S&P Global
Market Intelligence

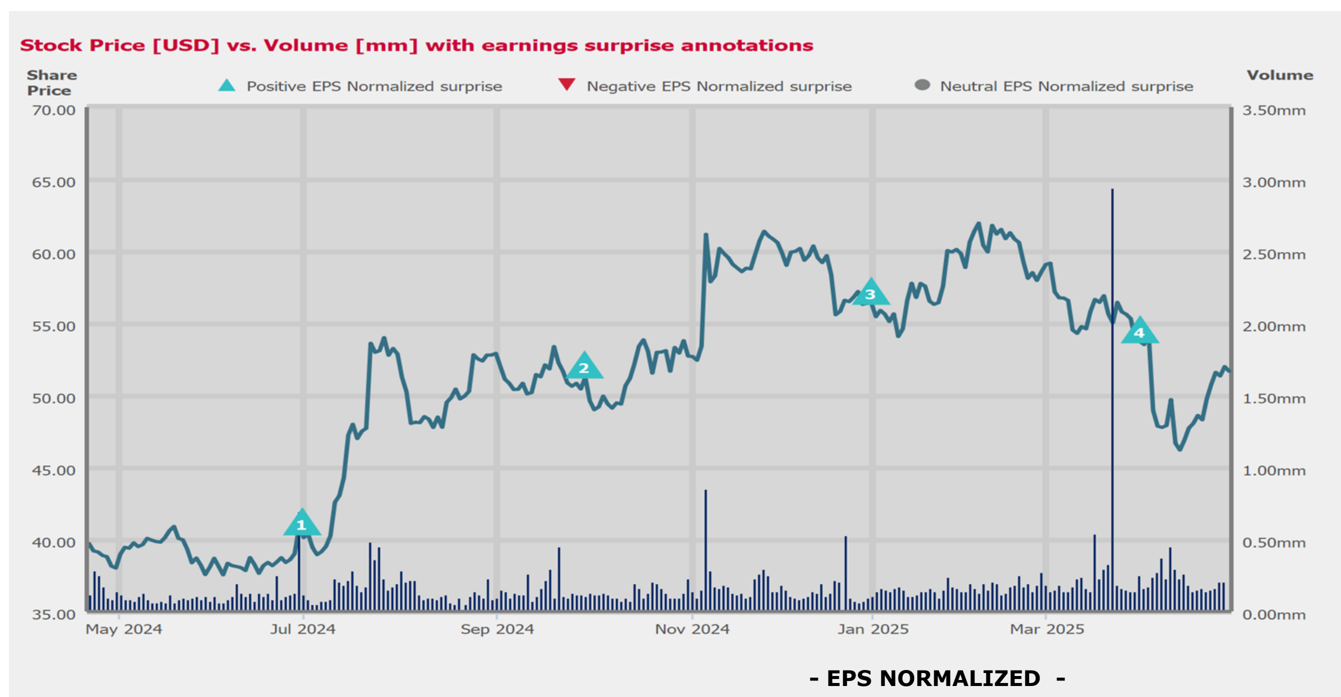
Enterprise Financial Services Corp NasdaqGS:EFSC
FQ1 2025 Earnings Call Transcripts

Tuesday, April 29, 2025 3:00 PM GMT

S&P Global Market Intelligence Estimates

	-FQ1 2025-			-FQ2 2025-	-FY 2025-	-FY 2026-
	CONSENSUS	ACTUAL	SURPRISE	CONSENSUS	CONSENSUS	CONSENSUS
EPS Normalized	1.17	1.31	▲11.97	1.12	4.65	5.21
Revenue (mm)	162.83	166.00	▲1.95	162.00	658.00	677.28

Currency: USD
Consensus as of Apr-29-2025 1:00 AM GMT



- EPS NORMALIZED -	CONSENSUS	ACTUAL	SURPRISE
FQ2 2024	1.06	1.21	▲14.15 %
FQ3 2024	1.14	1.29	▲13.16 %
FQ4 2024	1.16	1.32	▲13.79 %
FQ1 2025	1.17	1.31	▲11.97 %

