Origin Bancorp
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9:00 a.m. EST

OPERATOR: Good day, ladies and gentlemen, and welcome to the Origin Bancorp, Inc. Third Quarter 2022 Earnings Conference Call. All lines have been placed on a listen only mode and the floor will be open for questions and comments following the presentation. If you should require assistance throughout the conference, please press “star,” “0” to reach a live operator. Please note, this event is being recorded.

I would now like to turn the conference over to Chris Reigelman, Head of Investor Relations. Please go ahead.

CHRIS REIGELMAN: Good morning and thank you for joining us today. We issued our earnings press release yesterday afternoon, a copy of which is available on our website, along with the slide presentation that we will refer to during this presentation.

Please refer to Slide 2 of our slide presentation, which includes our safe harbor statements regarding forward-looking statements and use of non-GAAP financial measures.

For those joining by phone, please note the slide presentation is available on our website at www.origin.bank.

Please also note that our safe harbor statements are available on Page 7 of our earnings release filed with the SEC yesterday. All comments made during today's call are subject to the safe harbor statements in our slide presentation and earnings release.

I'm joined this morning by Origin Bancorp's Chairman, President and CEO, Drake Mills; President and CEO of Origin Bank, Lance Hall; Chief Accounting Officer, Steve Brolly; our Chief Risk Officer, Jim Crotwell; our Chief Financial Officer, Wally Wallace; and our Chief Credit and Banking Officer, Preston Moore. After the presentation, we'll be happy to address any questions you may have.

The call is now yours, Drake.

DRAKE MILLS: Thank you, Chris, and good morning. This is an exciting and significant quarter for Origin as we completed the merger with BT Holdings on August 1 and the full system conversion at the beginning of October. When we publicly announced the partnership, I talked about BTH being a unicorn, that this is a cultural fit, a geographical fit, a financial fit for both companies. I am proud of the Origin and BTH employees who made this process go so smoothly. The fact that this deal was announced in late February, received regulatory approval in June, closed in August and finalized the system conversion in early October with flawless execution is a testament to the quality of our people, the strength of our relationships with the communities we serve and the ability of our company to capitalize on the right opportunities.

In our investor presentation, we provided an update to the financial metrics that resulted from the close of the BTH acquisition. Since our announcement in February, the rate environment has changed materially, leading to changes in our estimated purchase accounting fair value marks. While these purely accounting adjustments resulted in changes to our tangible book value dilution and EPS accretion, the bottom line is that the rate environment has improved the fundamental performance of both Origin and BTH, lowering the estimated tangible book value earn back period to 1.6 years.

With the completion of the merger with BTH, Origin has enhanced its (inaudible) quarter presence with significant opportunity to grow market share in the deposit and loan rich East Texas footprint while adding impressive scale to our Dallas-Fort Worth markets.

Culture can often get overlooked in our industry, particularly with partnerships. This past quarter, I was in each of our markets across Texas, Louisiana, Mississippi for our annual culture celebrations. There is a buzz around our company and a deep commitment to our culture of serving our customers, communities and shareholders that is stronger than I've seen in my 39 years of being with this company. I'm optimistic and excited about where we are and what we will accomplish. Lance, Steve and Jim will get into the details of the quarter later in the presentation.

As I look at the performance for the quarter and remove all the noise, our core profitability continues to strengthen and is in line with our long-term strategic goals. I am particularly pleased with our adjusted ROA of 1.34% and adjusted ROE of 13.14%. With the addition of BTH, we showed impressive loan growth again this quarter with 14% annualized growth while applying strict underwriting standards to our process and continue to show improvement in our net interest margin, which was up approximately 40 basis points for the second quarter in a row.

We remain focused on building long-term value for this company and took major steps this quarter to put us in a position of strength as we move forward. I'm proud of our growth. I'm proud of our employees for all they do to make us successful. And I'm proud of the discipline we apply to managing our business with a strategic focus and commitment toward doing what we say we will do.

Now I'll turn it over to Lance.

MARTIN HALL: Thanks, Drake. We have a lot to be proud of as a company. And as I analyze the fundamentals of our production, I'm very pleased with the performance of our bankers across Texas, Louisiana and Mississippi. I talk often about our strategy and our relationship-based approach to attracting and retaining clients. I feel strongly that we are executing on this strategy and are capitalizing on opportunities in all of our markets, particularly Dallas, Fort Worth, Houston and now East Texas.

