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Market Intelligence

Camden National Corporation NasdaqGS:CAC
FQ2 2020 Earnings Call Transcripts

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Call Participants

EXECUTIVES

Gregory A. Dufour
President, CEO & Director

Gregory A. White
Executive VP, CFO and Principal Financial & Accounting Officer

ANALYSTS

Damon Paul DelMonte
Keefe, Bruyette, & Woods, Inc., Research Division

Jacob F. Civiello
Janney Montgomery Scott LLC, Research Division

Presentation

Operator

Good day and welcome to Camden National Corporation Second Quarter 2020 Earnings Conference Call. My name is Kate, and I will be your operator for today's call. All participants will be in listen-only mode during today's presentation.

[Operator Instructions]

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 earning press release, the company's 2019 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 reference in today's presentation to non-GAAP financial measures are intended to provide meaningful insight and are reconciled with GAAP in your press release.

Today's presenters are Greg Dufour, President, Chief Executive Officer; and Greg White, Executive Vice President, Chief Financial Officer.

Please 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.

Gregory A. Dufour
President, CEO & Director

Thank you, Kate, and I want to welcome everyone to Camden National Corporation's earnings conference call for the second quarter. And I hope that you and your loved ones are safe and healthy.

Earlier today, we reported second quarter net income of $10.9 million or 17% below the second quarter 2019 and diluted earnings per share of $0.73 or 14% below the same period last year.

On a year-to-date basis, net income was $24.4 million, 11% below prior year levels, while diluted earnings per share were $1.62 or 8% below the first 6 months of 2019.

On a more positive note, our pretax, preprovision earnings of $23.1 million second quarter 2020 was an increase of $5.4 million over the second quarter of 2019, demonstrating the underlying operations of the company. This performance was driven by higher provision for loan losses, increased revenues from mortgage banking and revenues from our participation in the PPP program.

Our CFO, Greg White, who you met last quarter, will provide additional detail into our performance in a moment, but I'd like to provide some additional insights as well.

Camden National delayed its adoption of CECL as allowed by the CARES Act, so we use the incurred loss model to determine the reported allowance for credit losses and resulting provision expense year-to-date. However, we have run both CECL and the incurred loss model in parallel and have provided additional discussion in our supplemental investor package on what our allowance for credit losses would potentially have been under CECL. We expect to provide even more discussion in our 10-Q.

Greg will also elaborate on this in his comments.

I'd like to switch gears and discuss a few other items before turning the call over to Greg. We are closely monitoring economic conditions nationally, regionally and locally. Maine has taken a stronger stance regarding opening up public places such as restaurants and hotels, which is negatively impacting the tourist season. But at the same time, incidents of new COVID-19 cases are favorable when compared to many other areas of the country. This is stressing our hospitality loan portfolio and retail customers. However, by utilizing the flexibility afforded to us under the CARES Act and regulatory

guidance, our special asset and lending teams have been able to work with impacted customers to provide temporary debt relief while avoiding the ramifications of troubled debt restructuring accounting.

Through June 30, we have seen strong residential mortgage volumes on both the refinance and purchase side. And although commercial demand is down, we've been involved in reviewing several requests. In both cases, we are very cautious from a credit perspective and will continue our strong underwriting standards, which are enhanced by even stronger due diligence requirements.

Camden National is also taking a measured approach in our return to working in our offices. Our retail banking centers are open but are operating under reduced hours. While we have not seen a full month yet of those centers being completely open, we are estimating our second quarter banking traffic is down 20% from last year's levels, while digital banking activity is up 33% and and call center volumes are up almost 69%. Our investments in technology and digital-based products over the past several years have provided us a strong foundation and resource base to adapt to our new environment.

Finally, I want to share that like many of you in other companies, we've watched with sympathy the various events over the past several weeks regarding racial injustice. The Board of Directors and management have reaffirmed to our employees that we do not discriminate nor tolerate discrimination based on race, gender, sexual orientation, religion or any other biases or basis.

We have always taken steps to educate our employees and communities, and we are developing even more opportunities to improve inclusiveness.

As a community bank, we understand and have reaffirmed that one of our most important roles is to ensure we provide banking services and products to all members of our communities.

I'd like to now turn our discussion over to Greg White, our Executive Vice President and Chief Financial Officer.

Gregory A. White
Executive VP, CFO and Principal Financial & Accounting Officer

Thank you, Greg. Good afternoon, everyone. Again, my name is Greg White. I've been the CFO of Camden National a little over 3 months now, and I'm really excited to be a part of this team. With that said, let me just jump into the second quarter results. So despite a $9.4 million provision expense, which I will comment on further in a moment, we had a strong second quarter.

