish this, we will continue to be disciplined with our loan and deposit pricing.

Our focus continues to be on profitable growth to drive long-term sustainable shareholder value, which means being more selective for growth opportunities. Although, we experienced a higher level of loan charge-offs in the third quarter, asset quality remains very strong with non-performing assets of $13.5 million, or just 0.30% of total assets at September 30. For the nine-month period, our annual charged-off rate of seven basis points is consistent with the same level as a year ago.

Operating expenses of $23.7 million for the third quarter declined 1% compared to the previous quarter, as we benefited from the FDIC assessment credit on our third quarter fees. Like many other qualifying community banks, we anticipate future FDIC assessment credits in coming quarters, should the depository insurance fund continue to exceed its required ratio.

That concludes our comments on the third quarter results. On a personal note, I want to follow up on my retirement announcement last week. I'm very excited for the next phase of my life. I've been fortunate to work for a great company with great people, and I'm very confident of the company's continued success.

We'll now open the call up for questions. Thank you.

QUESTION AND ANSWER

Operator
We will now begin the question-and-answer session. To ask a question, you may press "*", then "1" on your touchtone phone keypad. If you are using the speakerphone, please pickup your handset before pressing the keys. To withdraw your question please press "*", then "2."

Our first question comes from Damon DelMonte with KBW.

Damon DelMonte
Hi, good afternoon, guys. How is it going today?

Greg Dufour
Good, Damon. How are you?

Damon DelMonte
Good, thanks. Before I ask my question, first off, congrats Debbie on your announcement. I know we'll be talking over the next few months, but I just wanted to officially say congratulations and wish you all the best.

Deborah Jordan
Thanks, Damon.

Damon DelMonte
So, first question I had, if you could talk a little bit about the margin and kind of your expectations for…I know you said, your goal is to keep it above 3% as you go into 2020. But, could you just talk a little bit about the dynamics of re-pricing opportunities on the deposit side and the pressures you're feeling on the asset side?

Deborah Jordan
Sure, I'd be happy to. And we were joking before the call whether I'm really, actually allowed to forecast for next year, since I won't be here. But, I'll take a stab and Greg can jump in. As you know, our deposits are cyclical. We have a high level of seasonality in the last half of the year. And so, we usually have a higher net interest margin on the back half of each year. We did see a slight decline in margin between quarters. And last quarter, I was hoping that we could maintain it. So, we were down two basis points. Part of it is the level of cash that we have on the balance sheet as of September 30, which, in part, relates to our derivatives and how we post cash collateral, and just the deposit inflow that we received.

The fourth quarter, we're working pretty aggressively on deposit exceptions. On the pricing side, we're assuming the Fed funds rate drops again in October. Our goal with pricing is a one-to-two basis point decline in the fourth quarter, really depending on what we can do on the cash side of things. On the loan side, although prepayments slowed down in the third quarter, what we did see is elevation on the residential mortgage side. The CPR really doubled in the second and third quarter compared to the first quarter. So our challenge is we're going to continue to have cash flow come at us, whether it's on the investment or the loan side, getting reinvested at lower rates.

On the funding side, we do have some offset capabilities. We have broker deposits that will be re-pricing shortly, and then continue to manage certificates of deposit on the short end and bringing those rates down, and then managing [deposit] exception pricing further. And then, more importantly, growing checking accounts. We have a strong treasury management function. We've been very successful in attracting business accounts. And to the extent we can continue to have that success, this should also help us with the margin. It's going to be a challenge next year though.

Damon DelMonte
Got it. Yes. Okay. That's helpful. I appreciate the color. And then with regard to expenses, you alluded to the potential of having FDIC assessment credits again next quarter and potentially probably carrying into 2020. How should we think about the overall expense base next quarter with that component of it?

Deborah Jordan
I had provided guidance that I thought for the entire year for 2019 we'd be at $24 million. I still think we'll be at $24 million minus $300,000 [for the FDIC credit] is probably where we'll land for the fourth quarter.

Damon DelMonte
Okay. And then, from a modeling standpoint here, you guys kind of have around what $400,000, $500,000 per quarter in FDIC costs. Is that correct?

Deborah Jordan
Well, we received a credit of $300,000 and so I would build that in.

Damon DelMonte
Just the $300,000, okay.

Deborah Jordan
Yes.

Damon DelMonte
Got it. Okay. And then, a question for Greg, on the loan growth outlook. You kind of reiterated your cautious outlook with the pricing in terms of some of the competition in the marketplace. How do we think about overall loan growth as we go through the last quarter and into 2020?

Greg Dufour
Yes. I typically say that we're in the mid-single-digit range of loan growth. And I would say, probably that, but with a caution of probably on the lower end of that mid-single-digit range. It's purely a risk-reward trade-off. We are seeing some really aggressive pricing. And we want to be cautious on how much fixed-rate assets we put on our books, even though we do have capacity. But at some point we got to make sure we're doing the right thing, which we will do for high-quality credits.

We're seeing some extension in the loan structuring and actually, amortizations are stretching out especially in CRE. Over probably the past eight quarters it's gone from 20-to-25 year amortizations to 25-to-30 years. There are even some rumors they're going above 30 [years]. And that's causing us pause. But it's the block and tackling banking that we got to be focused on. The higher credit quality customers, we have greater flexibility in pricing. For those we take more risk on, we just want to be compensated for that risk.

Damon DelMonte
Got it. Got it. Okay. I'll step off for a second and see if anybody else has a question for now. Thank you.

Operator
Again, if you have a question, please press "*", then "1."

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, again, I want to thank everybody on the call for your interest in Camden National. Just to reinforce, I want to thank Debbie very much. She's been a real trusted adviser and partner, not just to me, but to everybody throughout the company. We're really fortunate that she'll be here until April 2020, so we'll have a smooth transition between now. We will keep you all posted as that progresses. Thank you all very much. Have a great day.

Operator
The conference has now concluded. Thank you for attending today's presentation. You may now disconnect.