Organic loan growth for the quarter was very strong. Adjusting for BTH and excluding mortgage warehouse, loans grew $215.3 million or 3.5% compared to the linked quarter. This equates to a 14% annualized growth rate ahead of our low double-digit target.

On Slide 11, you can see the impressive 16.9% compounded annual loan growth we have shown since our IPO in 2018. As Drake mentioned, we're extremely excited about the partnership with BTH and the opportunities it presents in Dallas, Fort Worth and East Texas.

Origin and BTH have a shared vision for what we can accomplish. Like Origin, they have built and strengthened profitable core relationships. Their focus on C&I and owner-occupied commercial real estate have been impressive. And we believe we will be able to bolster those relationships through our suite of treasury management products and services, our larger balance sheet and our targeted marketing efforts.

Our bankers remain focused on driving deposits within our markets, and I'm proud of how they delivered, particularly with noninterest-bearing deposits. In the third quarter and adjusting for BTH, we showed an increase of noninterest-bearing deposits of $91.2 million or 3.5%, which is 14% annualized. Total deposits declined for the quarter, however. This decline was due in large part to one customer moving significant dollars based on a business transaction and our strategic decision to allow some noncore funding to leave the bank. With an 83% loan-to-deposit ratio, excluding mortgage warehouse, Origin is well positioned to fund continued loan growth.

We know deposit betas are top of mind, but I think it's important to point out that deposit betas aren't the only piece of the puzzle as it relates to net interest margin. We are pleased with how our deposit and loan pricing has been trending. As of the third quarter, our cumulative total deposit beta was 16%, and our cumulative NIM beta was 40%. We looked back at prior tiding cycles with our deposit beta range from 27% to 37% and our NIM beta range from 22% to 30%. Where we stand today, we believe Origin is well positioned based on this historic analysis. Steve will provide more detail on our NIM later in the presentation.

Before I turn it over to Jim to talk about our impressive credit metrics, I want to brag on our bankers. As Drake mentioned, we completed the system conversion with BTH at the beginning of October, and our employees did an incredible job throughout that entire process. We are always focused on the client experience, and our teams executed in a dynamic way. I'm so proud of where we are in 2022.

Our loan growth is up. Our focus on NIBs remain strong. Our treasury management team continues to be a differentiator. The integration with BTH and how our teams rose to that challenge was remarkable, and our culture has never been stronger.

Now I'll turn it over to Jim.

JIMMY CROTWELL: Thanks, Lance. Slide 14 provides a recap of our credit quality metrics. We continue to be extremely pleased with the strong performance of our loan portfolio. As a percentage of total loans held for investment, pass-through loans held for investment were 0.16% at quarter end, while nonperforming loans held for investment came in at 0.20%. Classified loans held for -- to total loans held for investment were stable at 1.01%, while annualized net charge-offs to average loans held for investment came in at 0.07% for the quarter, down from 0.12% for Q2. As I shared last quarter, our focus on relationship banking, along with sound underwriting and credit structure, continues to be the drivers behind the solid performance of our loan portfolio.

For Q3, we increased our allowance for credit losses from $63.1 million to $83.4 million, resulting in our reserve to loans held for investment increasing from 1.25% to 1.29% net of mortgage warehouse. As a percentage of nonperforming loans held for investment, our reserve increased to 594% at the end of Q3 compared to 448% at the end of Q2 and 285% a year ago, which also shows our strong and improving debt profile.

While our portfolio continues to be resilient, we are closely monitoring the impact of inflation and the likelihood of an economic recession on our portfolio. In addition, headwinds continue to persist as to labor supply, wages, supply chain disruptions and yield political concerns and their impact on the performance of our portfolio.

As stated last quarter, we continue to believe that the markets we serve will be impacted to a lesser degree by a recession than other areas of the country. Again, we feel that we are well prepared in this time of continued uncertainty and are extremely pleased with the overall performance and outlook of our portfolio.

I'll now turn it over to Steve.