COPYRIGHT © 2025 S&P Global Market Intelligence, a division of S&P Global Inc. All rights reserved
spglobal.com/marketintelligence

Table of Contents

Call Participants 3
Presentation 4
Question and Answer 9

COPYRIGHT © 2025 S&P Global Market Intelligence, a division of S&P Global Inc. All rights reserved

Call Participants

EXECUTIVES

Douglas N. Bauche
Senior EVP & Chief Credit Officer

James Brian Lally
President, CEO & Director

Keene S. Turner
Senior EVP & CFO

Scott R. Goodman
President

ANALYSTS

Andrew Brian Liesch
Piper Sandler & Co., Research Division

Brian Joseph Martin
Janney Montgomery Scott LLC, Research Division

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

David Joseph Long
Raymond James & Associates, Inc., Research Division

Jeffrey Allen Rulis
D.A. Davidson & Co., Research Division

Copyright © 2025 S&P Global Market Intelligence, a division of S&P Global Inc. All Rights reserved.

Presentation

Operator

Thank you for standing by. My name is Pam, and I will be your conference operator today. At this time, I would like to welcome everyone to the Enterprise Financial Services Corp. 1Q '25 Earnings Conference Call. [Operator Instructions]

I would now like to turn the conference over to Jim Lally, President and CEO. You may begin.

James Brian Lally
President, CEO & Director

Well, thank you, Pam, and good morning, everybody. Thank you all very much for joining us this morning, and welcome to our 2025 first quarter earnings call.

Joining me this morning is Keene Turner, EFSC's Chief Financial Officer and Chief Operating Officer; Scott Goodman, President of Enterprise Bank & Trust; and Doug Bauche, Chief Credit Officer of Enterprise Bank & Trust.

Before we begin, I would like to remind everybody on the call that a copy of the release and accompanying presentation can be found on our website. The presentation and earnings release were furnished on SEC Form 8-K yesterday, in addition to 2 other press releases that we'll be referencing in our remarks this morning.

Please refer to Slide 2 of the presentation titled Forward-Looking Statements and our most recent 10-K and 10-Q for reasons why actual results may vary from any forward-looking statements that we make this morning.

Our financial scorecard begins on Slide 3. 2025 is off to an exciting start for our company. In addition to strong financial results for the first quarter, yesterday, we announced the acquisition of 12 branches from First Interstate Bank, 10 of which are in our Arizona market, complementing very well, the focused commercial bank we have built over the last 15 years.

The strong financial performance that we have generated for the past several years continued into the first quarter of 2025. For the quarter, we earned $1.31 per diluted share, which compares favorably to the seasonally strong $1.28 that we earned in the linked quarter and the $1.05 that we earned in the first quarter of 2024. This level of performance produced an adjusted return on assets of 1.29% and a pre-provision ROAA of 1.71%. I would characterize our performance in the quarter as strong and consistent.

Net interest income and net interest margin both saw expansion in the quarter. NII came in at $1.1 million better than the previous quarter despite 2 fewer days in the quarter and represented the fourth consecutive quarter where we saw NII expansion. This reflects both better seasonal performance in our deposit balances and net interest margin expansion resulting from our relationship-oriented deposit base and our team's ability to provide value-added service to our customers that is well worth the extra few basis points when it comes to loan and deposit pricing.

Loan growth in the quarter was 3% or $78 million with active production across all of our markets and businesses. However, net growth was somewhat muted by 2 factors: the first was a sale of $30 million of SBA loans, and the second was the seasonal decline due to sales in loans in our tax credit business that totaled approximately $75 million.

Our diversified deposit base remains a differentiator for us. Typically, in the first quarter, it shows significant outflows due to the heavy concentration of commercial-oriented accounts. This year, absent the municipal relationship that we knew was exiting, our deposit flows were stable overall. We worked extremely hard to blunt this trend through growth of our national deposit verticals as well as through market and business diversification within both the commercial bank and our more granular business banking and consumer relationships. The composition of deposits also remained stable with DDA at 33%.

Copyright © 2025 S&P Global Market Intelligence, a division of S&P Global Inc. All Rights reserved.

