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**Southside Bancshares,
Inc.** NYSE:SBSI

Earnings Call

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Call Participants

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SVP & Investor Relations Officer

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*Hovde Group, LLC, Research
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Stephens Inc., Research Division

Michael Edward Rose

*Raymond James & Associates,
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Wood Neblett Lay

*Keefe, Bruyette, & Woods, Inc.,
Research Division*

Presentation

Operator

Hello, everyone. Thank you for joining us, and welcome to the Southside Bancshares, Inc. Fourth Quarter and Year-End 2025 Earnings Call. [Operator Instructions] I will now hand the call over to Lindsey Bailes, SVP, Investor Relations.

Lindsey Bailes

SVP & Investor Relations Officer

Thank you, Alexandria. Good morning, everyone, and welcome to Southside Bancshares Fourth Quarter and Year-end 2025 Earnings Call. A transcript of today's call will be posted on southside.com under Investor Relations. During today's call and in other disclosures and presentations, I'll remind you forward-looking statements are subject to risks and uncertainties.

Factors that could materially change our current forward-looking assumptions are described in our earnings release and our Form 10-K. Joining me today are President and CEO, Keith Donahoe; and CFO, Julie Shamburger. First, Keith will start us off with his comments on the quarter, and then Julie will give an overview of our financial results. I will now turn the call over to Keith.

Keith M. Donahoe

CEO, President & Director

Thank you, Lindsey, and welcome to today's call. Early in the fourth quarter, market conditions allowed us to continue the partial restructuring of our available-for-sale securities by selling approximately \$82 million of lower-yielding long-duration municipal securities with a combined taxable equivalent yield of 2.6% and generating a \$7.3 million net loss. All sales were completed at the end of October with net proceeds together with additional portfolio cash flows and a \$49.7 million sale of a T-bill reinvested in various low premium, primarily 5.5% coupon Agency MBS with an average yield of 5.36%.

Similar to the third quarter security sales, we believe the fourth quarter sales enhances future net interest income while providing additional balance sheet flexibility as we grow. We estimate the payback on the third quarter security sales to be less than 3.5 years. Overall, we experienced a \$1.5 million linked quarter increase in net interest income, resulting primarily from lower funding cost and moderate loan growth. Our net interest margin expanded to 2.98%, and we expect additional net interest margin expansion resulting from the redemption of approximately \$93 million of subordinated debt on February 15, 2026.

Fourth quarter new loan production totaled approximately \$327 million compared to third quarter production of approximately \$500 million. Of the new loan production, \$215 million funded during the quarter with the unfunded portion of this quarter's production expected to fund over the next 6 to 9 quarters. Excluding regular amortization and line of credit activity, fourth quarter payoffs totaled approximately \$164 million. While higher than the third quarter payoffs of \$117 million, it was the second lowest quarter for payoffs during 2025.

Third quarter CRE payoffs included 28 loans secured by industrial, retail, multifamily, medical office, general office and commercial land. Most of these were concentrated in five industrial properties and 8 retail properties. Outside of CRE payoffs, we did exit a C&I participation during the quarter due to pricing well below our comfort zone. Our loan pipeline dipped to \$1.5 billion mid-quarter, but rebounded after the first of the year to just over \$2 billion today. The pipeline is well balanced with approximately 42% term loans and 58% construction or commercial lines of credit.

This mix is unchanged from the third quarter. C&I-related opportunities represent approximately 20% of today's total pipeline, and that's down slightly from third quarter's 22%. Credit quality remains strong. During the fourth quarter, nonperforming assets increased \$2.6 million, primarily related to a \$2.4 million loan secured by a small residential condo project, but remain concentrated in the previously disclosed \$27.5 million multifamily loan we moved into the nonperforming category during the first quarter of '25.

Despite this loan not paying off in the fourth quarter, we remain optimistic that the borrower will finalize their refinance within the next 2 weeks. As a percentage of total assets, nonperforming assets remained low at 0.45%. When considering our net income, earnings per share and other financial results, excluding the onetime loss on the sale of securities, we had an excellent quarter. Overall, the markets we serve remain healthy, and the Texas economy is anticipated to grow at a faster pace than the overall projected U.S. growth rate. With that, I'll turn the call over to Julie.

