First Quarter 2019 Earnings Call Transcript

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CORPORATE PARTICIPANTS

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Keith Mestrich, *President and Chief Executive Officer*

CONFERENCE CALL PARTICIPANTS

Steven Alexopoulos, *JPMorgan*

Matthew Keating, *Barclays*

Chris O'Connell, *KBW*

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PRESENTATION

Operator:

Greetings, and welcome to the Amalgamated Bank First Quarter 2019 Earnings Call. At this time, all participants are in a listen-only mode. A question-and-answer session will follow the formal presentation. If anyone should require Operator assistance during the conference, please press star, zero on your telephone keypad. As a reminder, this conference is being recorded.

I would now like to turn the conference over to your host, Mr. Drew LaBenne, Chief Financial Officer for Amalgamated Bank. Please go ahead.

Drew LaBenne:

Thank you, Operator, and good morning, everyone. We appreciate your participation today in our first quarter 2019 earnings call. With me today is Keith Mestrich, President and Chief Executive Officer. As a reminder, a telephonic replay of this call will be available on the Investor section of our website for an extended period of time. Additionally, a slide presentation to complement today's discussion is available on the Investor Resource section of our website.

Before we begin, let me remind everyone that this call may contain certain statements that constitute forward-looking statements within the meaning of the Private Securities Litigation Reform Act of 1995. We caution investors that actual results may differ from the expectations indicated or implied by any such forward-looking information or statements. Investors should refer to Slide 2 of our earnings call presentation, as well as our 2018 10-K filed on March 28, 2019, and our other periodic reports that we file from time-to-time with the FDIC, for a list of risk factors that could cause actual results to differ materially from those indicated or implied by such statements.

Additionally, during today's call we will discuss certain non-GAAP measures which we believe are useful in evaluating our performance. The presentation of this additional information should not be considered in isolation, or as a substitute for results prepared in accordance with U.S. GAAP. A reconciliation of these non-GAAP measures to the most comparable GAAP measure can be found in our earnings release as well as on our website.

At this point, I'll turn the call over to Keith.

Keith Mestrich:

Thank you, Drew and good morning, everyone. We appreciate your time and attention today. I'm quite pleased with our first quarter results that they clearly demonstrate the attractive position that Amalgamated Bank holds as we work to service the needs of values based institutions, and further our reputation as America's socially responsible bank. As you will see, the investment thesis that we described at the launch of our IPO in August is generating positive results for the Company.

For the first quarter, we delivered net income of $10.8 million or $0.33 per diluted share, which compares to net income of $16 million or $0.49 per diluted share in the linked quarter, and net income of $7.7 million or $0.27 per diluted share for the first quarter of 2018.

As we have previously stated, core earnings continue to be a better representation of our financial performance, as well as the run rate earnings power of the bank. For the first quarter, core earnings were $10.7 million or $0.33 per diluted share, as compared to $9.7 million or $0.30 per diluted share in the linked quarter, and $7.9 million or $0.28 per diluted share in the first quarter of 2018.

As a reminder, core earnings in the fourth quarter of 2018 excludes a previously disclosed deferred tax realization of $7.6 million, $1.6 million of expenses related to our New Resource acquisition and other more minor onetime adjustments.

Turning to the highlights of the quarter in more detail, I am very pleased with the success that we achieved growing our deposit franchise as we continue to drive organic growth in our core markets of New York City, Washington D.C. and San Francisco. For the quarter, deposits grew by $329 million or 35% annualized when you adjust for the $327 million of short-term deposit from one-trust client, which came on to our balance sheet at year-end 2018, and subsequently exited the bank on January 2, 2019. You may recall that we discussed this deposit anomaly on our fourth quarter call.

Importantly, the strength in our deposit franchise was broad based, as we continue to welcome new relationships from across the many business sectors that we focus on, including unions and their funds, nonprofit, social enterprises and philanthropists. Looking forward, our deposit pipeline remains strong in all three of our regions and across all of our business verticals. Our relationships continues to expand, which drives real deposit growth optimism for the balance of the year.

As Drew will discuss in more detail, our political deposit growth was also a key driver of the strength this quarter, having bounced back strongly after the expected fourth quarter declines associated with the 2018 election. This strength was driven by the growing list of Democratic presidential candidates for the 2020 election, and healthy fundraising activity across the country. For the quarter, political deposits grew $89 million to $271 million as compared to a year-end 2018 deposit balance of $182 million. We remain pleased with the success that we continue to achieve as we continue to work with the Democratic Party and numerous candidates. As we exit the first quarter, we are proud to be banking the majority of the Democratic candidates for the upcoming Presidential Election.