STEPHEN BROLLY: Thanks, Jim. Slide 15 is our yields, costs and loans held for investment portfolio slide. During the third quarter, our total yield on loans held for investment increased 68 (ph) basis points, which includes the impact of $1.4 million were approximately 7 basis points from BTH purchase accounting adjustments recorded during the third quarter.

As an asset-sensitive bank, increased interest rates will be beneficial for Origin. We expect to generate an incremental $7.2 million or 2.50% and net interest income from a 100 basis point instantaneous parallel shift in interest rates.

Slide 16 shows our recent net interest income and NIM trends. Of the total $19 million increase in net interest income during the quarter, $11 million was attributable to BTH, with the majority of the remaining change from increased yields and volume on loans. In addition, the changes in our NIM quarter-over-quarter are consistent with the changes in net interest income.

Slide 17 is the investment security slide. On a net basis, we ended the third quarter relatively flat compared to June 30. As of BTH, investments were recorded at fair value on day 1 of the merger. This gave us the opportunity to liquidate most of their portfolio without incurring a realized loss. We use that liquidity primarily to pay down short-term borrowings.

Slide 18 is our net revenue distribution. The top graph shows our net revenue growth since our IPO. Our revenue has nearly doubled in the last 3 years driven by strong consistent loan growth and, most recently, the BTH merger and increased interest rates.

We made a strategic decision to impair our Ginnie Mae MSR portfolio by $2 million, which is part of the bottom-right table. We believe that there is a current oversaturation in the market for these assets. Therefore, it was prudent to reduce the carrying value.

Slide 19, our noninterest expense analysis. We reported total noninterest expense of $56.2 million, an increase of $12.1 million. The increases this quarter are primarily due to $2.8 million of merger-related expense, $2.3 million in salaries and employee benefits from the additional BTH employees, $1.3 million amortization of intangible assets from the merger, $2 million from BTH operational expenses other than those I just mentioned above, and $1 million increase in our incentive accruals due to exceeding performance matrix.

Moving to the next slide. We show trends on our regulatory capital ratios. We continue to be well capitalized and are in a strong position to take advantage of future opportunities to drive value for our shareholders.

Now I'll turn it over to Drake.

MILLS: Thanks, Steve. Since I've been leading this organization, we've been focused on building a company, which is committed to a unique corporate culture, with a drive to create long-term profitable growth for the benefit of all stakeholders.

There is a slide in our presentation that demonstrates long-term growth in total assets, total stockholders' equity and total shareholder return and have increased substantially over the past 3 decades. Origin is built for long-term success, and the additions of BTH this quarter strengthens our company even more.

Throughout our history, we've been committed to our culture and hiring the best employees within our markets. As Steve mentioned earlier, we made a decision last quarter to implement inflationary raises for a large segment of our employees. While this impacts our expenses, it was the right thing to do. Our mission is to passionately pursue ways to make banking and insurance more rewarding for our employees, customers, communities and shareholders, and we remain focused on that mission every day.

I am very pleased with where we are as a company. Looking at the fourth quarter, we anticipate additional net interest margin expansion, loan and deposit growth, further improvement in our efficiency ratio and continued stability in our credit metrics. Our current capital and liquidity levels put us in a strong position. We have the right people in dynamic growth markets, and we have shown our ability to drive long-term value.

Thank you to our employees who are committed to our culture and to our shareholders for their confidence in the vision of Origin. Thank you for being on the call today. Now we'll open the call up for questions.

OPERATOR: Thank you. Ladies and gentlemen, the floor is now open for questions. If you do have a question please press “star,” “1” on your telephone keypad at this time. If you’re using a speaker phone we ask that while posing your question you just pick up your handset to provide favorable sound quality. Once again, ladies and gentlemen, if you do have a question or comment please press “star,” “1” on your telephone keypad at this time. Please hold as we poll for questions. And we'll take our first question from Michael Rose from Raymond James.

MICHAEL ROSE: Hey, good morning guys. Thanks for taking my questions.

MILLS: Morning, Michael.

ROSE: Morning. Maybe just if we could start with the updated thoughts around the acquisition. So I think clearly, the -- what you show in the slides is the EPS accretion is less, and you foreshadowed that in the 8-K that was put out a couple of weeks ago, but the tangible book dilution and earn back are less as well. So if you can kind of just walk us through kind of the changes in the marks and what kind of transpired from start to finish would be helpful.