Julie N. Shamburger

Chief Financial Officer

Thank you, Keith. Good morning, everyone, and welcome to our fourth quarter and year-end call. For the fourth quarter, we were pleased to report net income of \$21 million, an increase of \$16.1 million or 327.2%. Diluted earnings per share were \$0.70 for the fourth quarter, an increase of \$0.54 per share linked quarter. We reported net income of \$69.2 million for 2025, a decrease of \$19.3 million or 21.8% and diluted earnings per share of \$2.29 compared to \$2.91 for 2024.

The decrease was driven by the restructuring of the AFS securities portfolio. As of December 31, loans were \$4.82 billion, a linked quarter increase of \$52.7 million or 1.1%. The linked quarter increase was driven by an increase of \$29 million in construction loans, \$24.1 million in commercial real estate loans and \$14.8 million in commercial loans, partially offset by decreases of \$6.6 million in municipal loans and \$5.7 million in 1-4 family residential loans. The average rate of loans funded during the fourth quarter was approximately 6.6%.

As of December 31, our loans with oil and gas industry exposure were \$71 million or 1.5% of total loans compared to \$70.6 million or 1.5% linked quarter. Nonperforming assets remained low at 0.45% of total assets as of year-end. Our allowance for credit losses decreased to \$48.3 million for the linked quarter from \$48.5 million on September 30. Linked quarter, our allowance for loan losses as a percentage of total loans decreased 1 basis point to 0.94% at December 31.

During the fourth quarter, we continued restructuring a portion of our AFS securities portfolio that included sales of approximately \$82 million of lower-yielding, longer-duration municipal securities. Purchases of \$373 million, primarily mortgage-backed securities occurred during the fourth quarter to replace securities sold during the restructuring of the AFS portfolio during the third and fourth quarters. The purchases more than offset sales, maturity and principal payments, resulting in an increase in the securities portfolio of \$147.9 million or 5.8% to \$2.70 billion at December 31 when compared to \$2.56 billion on September 30.

The increase for the linked quarter brought the total securities portfolio to a level consistent with the first and second quarters of 2025. As of December 31, we had a net unrealized loss in the AFS securities portfolio of \$767,000, a decrease of \$14.7 million compared to \$15.4 million last quarter. The improvement occurred primarily due to the restructuring of the AFS portfolio and an improvement in the remaining AFS portfolio. There were no transfers of AFS securities during the fourth quarter.

On December 31, the unrealized gain on the fair value hedges on municipal and mortgage-backed securities was approximately \$788,000 compared to \$905,000 linked quarter. This unrealized gain more than offset the unrealized losses in the AFS securities portfolio. As of December 31, the duration of the total securities portfolio was 7.6 years compared with 8.7 years at September 30, and the duration of the AFS portfolio was 4.8 years compared to 6.5 years on September 30.

At quarter end, our mix of loans and securities was 64% and 36%, respectively, a slight shift compared to 65% and 35%, respectively, last quarter. Deposits decreased \$96.4 million or 1.4% on a linked-quarter basis due to a decrease in broker deposits of \$233.5 million, partially offset by an increase of \$40.8 million in retail deposits and an increase of \$86.3 million in public fund deposits. On February 15, we will redeem our \$93 million of subordinated notes due in 2030. The rate on the notes adjusted during the fourth quarter to a floating rate of 7.51%.

Our capital ratios remain strong with all capital ratios well above the threshold for well capitalized. Liquidity resources remained solid with \$2.78 billion in liquidity lines available as of December 31, and we purchased 369,804 shares of our common stock at an average price of \$28.84 during the fourth quarter.

There have been no purchases of our common stock since December 31, and we have approximately 762,000 shares remaining authorized for repurchase.

Our tax equivalent net interest margin was 2.98%, an increase of 4 basis points on a linked-quarter basis, up from 2.94% at the end of the quarter. Our tax equivalent net interest spread for the same period was 2.31%, an increase of 5 basis points from 2.26%. The increase in the net interest margin and net interest spread is primarily due to lower funding costs. For the 3 months ended December 31, we had an increase in net interest income of \$1.5 million or 2.7% compared to the linked quarter.