While our deposit growth was very strong in the first quarter, we continue to experience a very benign pricing environment as our cost of funds remained relatively stable at 31 basis points, up only four basis points compared to the fourth quarter of 2018, and up five basis points from the year ago quarter. The bank continues to benefit from our low cost of deposit, which remains a significant contributor to our strong profitability and a competitive advantage in the market.

Turning to the other side of the balance sheet, loans increased 7% annualized during the first quarter, or $56.4 million compared to the linked quarter and up 13.4% compared to the first quarter of 2018. Our loan growth was achieved despite the continued headwind from our decision to actively reduce our indirect C&I portfolio, as part of our ongoing efforts to further derisk our balance sheet. Drew will detail the characteristics of this one-off in a few minutes.

As part of our loan growth strategy, we are committed to doubling the loans and securities in the sustainable industry that the New Resource lending team has focused on. As we have previously discussed, we relocated New Resources' former Chief Credit Officer to New York to lead our relationship lending team. This has proven to be a wise move, and it's helped spark a better use of our larger balance sheet, industries like renewable energy, energy efficiency, real estate, including both residential and commercial PACE (phon) financing, and social enterprise lending.

I'm very pleased that between the closing of the acquisition in the spring of 2018 and the end of the first quarter, we have seen an increase of over $256 million in loans, mission-aligned industry. Moreover, the yields of the loans in these industries are quite attractive and are comparable to the yields on the indirect C&I loans that we are running off. We are also quite happy with the credit characteristics of these loans, as many have off taker contracts and/or third party guarantee. Unlike the indirect C&I loans we are running off, most of the new loans we are originating or directly sourced and often come with the positive relationships.

The combination of a very low cost of deposits and improved yields in both our loan book and securities portfolio resulted in an increase in our net interest margin this quarter of one basis point on an adjusted basis over last quarter, and 22 basis points over the first quarter of 2018.

Turning to our capital allocation strategy, I would like to remind everyone that we remain focused on growing our franchise through creative acquisitions of banks that share the same mission and values as Amalgamated. During the quarter, we had the opportunity to take a deep look at one such bank that we thought would be a strong fit for Amalgamated. Unfortunately, the sellers' valuation expectations were elevated and did not match the contraction and bank valuations in the public markets. As a result, we decided not to pursue the opportunity at this time.

We will be disciplined acquirers and will not pursue deals which unnecessarily dilute our shareholders. Additionally, we have the flexibility to be selective given the strong organic growth opportunities that we see in front of us. We will continue to be active in pursuing our M&A opportunities, which include community banks, specialty lenders, and trust assets. But we'll remain focused and disciplined on opportunities that represent a solid strategic fit and a good economic return.

Another barrier to our M&A strategy is the current level of our share price. As a result, and as part of our disciplines capital allocation strategy, our Board and Management team have proposed the authorization of a $25 million share repurchase plan. That plan is subject to approval by our shareholders, and by the New York State Department of Financial Services. I am pleased to report that as of Monday 89% of our shareholder base have voted and 99.99% of those voting have approved the repurchase. The approval will permit us the flexibility to be opportunistic when we see our shares trading meaningfully below intrinsic value. As we look forward, we will maintain a thoughtful and balanced capital allocation strategy with our priorities being first, commanding capital to attractive an accretive acquisition; second, maintaining a steady return of capital to Shareholders through our quarterly dividend; and third, being opportunistic with share repurchases when the circumstances warrant, all with a view of creating long-term value for Shareholders.

To conclude, I'm very pleased with our results and excited with the many opportunities that lie ahead of us as we work to grow our bank. As we focus on our core markets, as well as our commercial banking business, we are well positioned to capture share in what is a very large market opportunity. Our brand is strengthening and our brand awareness is increasing as we work to service the needs of values based institutions. As we partner with those both on the individual and organizational levels who share our mission, we will continue to see our franchise grow.

I'd now like to turn the call over to Drew for a more detailed review of our financial results.

Drew LaBenne:

Thank you, Keith. I will begin by reviewing our first quarter results before turning the line back to the Operator to open the call for questions.

Turning the Slide 4, in the first quarter deposits were relatively flat compared to the $4.1 billion from the fourth quarter of 2018, while average deposits for the quarter were $3.9 billion.

As Keith discussed, we experienced strong organic deposit growth in the quarter, when adjusting for the short-term deposits, which came onto our balance sheet at year-end 2018 and exited on January 2, 2019. This organic growth was well ahead of our expectations which we outlined on our fourth quarter earnings call.

Non-interest bearing deposits increased $144 million from the prior quarter, and now represent 41.6% of average deposits at quarter end. Of note, our deposit beta continues to be low throughout the first quarter as our cost of funds increased only 4 basis points to 31 basis points, representing the continued value of our unique deposit franchise.