On a pretax, preprovision earnings basis, we were up $4.4 million or 24% on a linked-quarter basis. And as Greg Dufour mentioned, up $5.4 million or 31% compared to the same quarter last year. The growth in our pretax, preprovision earnings was primarily driven by a 9% increase in our net interest income in the second quarter of 2020 compared to both linked and prior year quarters.

Net income was up $2.7 million in the second quarter of 2020 compared to linked quarter and up $3 million compared to the second quarter of 2019.

Net interest margin for the second quarter was up 3 basis points to 3.11% compared to 3.08% in the first quarter due to very effective cost of funds management strategies in this low interest rate environment, which resulted in a 42 basis point decrease in our cost of funds on a linked-quarter basis. Net interest margin for the second quarter of 2020 was flat compared to the prior year quarter at 3.11%. Assuming interest rates stay around the current levels, we do expect our margin to have downward pressure, and we estimate our fourth quarter net interest margin will decline to approximately 3% to 3.05% during the fourth quarter.

Total loans grew by 5% or $168 million during the second quarter of 2020, excluding the $219 million in growth from the PPP loans, our loans were down $51 million or 2% since March 31 of this year.

Total deposits were up 12% or $433 million during the quarter despite our CD book declining by 21% or $114 million as a part of our funds management strategy.

Noninterest-bearing checking was up 33% or $176 million during the quarter. Again, net income for the second quarter of 2020 was down 17% to $10.9 million, and diluted earnings per share was down 14% to $0.73 per share compared to the

same quarter a year ago. That decrease was driven by a provision expense of $9.4 million during the second quarter due to the economic environment created by the pandemic compared to $1.2 million for the second quarter of 2019.

Our return on assets was 90 basis points for the second quarter of 2020, and our return on average tangible common equity was 11.09%.

As mentioned in our first quarter 2020 earnings release, we opted not to implement CECL during the first quarter of this year. Under the terms of the CARES Act, we will now implement CECL during the first -- during the fourth quarter of this year or during the third quarter, if the COVID-19 national emergency is lifted during the third quarter. Under the incurred loss reserve methodology, and as mentioned previously, we recorded a $9.4 million provision expense for the second quarter of 2020, which resulted in a 23 basis point increase in our allowance for loan losses to 1.07% of loans, up from 84 basis points at the end of last quarter.

If we back out PPP loans from our allowance -- our allowance for loan losses stood at 1.14% of loans or on that basis, up 30 basis points during the second quarter compared to the first quarter.

As noted in the earnings release, we implemented CECL -- excuse me, as noted in the earnings release, had we implemented CECL earlier this year, we estimate that as of June 30, our allowance for credit losses would have been between 1.20% and 1.32% of total loans, including the PPP loans. Given relatively stable nonperforming loan numbers on a linked-quarter basis, 0.34% of total loans at June 30 compared to 0.33% of total loans at March 31, our coverage ratio of reserves to nonperforming loans increased to 3.11x at June 30 from 2.57x at March 31. Net charge-offs were 5 basis points of average loans for both the first and second quarters of 2020. We have provided additional information on our deferred loan program on Page 12 of the supplemental deck that we provided with our earnings release, including an update on balances of deferred loans as of July 23.

At June 30, our total deferred loans were 400 -- $547 million or 16% of total loans. And as of July 23, total loan deferments, including $68 million of redeferred loans was $351 million or 11% of total loans. We continue to work with certain customers that have returned back to their original loan terms and may possibly again redefer their loan payments in full or in part. We continue to have a strong capital position, and there is more detail on capital in the supplemental information that was provided with the earnings release.

From a regulatory capital perspective, we remain well above regulatory minimums. Our total risk-based capital ratio increased 75 basis points during the second quarter to 14.56% from 13.81% at the end of the first quarter. And our Tier 1 risk-based capital ratio increased by 45 basis points during the quarter to 13.01% from 12.56% at the end of the first quarter.

Due to balance sheet growth, our tangible common equity did drop a little bit during the quarter. It was at 8.41% as of June 30.

Lastly, I'm happy to report our tangible book value per share was up $0.92 during the second quarter of 2020. It was at $27.31 at the end of the quarter.
That concludes our comments on the second quarter. We'll now open the call up for questions. Thank you.

Question and Answer

Operator

[Operator Instructions] Our first question comes from Damon DelMonte from KBW.

Damon Paul DelMonte
Keefe, Bruyette, & Woods, Inc., Research Division

So my first question, I just wanted to touch on expenses a little bit. They came in down on a linked-quarter basis. And I know you identified a couple of those drivers. Can you just talk a little bit about the go-forward outlook for expenses? And would you expect some of those compensated-related costs to come back into the expense base in the third quarter?