MILLS: Yes. I'll start, Michael. It's -- really when you look at where we announced versus where we close, and I think if you put up the metrics, you would say the deal looks better after we close. But obviously, the interest rate environment changed significantly. I think the bulk of what we're dealing with from the standpoint of EPS accretion or the decline in EPS accretion has the most to do with the CDI and the amortization at CDI. I mean we start -- we announced the bill interest rates at, let's say, 50 -- whatever, half. And then all of a sudden, we're starting, what, 3 30, Steve, or somewhere in that range. And so you move from $6 million accretion to $38 million accretion, and that's that -- I would say that's the majority of the impact of the change in metrics as we looked at this deal overall. But for me, that's accounting.

And when you look at the deal overall from loans, deposits to people in the markets, our opportunity to really leverage East Texas, which I am so excited about, I understand the accounting is a big part of it, but the metrics around the deal, the markets, the people and the opportunities did not change, and we're so excited about it. So Wally, I don't know if you want to add anything to the deal metrics.

WILLIAM WALLACE: The only thing I'd add -- Michael, it's kind of funny talking to you first, by the way. The only thing I'd add is, like Drake said, the change in the rates drove meaningful changes in all the purchase accounting marks. It adds a ton of noise. At the end of the day, a lower tangible book value payback period is what we ended up with, which we think is positive. And that doesn't take into account the fact that also what changed in that period was that our asset sensitivity made our earnings power stronger and BTH's earnings power stronger. So ultimately, we think the earn back is even less than what was on that slide. I'll just stop there.

MILLS: Yes, Michael, I'm sorry. I said accretion. I mean amortization on the CDI. I apologize.

ROSE: Understood. And I really appreciate all the non-GAAP adjustments in the slide, especially the expected accretion as we think about the next couple of years. But if I strip that out, which won't have a major impact or at least as big as I would -- we would have thought at the beginning, just what you mentioned -- even what you just mentioned, how should we kind of think about BTH being layered in and the balance sheet moves that you made and how that's going to relate to margin expansion moving forward, particularly in the context of what still looks to be like a pretty good loan growth, positive earning asset mix shift as we move forward? Just any sort of near-term call would be great.

MILLS: And for us, one thing that I saw in the last 2 months for BTH is, as we announced, they had hit a wall from the standpoint of production. Their people were so overwhelmed by volumes and customers that they were taking care of what they had without (inaudible) outreach. Well, what we saw was a pickup in growth in the last 2 months. And so our intuitions told us that you support these people do the things that they need to do. And certainly, we're in the midst of that. We have to provide these people with portfolio managers and really the systems that we use. And this will take some time, but we're seeing some early growth opportunities.

And I do think that what those growth opportunities in their markets, especially East Texas will do, will help continue NIM expansion. But from a NIM expansion process or where we are today, we certainly have not peaked. I think we're going to see good NIM expansion in the fourth quarter. And we will continue to focus on starting the process of growing out or doing the things we need to do in East Texas, which -- I keep talking about East Texas. They have a significant impact as I talked about on the introduction in our Dallas-Fort Worth market, and Jay and Rory Berger (ph) working well together with those teams. But I'm just excited about our operate to go in, do some marketing in East Texas and really start to benefit from the growth in those markets. So -- and I hope I'm answering your question. But I'm really bullish about NIM next quarter.

We have some good opportunities as we continue to see, I think, fair pricing in the new credits that we're bringing on.

ROSE: Very helpful. And then maybe just finally for me. I know the deal just recently close, but there clearly is going to be -- there is and will continue to be dislocations kind of in your core markets. I mean would you be open to doing another deal should an opportunity arise in the near term? Or kind of take a pause and get the cost savings and realize all the benefits from the deal before you look at the next one?

MILLS: We're focused on integrating BTH. So that's what I'm focused on. And I'm not going to say that there couldn't be another great deal walk in, but there's not going to be a BTH that walks in. I think we need to do the things necessary to make sure that, look, we -- and I've used the term flawless execution in the BTH deal. For the most part, that is exactly on point. But we can't stop in making these people feel comfortable in this organization.