Deposits from politically active customers, such as campaigns, packs, and state and national party committees increased $89 million from $182 million at December 31 2018, and in the quarter at $271 million as outlined on Slide 5. As Keith touched on, we anticipate our political deposits to continue to trend upward as we near the 2020 Presidential Election. As campaigns are launched within the Democratic Party, we continue to actively support the businesses of these individuals and their campaigns.

As seen on Slide 6, we delivered fourth quarter loan growth of $56.4 million or 7.0% annualized as compared to the fourth quarter of 2018, and ended the quarter with $3.3 billion of total loans. Loan growth was driven primarily by a $93.3 million increase in residential first liens and pace loans offset by continued strategic reduction in our indirect C&I portfolio of $29.3 million and a $12.2 million reduction in commercial real estate.

Our indirect C&I portfolio totaled $203 million at the end of the first quarter. We've seen a recovery in the syndicated and leverage lending credit market since our last earnings update, and have taken advantage of this recovery. Through a combination of sales and payoffs, we have reduced our indirect C&I balances by approximately $127 million since the end of the first quarter of 2019.

Details of our remaining indirect C&I portfolio are outlined on Page 7 of the presentation. The remaining portfolio is approximately $80 million to $69 million in leveraged loans and $11 million in non-leveraged loans. The remaining portfolio is expected to runoff at a more gradual pace.

Skipping ahead to Slide 9, our net interest margin was 3.65% for the quarter, compared to 3.57% in the fourth quarter of 2018, or 3.64%, on adjusted basis, and 3.43% in the year ago quarter. Our NIM expansion was better than expected resulting from a year-over-year increase in average loans and securities of $375 million and $276 million, respectively, and an increase in yields of 29 and 54 basis points, respectively.

Net interest income for the first quarter of 2019 was $40.8 million, which compares to $40.2 million in the linked quarter and an approximately $8.0 million increase as compared to $32.8 million in the same quarter of 2018. Yield on average earning assets was 4.10% for the first quarter, an increase of 31 basis points as compared to the same period in 2018 driven by an increase in yields due to higher market rates. The yield on our total loans increased to 4.44% compared to 4.32% during the fourth quarter of 2018, an increase of 12 basis points or 2 basis points after adjusting for the impact of the accounting adjustments in the fourth quarter of 2018.

Now on to noninterest income. Noninterest income for the first quarter of 2019 was $7.4 million, decreasing slightly from $7.6 million in the fourth quarter of 2018, and a $400,000 increase compared to the first quarter of 2018. The year-over-year increase was primarily due to higher gains on sale of investments securities of $300,000 in the first quarter of 2019 compared to a loss of $100,000 in the year ago comparable period, combined with modest increases in trust department fees, service charges on deposit accounts and other income.

In April we have distributed $60 million in cash back to holders of our real estate fund that is winding down and expect income that we received from that fund to decrease by approximately $50,000 per month going forward. This decline is in line with our estimates for 2019 and included in our previous guidance.

Turning to Slide 10, noninterest expense for the first quarter of 2019 was $31.4 million, which compares to $35 million in the fourth quarter of 2018 and $28.8 million in the first quarter of 2018. This contributed to a reduction in our efficiency ratio this quarter. We will continue to implement initiatives to reduce our expenses, including reviewing our most significant vendor contracts and identifying opportunities for continued real estate cost savings. Looking forward we will continue to aggressively manage our expenses as we strive to improve our cost structure.

Skipping ahead Slide 12, the credit quality of our portfolio held steady throughout the fourth quarter after adjusting for the charged off C&I loan as non-performing assets totaled $56.6 million or 1.15% from period end total assets at March 31, 2019 which was a decrease of $2.7 million from the linked quarter. The non-performing assets includes $7.2 million of loan 90 days past due and accruing which are primarily related to the delay in renewals of one borrower on four loans. The provision for loan losses in the first quarter of 2019 was $2.2 million which compares to $864,000 of provision in the fourth quarter of 2018. The provision expense in the first quarter was primarily driven by an increased provision on the C&I portfolio.

As previously reported, there was one indirect C&I leveraged loan of $8.4 million that was charged off during the first quarter which was fully reserved and had a minimal impact on our P&L. The provision expense was partially offset by a $600,000 release in the off-balance sheet reserve which is a reduction in other expenses within total non-interest expense.

Turning to slide 13, the allowance for loan losses decreased $5.8 million, $31.4 million at March 31, 2019 from $37.2 million in the linked quarter primarily driven by the charge-off of $8.4 million and partially offset by increasing allowance on two leverage loans and increasing factors related to the charge-off. The increase was offset by a release of the previously mentioned off balance sheet provision of $600,000 which is reported through our non-interest expense.