Gregory A. White
Executive VP, CFO and Principal Financial & Accounting Officer

We would think expenses in the third quarter should be similar to the second quarter expenses. Beyond that, it's difficult to predict. But if you had a best guess for the fourth quarter, maybe up slightly. But third quarter, probably similar to second quarter here.

Damon Paul DelMonte
Keefe, Bruyette, & Woods, Inc., Research Division

Got it. Okay. And then with respect to the loan deferrals, you guys may have said this and I missed it, but what are you seeing in the way of kind of that round 2 requests from borrowers to extend another 90 days?

Gregory A. White
Executive VP, CFO and Principal Financial & Accounting Officer

Damon, actually, let me back up on expenses a little bit. The one thing is they're -- total compensation expense might increase slightly. But with that said, it's possible that total expense number is similar to the second quarter. But maybe adding $0.5 million to that number, is probably an appropriate estimate.

Gregory A. Dufour
President, CEO & Director

So on the loan deferrals, Damon, what I would really say what we're seeing is when we originally started doing deferrals, we're just doing it 90-day primarily basis out of the allowable 180. So we're still in the midst of really relooking at that first wave, if you will. And what we're seeing is some borrowers are still looking to get, call it that, another 90 days, some were working with more of a loan modification approach. Some of that's driven not only by what we want to do, but also we're asking our borrowers who do want loan modifications for a lot more information and taking more of a negotiation approach to going beyond that second 90-day tranche. But when they do, they are looking for interest-only relief type of thing. We have returned some to our full-billing status, and we're working with them to make sure that those will remain current and within the loan terms.

Damon Paul DelMonte
Keefe, Bruyette, & Woods, Inc., Research Division

Got it. Okay. And then with regards to your outlook for provision, obviously, a very challenging component of the income statement to forecast. But when you look at the build and the reserve level this quarter, do you feel like this was kind of like step 1 of a process that will continue for the next couple of quarters? Or do you feel, given your underlying strength in your credit, in your portfolio that you're comfortable at this level?

Gregory A. Dufour
President, CEO & Director

I would raise it, Damon. And that's why in the supplemental package, we've addressed what CECL would be. So it kind of makes it a big change because we're alluding to -- in CECL.

On a CECL basis, we gave a range of $40 million to $44 million of what the allowance of credit losses would be compared to the $35.6 million. So just from CECL, we expect that to happen. So it's kind of -- I would say the big change will come from adoption of CECL, and we will play out on how the loan portfolio looks quarter-by-quarter.

Damon Paul DelMonte
Keefe, Bruyette, & Woods, Inc., Research Division

Got it. Okay. And then just my last question. Just -- could you just give us a little update on kind of how the tourism season is going across Southern Maine and other areas of your New England footprint?

Gregory A. Dufour
President, CEO & Director

Yes. Well, obviously, the state, as I mentioned, has taken a very strict approach to reopening. And I think that's allowed good numbers from a COVID-infection perspective. The impact has been to tourism, and it's been very slow. However, in the past few weeks where the government did open up tourism and loosening the quarantine restrictions for residents of some states. We have seen an uptick starting, but that's probably a couple of weeks old. We're seeing some people who are now coming to the summer homes and increasing activity. So it's building up a little more each day, but we are not expecting it to, call it, August of 2020 to be like what August of 2019 will be.

Operator

Our next question is from Jake Civiello from Janney.

Jacob F. Civiello
Janney Montgomery Scott LLC, Research Division

Kind of wanted to start on the investment securities portfolio. So the end-of-period balance was up almost 10% over the first quarter. Can you talk a little bit about the timing, yield and duration of any new securities purchases in the quarter?

Gregory A. White
Executive VP, CFO and Principal Financial & Accounting Officer

Yes. So I mean, that in part is because of the liquidity buildup, investments are certainly earning more than cash and kind of drove the variance there. Originally, the bank had extended duration earlier in this year. Given the possibility of long rates coming down and that is still happening to some extent, the yield is now in kind of that low 1% to 1.5%. But it is not our goal to build investments from here. You could almost look at that as a little bit in lieu of loans short term. We do have a lot of cash flow coming off the investment portfolio over the next 12 months. That's a quick summary.

Gregory A. Dufour
President, CEO & Director

Yes. And if you look at our -- the targeted duration in the quarter is 4 to 6 years. And so that -- in this stage of what we're seeing, that's probably a pretty decent target range that we find palatable. And we're still throwing off $15 million to $20 million of cash flow off the portfolio.