Noninterest income, excluding the net loss on the sale of AFS securities, increased \$494,000 or 4% for the linked quarter, primarily due to an increase in deposit services, BOLI income and brokerage services income, partially offset by a decrease in other noninterest income. Other noninterest income decreased primarily due to a decrease in swap fee income. Noninterest expense was \$37.5 million for the fourth quarter, consistent with the last quarter with a slight decrease of \$57,000.

Our fully taxable equivalent efficiency ratio decreased to 52.28% as of December 31 from 52.99% as of September 30, primarily due to an increase in total revenue. We have budgeted a 7% increase in noninterest expense in 2026 over 2025 actual, primarily related to salary and employment benefits, software expense, professional fees, retirement expense and a onetime charge of approximately \$800,000 in connection with the redemption of the subordinated notes on February 15.

During 2025, we budgeted for several software initiatives that did not materialize, and we have allocated those into the 2026 budget. For the first quarter of 2026, we anticipate noninterest expense of approximately \$39.5 million. We recorded income tax expense of \$3.8 million compared to \$189,000 in the prior quarter, an increase of \$3.6 million, driven by the loss on sales of AFS securities in the third quarter.

Our effective tax rate was 15.3% for the fourth quarter, an increase compared to 3.7% last quarter. And we are currently estimating an annual effective tax rate of 17.4% for 2026. Thank you for joining us today. This concludes our comments, and we will open the line for your questions.

Question and Answer

Operator

[Operator Instructions] Your first question comes from the line of Woody Lay with KBW.

Wood Neblett Lay

Keefe, Bruyette, & Woods, Inc., Research Division

I believe you just called out 7% expense growth is what you're budgeting in 2026. I was just hoping to get a little more detail and exactly how much of the incremental expense build is related to these software projects? And could you also talk about the hiring strategy and how that's built into the budget?

Keith M. Donahoe

CEO, President & Director

Yes. I'll hit it at a high level, and Julie can provide some details. So I don't have the breakdown in front of me on the expense between software and FTEs. But what's going -- what's really happening is on the software front, we are looking at moving our core to outlink. And so we're currently hosting on-premise, and we're going to take it off-premise. In the long run, we anticipate that to create some efficiencies for us as we move into -- expanded growth mode and/or if we make an acquisition, it's going to make that a more efficient prospect for us.

So that's part of it. We're also starting an initiative to build out a data platform, which we do believe will give us over time, much more insight into the raw data that we have in multiple systems right now. So those are the two biggest components of the software spend. From an FTE standpoint some of this is -- we hope will make us more efficient in the long run as well because we are changing some of our processes within the loan origination group.

And we are kind of wearing everybody thin right now. We're pumping high volume of loan growth through a system that probably wasn't ready for it yet. So we are making some personnel changes and shifting people around, which means also adding some staff in certain situations. So that's the bulk of what we're doing. Julie, if you've got any additional detail?

Julie N. Shamburger

Chief Financial Officer

I was just going to point out on the FTEs. Since December '23, our FTEs have been down about 6% actual number of FTEs. So that speaks somewhat to Keith's comments about adding some staff. Also, as far as numbers in the software and data processing, we've got about \$2.3 million, \$2.4 million additional in the budget over 2025 spend.

So I don't know if that answers your question, Woody, on the software and data processing, which is where combined, how it's reported in our -- all of our filings in the 10-Q and 10-Ks and earnings.

Wood Neblett Lay

Keefe, Bruyette, & Woods, Inc., Research Division

Got it. That's really helpful color. I appreciate that. Maybe a follow-up. You mentioned...

Julie N. Shamburger

Chief Financial Officer

I was just going to say the \$39.5 million that I forecasted, if you will, for the first quarter doesn't reflect a full 7% as these are not, all day 1 increases. We expect them to come in over the course of the year. So just wanted to add that color as well.

Wood Neblett Lay

Keefe, Bruyette, & Woods, Inc., Research Division

Yes. I appreciate that. And maybe a follow-up. You mentioned the core switch might help with M&A down the road. And I just wanted to get your thoughts on just given the deal activity we've seen recently in Texas, how you are thinking about M&A for Southside in this current environment?

Keith M. Donahoe

CEO, President & Director

Yes. It's still part of the strategy. We are open to discussions. Again, as I've told a lot of folks, we're not going to acquire just to acquire. We're going to be strategic, if it's filling out a geography for us and/or picking up -- we've got -- as an example, we've got only a loan production office in Dallas.