At March 31, 2019, the bank had $48.1 million of impaired loans for which a specific allowance of $1.5 million was made, compared to $58.3 million of impaired loans in the linked quarter for which specific allowance of $9.6 million was made. The ratio of allowance of total loans was 95 basis points at March 31, 2019 and 115 basis points at December 31, 2018.

Turning to slide 14 our GAAP and core return on tangible common equity were 10.31% and 10.18% respectively. The core return compared to 9.50% the fourth quarter of 2018 and 9.46% for the comparable period in 2018. The increase in core return on tangible common equity in the linked quarter was primarily due to the previously discussed factors. Lastly we remain well capitalized to support future growth.

To conclude, we're extremely pleased with our performance during the first quarter and are optimistic about the outlook for the remainder of the year. Given that we are still early in the months of 2019, we are not making adjustments to our 2019 outlook. We plan to provide an update on our 2019 guidance on the second quarter call as appropriate.

Thank you again for your time today. We look forward updating everyone on the second quarter results in July. With that, I'd like to ask the Operator to open up the line for any questions. Operator?

Operator:

Thank you. At this time, I'll be conducting a question-and-answer session. If you would like to ask a question, please press star, one on your telephone keypad. A confirmation tone will indicate your line is in the question queue. You may press star, two if you would like to remove your question from the queue. For participants using speaker equipment, it may be necessary to pick up your handset before pressing the star keys.

Our first question comes from the line of Steven Alexopoulos with JPMorgan. Please proceed with your question.

Steven Alexopoulos:

Hey, good morning, everybody.

Drew LaBenne:

Hi, Steve.

Steven Alexopoulos:

I want to start first on the loan side of this commentary about the recovery and the purchases. The market for the C&I loans that you sold in the quarter, was that improved demand coming from banks or non-banks?

Drew LaBenne:

It was—well, when we sell a lot of times, it's through the agent that we bought the deal from. So, we don't know the buyer necessarily on the other end. So for example, it might be a large bank who were doing the transaction through. I don't have a—can't give you a clean answer on who's on the other side of that transaction in all cases.

Steven Alexopoulos:

Got you, okay. But even with the accelerated pace of loan sales this quarter, you guys still feel good about prior loan growth guidance of the year, is that right?

Drew LaBenne:

So, I think that's one that we're going to wait to evaluate when we get to Q2. Obviously, the sales that happened here, or that we're disclosing that we did in Q2 are going to put some immediate pressure on the loan growth metrics. Our first quarter was a little bit on the low side of guidance at 7%. But we've historically been a little slow out of the gate in Q1 as well. So we're going to see where we come out in Q2 before updating, but I would say as far as the guidance we gave previously, we're certainly trending to the low end of that and maybe a little lower depending on how we replenish the loans that we just sold off over the past two weeks.

Steven Alexopoulos:

Right. Okay. Now the other side, the deposit side and I know you had guided down the political deposits in the first quarter, but they surged. What drove better than expected political deposit, is it just banking, many more democratic candidates than you expected?

Keith Mestrich:

Yes, I think it's a wide variety of factors, Steve. One is obviously, if you're looking at the scoreboard, there's 20 people running for the Democratic nomination for President and they're all raising money, and they're all raising small dollar money, which keeps those deposits increasing on a fairly steady basis. But it's across the board. I mean, it's not just Presidential candidates. I mean, the party, as a whole has had a tremendous fundraising quarter. There were a lot of Democratic candidates who are our clients, who wanted marginal districts from a democratic perspective and had—needed to start raising funds right away again.

So, it's really just robust campaign fundraising across the board.

Steven Alexopoulos:

Okay, given how strong the deposit quarter was, I know you're going to wait until 2Q to give the official update to guidance, but relative to the deposit guidance previously at 7% to 10%, do you feel like you're trending towards the upper end of that range?

Drew LaBenne:

Yes, definitely we are trending towards the upper end of that range. I mean, we want to watch and make sure that there's stability on that. While our political deposits did come back quite strongly, as we know, we saw nice deposit growth across all of our verticals on—and it was, it was, you know, very good deposit growth, for the franchise as a whole.

Steven Alexopoulos:

Okay, great. Thanks for all the color.

Drew LaBenne:

Thanks, Steve.

Operator:

Thank you. Our next question comes from the line of Matthew Keating with Barclays. Please proceed with your question.

Matthew Keating:

Yes. So maybe just sticking on the political deposit theme, can you remind us historically—I mean, I guess maybe there's not a good precedent for this, given the large number of Democratic candidates but maybe perhaps you can talk about the bank's success. Obviously with Biden coming out recently and raising a lot of money on the first day of this campaign, is that another account that the bank has access to? Thanks.