Jacob F. Civiello
Janney Montgomery Scott LLC, Research Division

Okay. That makes sense. And it sounds like the decline in the securities portfolio balances over the course of the next 12 months, we'll kind of coincide with what I would expect your decline in deposit balances would be as PPP kind of deposits are -- forgiveness transpires and they exit the bank? Is that kind of what the thought process is?

Gregory A. Dufour
President, CEO & Director

If it was solely based off PPP, I'd agree with you, Jake, on that. But we are seeing overall depositors, customers maintaining higher balances in all. And I think as you all are well aware, many banks are seeing that as well. So banks are building up liquidity at this point, in the situation that we're in. So we're balancing that out. We'll be looking to hold probably more mortgages, residential mortgage productivity than we potentially have in the past. But those are some of the tools or levers that we can pull going forward.

Jacob F. Civiello
Janney Montgomery Scott LLC, Research Division

Okay. Kind of on that latter topic in terms of mortgage banking revenue. I mean it sounds like you kind of have some confidence in the sustainability of mortgage banking revenue in the second half of the year? Is that -- am I interpreting that correctly?

Gregory A. Dufour
President, CEO & Director

What I would say is we are seeing a big inflow, our pipelines are at record levels from refi and purchase activity. That's driven by all kinds of different factors from low interest rates to refi. We are seeing purchasing activity going on, some from people in more metropolitan areas looking to come to Maine, especially now that they realize they can work remotely from anywhere and they're searching a quality of life, whether that's sustainable, the interest rate environment will be sustainable. However, at some point, everyone's refinanced. How that happens with a mortgage activity? That's all dependent on the real estate market.

Jacob F. Civiello
Janney Montgomery Scott LLC, Research Division

That makes sense. And then if I can, if I could just ask a couple of questions about PPP, what are your total PPP fees that you expect to receive?

Gregory A. White
Executive VP, CFO and Principal Financial & Accounting Officer

That is approximately $7 million.

Jacob F. Civiello
Janney Montgomery Scott LLC, Research Division

Okay. And then of the $226 million in PPP loans that you booked, what percentage do you anticipate would be forgiven? Or I guess another way of asking would be, how much do you anticipate would potentially remain on the books for the full term or, I guess, or at least through 2021?

Gregory A. White
Executive VP, CFO and Principal Financial & Accounting Officer

The short answer is we hope none of them remain on the books, meaning that they are forgiven. But that -- we're probably going to know a lot more over the next 3 months here to be able to answer that better at some point.

Gregory A. Dufour
President, CEO & Director

Yes. A lot of what we've done is, obviously, with Maine, I don't have the percentages. We can get back to you on that on the ones that are below $150,000, and that will be driven by, obviously, whatever is passed in Congress and signed by the President. Obviously, we hope it more is forgiven and easily forgiven that really is better on our, call it, operational throughput.

So that's going to play out over the next few weeks, I guess, and months if they're not on the ones that aren't forgiven. The other thing on the revenue is just to kind of come back and put a fine point on it, we've recognized $7 million of fees. In total, we'll have $8.4 million.

Jacob F. Civiello
Janney Montgomery Scott LLC, Research Division

Got it. Okay. And the margin number that Greg White mentioned for the fourth quarter, was that excluding PPP fees that you're assuming?

Gregory A. White
Executive VP, CFO and Principal Financial & Accounting Officer

There is still a little residual in that range. There is some -- it is not excluding.

Jacob F. Civiello
Janney Montgomery Scott LLC, Research Division

Okay. Okay. And then this is my last question, and I realize this is in the weeds a little bit, so we might have to follow-up at some later date. But do you happen to know what the customer overlap is that receives some level of deferral and then also received a PPP loan?

Gregory A. Dufour
President, CEO & Director

We'd have to get back on that. I don't know that answer.

Operator

[Operator Instructions]

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 closing remarks.

Gregory A. Dufour
President, CEO & Director

Well, first of all, thank you, Kate. Thank you, Damon and Jake, for your questions and all other people that are on the line. Maybe just a message to leave with you is that really this performance, especially when you look at our pretax, preprovision performance, when you look at the sheer amount of work that has been done, whether it's through PPP, loan deferrals, moving customers around from going more digital, our call centers, it's really successful because of our employees here. And I just want to publicly thank all of them. These folks are working major hours, many from their kitchen tables, all -- we're trying to balance kids who don't have school, a day care to go to. We're asking a lot from our employees, and we're really proud of the effort that they've put in, the results that they've driven.

With that, we look forward to continuing the discussion as time goes on. And again, I hope everyone stays safe and healthy. Have a good day.

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