This is all about culture. And when I tell you that these 2 organizations breathe culture the same way, that is accurate. And so for me, spending time in East Texas, making sure that Jay and his teams are on board, we still have to integrate products and services from the standpoint of making sure their customers are online. That's where we're focused. And if -- I think if we let up at all, we got -- we've been fortunate.

We had 79 open positions and desperate for quality people. In our cost saves as we build this out, there were 40-some-odd people BTH that historically would not have moved forward. The quality of their people and what they brought to the table filled 40 of those positions that we had in a big way. What that allowed us to do -- and you might say, hey, those should have been cost saves, but what it allows us to do is keep a very strong presence in East Texas where I think that benefits when the community looks at how we integrate and how we use their people and the quality of that market, those were all positives for us. So we're going to stay focused on that.

Certainly, if another unicorn -- I don't think that's the right way you describe unicorn has popped up, we would certainly take advantage of that.

OPERATOR: And our next question comes from Matt Olney from Stephens Inc.

MATT OLNEY: I want to ask about deposit growth. It looks like in the third quarter, the legacy end-of-period deposit balances contracted, but I think Lance mentioned in the prepared remarks that the NIB deposit growth was really strong ex the BTH. Any color on the pipeline of deposit growth from here and thinking about the fourth quarter? Is it something similar to where we could see continued strength of NIB growth but run off of some higher cost deposits? Or are we now at the point to where the deposit balance at 9 30 looks pretty sticky, and we could see total deposit balances start to grow again?

HALL: Yes. It's Lance. I mean, look, there's no question that liquidity has sort of been pulled out of a lot of the banking systems through treasuries, through brokerage firms. We're sort of balancing NIM. At the same time, we're balancing our asset size to make sure we stay under 10 B (ph) this year. So I think we've tried to be strategic and smart about how we focus on core deposits.

You know our story in the way that we've built our company around geographic management models, around incentive plans that pay an equal amount for deposits, and they do a loan for the way that we have used lift-outs to attract deposit specialists and treasury management. So I feel confident as the banks begin to compete more fiercely on deposit pricing, that we're going to be able to do a really good job of staying in our -- in the window that we want to, which is going to be mid- to high 80% loan-to-deposit ratio.

We continue to grow NIBs, which is critical for us. That's been a strategic focus for the last 3 or 4 years. Super excited about the opportunity to grow deposits and East Texas specifically. And then there's also kind of don't forget the, what I'm going to say, the luxury we have in North Louisiana. As we look at where deposit growth and deposit runoff has been for us this year, we still had strong growth in Louisiana and Mississippi and from some of our more rural markets. It's allowed us to be strategic and not fighting us harshly for some of the noncore stuff.

And if you remember, we talked about last quarter, we let $250 million go in Q2. So I think you'll see us manage the 10 B and then become much more competitive on the rate side, but very confident in our ability to manage through.

OLNEY: Okay. Appreciate that, Lance. And then on the loan growth front, nice results ex BTH. And now that you've folded in BTH and consider the pipeline and the current economic environment, want to get your thoughts around organic loan growth for the fourth quarter and looking into next year.

MILLS: Yes. Matt, it continues to surprise us when we look at pipelines. And current pipeline is -- looks extremely good going into the fourth quarter through the first month. And so at this point, because of the pullback -- and usually, we talk about loan growth, less mortgage warehouse. And I might as well go ahead and address this now on a mortgage warehouse. We ended up last quarter at 4 61 with obviously brought over about $40 million for BTH. And those were relationships that we were going to exit. We've gone through that process. We're going to end up, I think, at the end of the fourth quarter somewhere around $300 million in mortgage warehouse. But what is exciting about that is that we are focused on high-quality clients that are managing the expense structure. And relationships we feel will continue to be here.

We actually found out that several of our relationships are lowering or reducing their number of banks. We're not feeling that reduction from those high-quality clients, and that's a positive. So I think you're going to see mortgage warehouse about 5% or 6% of outstandings, and I like that where we are right now going into the uncertainty of the environment we're in.

So as long -- as far as loan growth ex mortgage warehouse, I think we're going to see, let's say, a low double-digit growth through the fourth quarter, which is still surprising. But quality, we continue to apply very strict underwriting guidelines as we had to set the last several years. So we feel good about the quality we're bringing on.