Keith Mestrich:

So it is publically disclosed that Joe Biden is our client. So that was a nice surge of deposits there. Historically Matt, I think what you're trying to get is what does it look like over a cycle. We really sort of see three periods of growth throughout our political cycles. Early in the cycle, we see campaigns raising more money than they're spending. So, we see an increase overall in deposits. We then see a period where campaigns raise and spend at roughly equilibrium. So, dollars coming in or matching dollars going out and our deposit base is very solid during that period. Then right at the end of the cycle, we see a fairly substantial outflow of deposit. We have no reason to believe that that wouldn't be the case, again this time.

I would just point to the deck that we handed out that went along with the—with our transcript here and sort of draw your attention to Page 5 on that, and if you look at the political trend, what we are seeing is very early on in the cycle here, I think a substantial increase in deposits much earlier in the cycle than we've seen in the past. If you look at what happened between the end of the last cycle from Q4 of 2016, and then the growth into Q1 to '17 and compare that of what happened at Q4 '18 and Q1 of '19, not only from a real dollar perspective, but from a percentage growth perspective, the increase in political deposits, very, very early in the cycle is substantial.

I think that both represent the ongoing maturation of our business. Just to, kind of go back to what Steve was asking about, I think the strength of fundraising that's happening very early on in the cycle.

Matthew Keating:

Understood, now that's very helpful. Then maybe on—obviously, not updating your full year outlook at this point in the year but certainly net interest margin starting at a much higher level than the 3% to 3.5% to 3.6% for your outlook. So, you feel comfortable running towards the high end of that level at this point, in broad terms? Thanks.

Drew LaBenne:

Yes, I think it—so there's competing factors here on the NIM, right? There's the strength of deposit growth in the—what I would call pretty benign repricing we continue to experience which is a positive to the NIM trajectory going forward. Then at least in the near-term, there's going to be how do we backfill the indirect C&I, how fast do we do it and then what yield do we replace it? Given we just made the move a couple weeks ago, we're still evaluating more purchases, and in our pipeline, and can we do anything to expand it. That's going to be a pull down in the NIM.

Those two are competing factors. It's a little early in the quarter for us to say anything near-term. But I think that still keeps us at the high-end of the NIM range over the course of the year.

Matthew Keating:

Understood, and then maybe just a question on the share buyback, so obviously that's good to see. Maybe just your thoughts on how the Board's evaluating buybacks versus liquidity in the stock at this point? How did the discussion go around that in particular? Thanks.

Keith Mestrich:

I think with the capital we have available, obviously, as we prioritize it, it's organic growth first, acquisitions with very positive economics, and then dividend and share buyback. Given where the stock is trading. An acquisition of our own stock looks pretty attractive right now based on what we think the intrinsic value of the Company is.

I think specific volume at specific prices, we're not going to give guidance on that, just as probably any active participant the market would do, but I think we'll evaluate the use of the Board—and Management will evaluate the use of capital as the circumstances warrant on a quarter-by-quarter basis.

Drew LaBenne:

Yes, but I think it's fair to say we're very pleased to have that sort of arrow in our quiver here now to give us an additional option on how to think about capital allocation. We have a Board meeting later this week where we'll be talking about this more in detail with our Board.

Matthew Keating:

Thanks very much.

Operator:

Thank you. Our next question comes from line of Chris O'Connell with KBW. Please proceed with your question.

Chris O'Connell:

Good morning.

Drew LaBenne:

Good morning.

Keith Mestrich:

Good morning, Chris.

Chris O'Connell:

So, yes, just wanted to kind of circle back on the NIM a little bit more and just the dynamics with the indirect C&I roll off next quarter. What is the yield on the indirect C&I? Is that like the mid-five range?

Drew LaBenne:

Yes, it's a couple of fixed rate loans, but just on a variable basis, it's about LIBOR plus 320, those loans are coming off at. So yes, so you're about right on that 5.5, little 575 in terms of what's coming off, so it's definitely higher yield than our average loan on the book.

Chris O'Connell:

How much are the loan purchases this quarter and what yields for those purchases?

Keith Mestrich:

The loan purchases this quarter was only the PACE loan which was $45 million PACE at 5.1%, Q1, just to be clear, Q1, 2019.

Chris O'Connell:

Are you looks looking toward maybe doing purchases that fill in that gap from kind of larger indirect C&I runoff next quarter, we assume that, that would be kind of at the yield.

Drew LaBenne:

We're always evaluating purchases and deciding what to do there. I think that some of the candidates for those purchases could be more PACE loans. We put on a fair amount of residential, as we call residential solar loans as well over the past quarters. We've been watching that in terms of how that's performed and that might be a place where we add additional volume as well. I think as far as just pure residential loans, we have pretty good production organically from those loans. I don't think we'll be doing any purchases in that space. But I don't have a definitive answer, Chris, because we took this action over the past couple weeks. We took advantage of the market when it was there and we're maybe taking a little extra time to make sure we make the right decisions in terms of how we redeploy that into our loan book going forward.