If we can find the right target in Dallas, that would be a good expansion for us because it would help us fill out the Metroplex. Same thing in Houston, we've got effectively a loan production office. We are opening a new retail location in the Woodlands, which should be opening in the next 60 days. But it's those target areas. And even in Austin with only two locations, if the right opportunity comes around, we are discussing those situations and are open to it. I hope that helps.

Operator

Your next question comes from the line of Michael Rose with RJ.

Michael Edward Rose

Raymond James & Associates, Inc., Research Division

Maybe we can just start on the margin. Obviously, the balance sheet restructure, the securities restructuring was smaller this quarter than last, but you are going to redeem the sub debt, as you mentioned. Just with those puts and takes and loan pricing competition, things like that, can you just give us some expectations on maybe what the first quarter margin could look like?

Keith M. Donahoe

CEO, President & Director

Yes. It's going to be positive, although it will be muted. I think we'll see a bigger pickup as we move through the rest of the year. We do have a onetime charge coming in the first quarter for the redemption. -- But directionally, it's going to be positive but -- and pick up towards the end of the year.

Julie N. Shamburger

Chief Financial Officer

From the standpoint of the sub debt, it repriced in the middle of the fourth quarter, and it's going to go away in the middle of the first quarter. So strictly with respect to the \$93 million, it's going to have about the same impact in the first quarter as it did in the fourth. But when those sources of funding are replaced in the second quarter, we'll certainly see -- we expect for sure to see some improvement just with respect to that one piece of funding. If that makes sense.

Michael Edward Rose

Raymond James & Associates, Inc., Research Division

Okay. Yes. No, that's -- thanks for the clarification Julie. I appreciate it. And then maybe as we just think about loan growth, I appreciate the comments at the beginning of the call just around some of the production and paydown activity. I know paydowns are really difficult to forecast.

But just given some of the investments that you've made in people and opening up new locations over the past few years, should we think about a higher level of production? It seems like the environment is pretty conducive for loan growth here. Just wanted to get a sense for how we should kind of think about at least on the production side as we move through the year.

Keith M. Donahoe

CEO, President & Director

Yes. From a production standpoint, I anticipate us to probably exceed '25, but we do have a large number of payoffs that are in our forecast, some of which are these construction projects that have stayed on our books longer than what they normally would as these projects are finished and stabilized occupancy comes around. So we've got a high number of those maturities happening this year. So we anticipate some of those moving out into the permanent market and/or sales.

So those are some of the headwinds that we're still facing. I'm excited because I was a little concerned that the pipeline dropped to \$1.5 billion in the middle of the fourth quarter, but we have rebounded strongly, and we're back up over \$2 billion now. Over half of that pipeline is in the very early stages, which means it hasn't run through our credit screening process.

But -- they're starting to move through. But we do have a significant number in the closing process right now. So I would love to tell you, I'm super optimistic that we may beat our numbers, but that right now, it's too early in the year to make that call. But we are very active across all of the markets, and I do anticipate it being a good year for us on the loan growth side.

Michael Edward Rose

Raymond James & Associates, Inc., Research Division

I appreciate it, Keith. And maybe just one final one for me. Obviously, the buyback stepped up a little bit this quarter. The restructuring is also a little bit smaller than the third quarter as well. But how should we think about kind of the pace of buybacks from here? You guys will have decent capital accretion as we kind of move through the year. Stock is still relatively attractive on a tangible basis. Just want to get your thoughts -- updated thoughts on the buyback.

Keith M. Donahoe

CEO, President & Director

Yes. I think from just a strategic standpoint, we're going to continue to be opportunistic with it. What may impact that is if there is an acquisition in the future. But at the same time, those are probably -- when you look at capital strategy, those are -- first, we've got the sub debt retirement is obviously the #1 capital strategy. Close behind that is stock buyback and then M&A. So we're all -- of that's going to work together, but -- and one of them may impact the other one, but we'll see how that goes this year.

Operator

Your next question comes from the line of Brett Rabatin with Hovde.

Brett D. Rabatin

Hovde Group, LLC, Research Division

I wanted to start off on just the fee income outlook from here. And it seems like brokerage has had some pretty good trends. I was just curious if there were any drivers you were specifically thinking about for '26 in terms of fee revenues? And then just any thoughts on the outlook for '26?