Going through '23, if we start looking at pipelines, talking to our markets and everything, I still think we can maintain a high single-digit growth through '23 on the loan side.

HALL: Yes. Matt, this is Lance. I would add, we just continue to be excited about where the loans are coming from. If you go back over the last 4 quarters, I mean, Houston has grown -- had loan growth of 44%; DFW, 29%, and that's reflective of what we're continuing to see in our pipelines. And we continue to be excited about our lift-out strategy. We have added another 7 producers in Q3. That stays right in line in the last 12 months has been 28%. And that continues to be a combination of commercial bankers as well as private banking with treasury management, deposit gatherers, business development. So it's very heavy deposit-focused on who we're hiring.

I went back and looked at sort of producers hired over the last 12 months. They've grown loans $339 million, deposits almost $140 million. So these people are producing at a really high level. We love the credit quality that we're seeing from these long-term relationships that they're dragging over. So just the strategy of the lift-outs and the focus on Texas continues to pay dividends.

OPERATOR: And next, we'll go to Brad Milsaps from Piper Sandler.

MILLS: Brad, glad to welcome you back after being absent for a while.

BRAD MILSAPS: Exile, I suppose. I wanted to just kind of follow up on maybe the size of the balance sheet. I know you guys were making a lot of adjustments to stay -- to make sure you stayed under $10 billion. Just wanted to make sure I kind of had the right starting point for average earning assets. Are you pretty much through kind of all the adjustments you wanted to make notwithstanding what you just said about mortgage warehouse? Just want to get a sense of does the balance sheet kind of stabilize from here or does it trend down further? Just kind of curious, I want to make sure I have the right sort of jumping off point to drive NII, et cetera.

MILLS: As I'm always going to be, as transparent as needed, it -- I felt like after we sold $450 million in securities from BTH and reduce debt that we had a very good runway to stay right under 10 B (ph) for 12/31. We're pushing that a little bit at this point with pipeline growth. We still have opportunities with a couple of triggers to pull to ensure that we stay below $10 billion. But I suspect we're going to end up the year somewhere around $9.8 billion. And then at that point, we're off to the races, continuing to grow the balance sheet as we have in the past.

MILSAPS: Great. And then maybe a similar question around expenses. Maybe a touch higher than I was looking for, but obviously, you got cost savings still to come. Can you just kind of speak to maybe the expense trajectory a little bit as we think about another month of BTH in the fourth quarter and then as maybe you start to see some cost savings into 2023?

BROLLY: Brad, it's Steve. There is a lot of noise in this past quarter. We ended up 56.2. When we look at the merger cost, it will be taken out, but you have to add in the salary expense that we talked about where we increased wages during the third quarter. The fourth quarter will be the entire quarter. We also have 1 month of operating expenses, as you said, for BTH.

So when you run your models, and if you end up between $57 million and $58 million for the fourth quarter, we would say that's very reasonable. And then going forward to next year, I think we're at single-digit increases from that number in the fourth quarter. Again, we've gotten ahead of the inflationary wage pressures because we had the extra salary increases during the third quarter. And so we really think -- and we haven't finalized the budget, but we think mid-single digits from that $57 million and $58 million fourth quarter mark.

MILLS: Let me say this because I think this is very important. We have in our plan for budget significant opportunities to grow, and we're going to continue to look at this. Even as we face an inflationary period, we think that our footprint will lag in the recession. And as we go through that, we see significant opportunities to enhance this organization from a growth perspective, but profitable growth.

And that's what we're focused on is NIM growth, but yet at the same time, doing the things and taking advantage of dislocation in the market. So that's what's built into some of this budget on top of the cost saves that we see in the next 12 to 14 months as we finalize systems and do the things as necessary. So I feel really good about where we are to continue positive operating leverage and do the things we need to do, but not forget about the growth and the taking advantage of the market dislocation that's currently in track.

MILSAPS: Got it. Makes sense. And that would include that step-up in the CDI number, correct, that $57 million to $58 million?

MILLS: Yes, it does.

OPERATOR: This does conclude today's conference as it ended abruptly due to an unforeseen telecommunications issue. This interruption was in no way caused by Origin Bancorp, and our conferencing partner sincerely apologizes for the disruption.