Keith Mestrich:

I do think the only think just on NIM though is cost of funds, right and before somebody get a chance to ask would probably address it a little bit. I mean, we're not seeing significant pressure on deposit pricing. I know a lot of bankers sort of saying that they're seeing released out happen on that a little bit is as well. I would echo that across the board in our commercial business. With an exception here or there we are really seen very little deposit pricing pressure.

Chris O'Connell:

Got it, and then I guess, can you give us a breakdown, it looks like that the non-interest-bearing deposit growth even outside of political deposit, very strong for this quarter. Just wondering what kind of relationship are driving that.

Keith Mestrrich:

So again, going back and thinking about the core thesis here at the Company where we really focus on our core customers in the union space along with their funds, with non-profit, with non electoral political actors that are political organization in the space. Then in this quarter in particular we saw some very nice growth in our philanthropic space, that really across all of those metrics. We saw some very nice large relationships come into bank as well as with organic growth of existing customers.

So really, just across the board, kind of growth in our franchise. We feel, I mean if there is two things I feel really, really good about this quarter if that across the board organic growth in deposits, which is very strong and a very, very good pipeline in that, and very, very comfortable with the opportunity to continue de-risking the balance sheet and sort of eliminating that potential drag on income that could come from future losses as the lending cycle turns here. Those are very core pieces of our investment thesis, ones that we feel really good about nailing this quarter.

Chris O'Connell:

Great. Thank you. One last one if could just go over you—I think you had mentioned down 50K a month, in trust fees related to the real estate fund but I just missed the detail on that. If you just over the details again real quick?

Drew LaBenne:

Sure, so as I think we talked about in prior calls we have a fund that's in runoff stage that's got little less than $0.5 billion of assets remaining under management in that fund. As we have disposed of property there we have done allocation to our shareholders on a fairly regular basis in that bond and it was $50 million allocation to shareholders right at the end of the first quarter.

Keith Mestrich:

Sixty million right at the end of the first quarter.

Drew LaBenne:

Sixty million right at the end of April that was distributed to shareholders

Keith Mestrich:

Last week.

Chris O'Connell:

Thank you.

Operator:

Thank you. Our next question comes from the line of Wally Wallace with Raymond James Financial. Please proceed with your question.

William Wallace:

Thanks, good morning, guys.

Drew LaBenne:

Hey, hi Wally.

William Wallace:

Just real quick on the NIM, what was the benefit from purchase accounting?

Keith Mestrich:

Five basis points, which I think was maybe—I think the previous quarters maybe 6 basis points so pretty consistent.

William Wallace

Okay, and then on the loan sales that have occurred in the second quarter of 127 million that you guys cited, if I'm reading the Slide 7 correctly, it looks like you have not sold any out of the indirect portfolio, since the balance $80 million at the end of April.

Keith Mestrich:

No, no. The indirect portfolio was about $210 million—slightly less than $210 million at the end of the first quarter. So we've sold—yes, $127 million.

William Wallace:

Okay. Okay. All right. So, I was reading it right. All right. So the closing sales…

Keith Mestrich:

It all came from the indirect portfolio.

Keith Mestrich:

Yes. Yes.

William Wallace:

Okay. Okay. Right. Thank you. So, the two leverage loans that you guys built reserves on, can you just talk a little bit about what you saw—what were the characteristics of those loans to drive the increased provision expense?

Keith Mestrich:

Yes, so they were both having trouble on the revenue side of their income statement, which was causing some deterioration in terms of their debt service. So, we downgraded them and took them provision on them, obviously, as you just said.

Building reserves that—right now they sit in the sub-stand—one's in the sub-standard and ones in the sub-standard unit tranche, bucket of that Page 7 that you're referring to right now. So, neither are on non-accrual status. So they're still performing loans, but they do show up in the sub-standard category, which is the first spot, where we really start building at least, what I would call significant reserves on loans.

What you have there is we have five loans that are totaling about $38 million, which are in our sub-standard and non-accrual buckets in our loan, criticized in class classifications.

William Wallace:

The two downgrades in the quarter, is there any collateral support on those?

Keith Mestrich:

There is no collateral support. They're both covered by all assets of the Company, as is pretty standard with the C&I loan. Unit tranche loan that we have—that was downgraded though, I know the unit tranche concept is maybe a little bit to people, but in that loan, we have about 70% of debt and equity behind us in that loan. So, it's more well protected than just a standard C&I loan. The other one that was downgraded is not a unit tranche loan, just the standard leverage loan.