Julie N. Shamburger

Chief Financial Officer

Sure, Michael -- sorry, I'll take that one. We are expecting an increase in -- a pretty nice increase in our fee income. We've put in our budget about \$1.5 million for an increase. That's what we're budgeting. And a lot of it does come -- most of that does come in the trust income fees. We've -- I think we told you on the last couple of quarters that we have picked up some additional talent in that area, and we've built up a really strong team that we're excited about and are even looking to increase that team into the Fort Worth, North Texas area.

Right now, it's pretty much -- well, it is completely in East Texas and Southeast Texas areas of our market areas, but we are looking to increase it in the North Texas area. So we have budgeted additional fees there and looking for some additional increase in just treasury fees and as well in the brokerage services because we have seen some nice pickup in those two areas over the last year. And that's where most of the increase is coming from.

Brett D. Rabatin

Hovde Group, LLC, Research Division

Okay. That's helpful, Julie. And then I wanted to just go back to the securities portfolio and just are all the actions that you guys have anticipated played out from here? Is there anything else that you might want to do? Or is basically anything from here would be more opportunistic relative to rates changing?

Keith M. Donahoe

CEO, President & Director

Yes. For us, we're going to continue to be opportunistic with it. We're sitting here today, rates aren't in the right position for us to continue to make moves, if they do, and we're watching it. It's a daily process for us. And so if we're seeing the right signs, we will make those moves. But right now, we're in a holding pattern, if you will.

Brett D. Rabatin

Hovde Group, LLC, Research Division

Okay. And then maybe lastly, just you've talked a little bit about it on hirings. There's been quite a bit of M&A activity in Texas. I was just curious, Keith, any thoughts on that disruption, if that's an opportunity for you, maybe in the Dallas market, Fort Worth market with either people or clients? Is there anything that you're specifically targeting related to disruption?

Keith M. Donahoe

CEO, President & Director

Yes. We're seeing opportunity both from a people -- on the people side as well as customer side. We've been working on a couple of C&I opportunities in the Metroplex that are sort of being disrupted because of the acquisitions we're seeing. Obviously, the transaction that was announced yesterday in Houston, I think we could see some activity out of that, but it's too early to tell that we have our antenna up and we are looking, and we'll be looking for both customer displacement as well as employee displacement. So yes, we're active in that, and we'll continue to be so.

Operator

Your next question comes from the line of Jordan Ghent with Stephens.

Jordan Spencer Ghent

Stephens Inc., Research Division

I just wanted to ask a question on M&A kind of going back to that. How do you guys think about that as far as the target asset size and especially in relation to crossing \$10 billion?

Keith M. Donahoe

CEO, President & Director

Yes. I mean it still remains that we aren't going to buy something in the \$2 billion category. We would be below \$1 billion -- I mean, \$1.5 billion roughly. But if there's an opportunity that can spring us over that in a significant way, we will look at that as well. But as you know, in the state of Texas, when you start getting into the \$3 billion to \$5 billion range, those are fewer.

So there's more opportunities in the lower than \$2 billion market. And we're looking and if we can get one done that gets us close, then that helps us get to the point that we can spring over \$10 billion with a second transaction. So we're -- it's a little bit of a puzzle to put together, but we are looking at opportunities and continue down the same strategy that we've had in the last couple of years on that topic.

Jordan Spencer Ghent

Stephens Inc., Research Division

Okay. And then maybe just one follow-up question for Julie on the operating expense for that 1Q '26 number, the \$39.5 million, does that include that onetime charge? Or is that excluding that onetime charge of \$800,000?

Julie N. Shamburger
Chief Financial Officer

Yes, Jordan, it will include it.

Operator

There are no further questions at this time. I will now turn the call back to Keith Donahoe, President and CEO, for closing remarks.

Keith M. Donahoe
CEO, President & Director

Thank you, everyone, for joining us today. We appreciate your interest in Southside Bancshares and the opportunity to answer your questions. We're optimistic about 2026 and look forward to reporting first quarter results during our next earnings call in April. Thank you.

Operator

This concludes today's call. Thank you for attending. You may now disconnect.

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