William Wallace:

Okay.

Drew LaBenne:

Wally, just one perspective here, I think on this overall page, and why we want to make sure that we included it here. There's a level of detail, I think, on our phone book that we haven't provided in the past. Was given that there was some movement here, a lot of which happened, because of the charged-off loan that happened and the change and some of the factors that were applied to certain loans as opposed to deterioration in one of the credits in particular itself, was that I think being able to show Shareholders here with some degree of accuracy, or some degree of transparency that this is the stress in the portfolio, to the extent that exists.

There's not a lot beyond this. Our classes of loans that are here are in relatively safe space outside of this indirect C&I bucket. I think we want to say we are selling off a lot of these loans here, even though we had a little movement down a couple of loans, there's not a lot of other things to be worried about in the overall loan portfolio really at this point.

Keith Mestrich:

Yes, basically size it.

William Wallace:

Okay, and then last question is just kind of helping us think about how you might make decisions to purchase these pace loans. Forty million in the quarter, you've got a goal to provide, I think it’s $700 million of what you call socially responsible financing. Are there other lines of business that you guys currently operate in, that gets you to that $700 million? I assume there are and what are they—what is it that you see in a PACE loan that makes you—or a pool of them, that makes you decide to go ahead and purchase them versus to wait and not purchase them?

Drew LaBenne:

You want to go and take it.

Keith Mestrich:

Well, let me take the first part of it. So the commitment is—from a perspective in terms of where we will allocate our dollars is to over the—over two year period it's double the number of social responsible loans that are in our portfolio. When we did the New Resource transaction, that portfolio was about $350 million. That would take it to about $700 million by some time in 2020. As we said in the formal presentation we’ve already done a little bit more than $250 million of those loans, $45 million worth the PACE purchase that we’ve done. The other category where we have focused on that have been both commercial and residential solar purchases, a broad category of energy efficiency green real estate lending that we’ve done and then primarily lending to other non-profits and social responsible enterprises.

In addition to that, it’s not just loans for securities that we’ve done which have included some options to be able to purchase, investment securities that are again in that environmental and sustainability space and I’ll let Drew talk a little bit about the characteristics of what makes a good PACE portfolio versus not a good PACE portfolio.

Drew LaBenne:

Yes, and so just to be clear that $700 million is loans and securities, it’s use of our balance sheet, it's not just loans. As far as PACE loans. So, the $45 million we did was our first PACE transaction and PACE lending is different than most other types of lending because you’re really dealing with the tax lien and it’s a more structured deal than just going out and buying mortgage loans.

In addition, a lot of the production is actually securitized on PACE loan. Finding the right partner to be able to purchase loans we feel good about how the loans have been structured and putting those in the place was I think fair amount of effort for our first transaction so we've gone back out and sourced a couple of more places where we can do additional purchases and we're just getting comfortable with doing that, but I would suspect that there will be more PACE transactions in the future.

William Wallace:

So just to get a sense of $40 million pool, how many individual credits are represented if they were securitized?

Drew LaBenne:

If it was securitized, well I don't know…

William Wallace:

You said they're mostly securitized, I'm assuming this one was.

Drew LaBenne:

No this one was not securitized.

William Wallace:

How many borrowers are in this pool?

Drew LaBenne:

Yes, so the average size on the PACE loans can go anywhere from $25,000 to $50,000 in terms of what's happening. It isn't just solar it can also be home improvement for anything related to energy efficiency and also I think a lot of times these are used for reconstructions related to natural disaster event such as the hurricane or earth stumping of that nature just to pick as an example.

William Wallace:

Okay, all right, thank you. I'll hop out. Let somebody ask a question.

Drew LaBenne:

Thanks, Wally.

Operator:

Thank you. Ladies, and gentlemen, as a reminder if you'd like to join the question queue please press star, one at this time. Our next question comes from the line of Matthew Breese with Piper Jaffray. Please proceed with your question.

Matthew Breese:

Good morning. I just wanted to follow up on the elevated provision along with the two leveraged loans you discussed you also mentioned that you released (phon) historical—increasing historical loss factors. Could you walk me through that change and what happened there?

Drew LaBenne:

Yes, so the historical loss factor that Keith was referring to was the leveraged loan factor and the one charge-off that we had for $8.4 million. So, what that does is that anything else that is sub-standard non-unit tranche, which was one loan only that was existing in that pocket in Q1, except the downgrade that we just discussed, takes on an additional provision related to that increase in the loss factor.

So, it really only applies to sub-standard leveraged loans that are non-unit tranche just a bucket of two at this point, two loans.

Matthew Breese:

Got it. Okay, understood, and then as we think about the political deposits, I just wanted to gain a sense for how that bucket is broken up how much of it is tied to Presidential candidates, how much is tied to tax or state campaigns, could you break it up a little bit and give us the sense for what the components are?

Drew LaBenne:

So, sort of roughly about $70 million of it is associated with presidential campaigns then of what is remaining there I would say that—getting some numbers here that'll give me some additional perspective. Then I would say about $40 million of it is sort of federal election campaigns, about $20 million of it roughly is sort of what I would call institutional business like the big institutions of the parties and then that balance is of variety of different kinds of categories.

So, it's nicely dispersed across different kinds of categories of people who are running for office. It's much more so sort of Federal election activities, and it is state and local activity. But it is dispersed across the presidential and sort of other campaign activity.

Matthew Breese:

As we think about the change from 4Q to this quarter, I think the $89 million pickup. Was that mostly in the presidential campaign? Or, could you break up with the change as well?

Keith Mestrich:

I don't know that I have that level of detail, Matt be able to do it, but a substantial and, obviously, in Q4, there wasn't a lot of Presidential money out there. So that was—a lot of that came from Presidential. I think we disclosed that there may be $70 million in Presidential money was raised. That's probably about it, without giving any more detail on individuals.

Matthew Breese:

Okay, no, that's, that's very helpful. Then just thinking about loan growth for the year, I know you provided some commentary earlier, but could you give us a sense for where the loan pipeline stood at quarter-end versus yearend? If you can't give us that level of detail, perhaps characterize it as terms of percentage difference?

Drew LaBenne:

Percentage difference. Yes, actually, because can't remember what the Q4 pipeline was honestly, that I'll say, Matt, I guess this is I think the pipeline feels pretty good at this point. It's a mix of both CRE transactions and non-CRE transactions. I think I think we feel pretty good about the lending pipeline. I like to watch and see what converts out of that. I wish the yield curve was a little steeper than it is right now.

So things that are coming on, in the multifamily space are, kind of in the 3.75% to 4% land again. That might just be where we're at, at this point, in terms of yields coming on. But, clearly with the hundred and $27 million we're running off in the C&I book that puts additional pressure on our long growth targets, which I think some of which I think we will be able to make up through purchases as well.

Matthew Breese:

Got it. Okay, and then just staying on the multifamily comment. Some are suspecting that rent regulated apartments, the valuation of those buildings or apartments might be impacted by the upcoming (inaudible) guidelines board. Could you give us a sense for the average LTV portfolio, and then more recently what kind of the underwriting perspective what the average LTV is?

Drew LaBenne:

Yes, so I think the average LTV in our portfolio was low 60s, on our multifamily portfolio. I'll tell you this is this is my perspective, but I suspect most members of our credit committee agree with that as well because we certainly discussed it is. We find debt service coverage to be maybe a better metric in terms of the credit worthiness than LTV, because you're looking at real cash flows that are coming through the business whereas LTVs move around obviously, based on appraisals, cap rates, but also, things like the potential regulation that you were just discussing, can have a big impact on LTV.

So, while they're also a reliable measure, I think maybe a little less reliable for underwriting standards than debt service coverage can be in terms of how you think about these loans. But, I think we have certainly sacrificed yield for better credit quality in multifamily and CRE, to be able to make sure that for any type of event like this, that happens, hopefully we're as well underwritten or maybe even better underwritten than the competition around us.

Keith Mestrich:

I would I would just add, even if the rent regulations does come into play, I don't think it's going to change our approach the market all that much unlike players who are primarily underwriting market rate deals, we are very comfortable and a bunch of our portfolio already has, substantial, affordable components to it, given sort of the size of our loans in that space and where we tend to—where we tend to land. I think we're going to be very comfortable with whatever comes out of all (inaudible).

Matthew Breese:

Right, I guess, I was just trying to get a sense for, if we recall portion of your portfolio potentially at risk from a valuation perspective, I would think it's the higher LTV segment. I wanted to gain a sense for a portion of your book that's called average LTV north of 70% or 75%.

Keith Mestrich:

No, no, we're not in that space at all.

Matthew Breese:

Understood. Okay, that's all I had. Thank you.

Drew LaBenne:

Great. Thanks, Matt.

Operator:

Thank you, ladies and gentlemen, this concludes our question-and-answer session. I'll turn the floor back to Mr. Mestrich for any final comments.

Keith Mestrich:

I just want to say thank you to everybody for joining us for a little bit today. We're very happy with the quarter. We had investment thesis that we had an investment thesis that we have stuck to, that we talked to the Street about back in August when we first went public. We think it's a smart business strategy. We're executing very well on it, and I think you can see that in the results from this quarter. I look forward to being in touch with many of you in the future. Thank you.

Operator:

Thank you. This concludes today's teleconference. You may disconnect your lines at this time. Thank you for your participation.