These trends aided a continued reduction in the overall cost of deposits to 1.83%, a 17 basis point drop in the quarter.

Another strength of our company is our well-positioned balance sheet, which provides for great flexibility with respect to capital planning. Capital levels at quarter end remained stable and strong, with our tangible common equity to tangible assets ratio at 9.30%. Despite TCE well above 9%, we still delivered 14% return on tangible common equity for the first quarter.

Our strong return profile aided continued expansion in tangible book value per common share to $38.54, an annualized quarterly increase of 14%. Given the strength of our earnings and our confidence in our continued execution, we increased the dividend by $0.01 per share for the second quarter of 2025 to $0.30 per share and returned another $11 million to common shareholders in the quarter through share repurchases.

Additionally, we were able to utilize our demonstrated experience in M&A by further leveraging our excess capital through the strategic branch acquisition we announced. To complement our organic growth, yesterday, we announced our agreement with First Interstate Bank to acquire 10 branches in Arizona and 2 in Kansas City. With this purchase comes approximately $740 million of favorably priced commercially oriented relationship-based deposits and approximately $200 million of related commercial loans. This purchase is highly strategic and supports our growth strategy of expanding our strong positions in attractive markets.

The large majority of these loans and deposits are in Arizona, a market we know well and have had tremendous growth and success in recent years, and it provides us physical presence in the Southeast Valley of Phoenix, Pinal County as well as in Tucson. These locations and markets fit extremely well with the position we have built over the last 15 years in Arizona, and we're very excited to further our commitment to this market and to capitalize on a rare opportunity given the complexion of the banking landscape in Arizona.

This acquisition is a low-risk, shareholder-friendly way to leverage our proven strength in acquiring and integrating organizations. For us, this is a highly strategic fit for both the types of businesses and relationships that we bank and the types of employees who serve them well. This acquisition supports our objectives of growing our balance sheet to deliver top-quartile returns and consistently deliver compounding tangible book value. When completed, this opportunity will immediately leverage a modest amount of TCE in capital and will also produce attractive EPS accretion in 2026 and beyond. We anticipate closing and converting by the early fourth quarter of this year.

Before we discuss the performance of our markets and businesses, I would like to address the increase in NPAs in the quarter. This is related to several loans that are linked through a common ownership and located in our Southern California market. You need to know that we are well prepared for situations like this one, and I'm confident that this matter will be resolved favorably. Doug and our experienced resolution management team are personally involved in resolving this matter, and I anticipate that we'll receive full repayment of these loans. I remain highly confident in Enterprise's risk management process and in the strength of our loans and assets.

Now I'd like to turn the call over to Scott Goodman, who will provide an update on our performance in our markets and national businesses. Scott?

Scott R. Goodman
President

Thank you, Jim, and good morning, everyone.

Expanding a bit more on Jim's comments regarding loan production. Loan activity was generally healthy with originations for the quarter up nearly 40% from Q1 of the previous year. Loan balances by category are broken out on Slide 6, showing the net growth for the quarter and for the trailing 12 months.

Copyright © 2025 S&P Global Market Intelligence, a division of S&P Global Inc. All Rights reserved.

C&I growth for Q1 reflects continued success in attracting new relationships to the bank as well as ongoing M&A, capital investment and succession-related financing activity from our existing base of clients. Working capital lines also posted a modest increase in aggregate balances for the quarter.

We also continue to originate new investor commercial real estate opportunities growing by $82 million in Q1. Our emphasis in this category is on leveraging markets with the strongest economic profiles and supporting existing investor relationships that would also feature well-rounded deposit balances and fee income.

The specialty lending businesses generally continue to perform well and in line with seasonal expectations. Life insurance premium finance grew by $35 million for the quarter, mainly reflecting advances for premiums on existing policy loans, along with several new originations. This business continues on a steady growth trajectory, up 14% year-over-year. The SBA business is also performing well with originations tracking on plan and rate-induced payoff pressures trending down. Net of the aforementioned SBA loan sales growth was roughly $15 million in the quarter.

Loan balances and sponsor finance were level for the quarter as origination of new senior debt by private equity sponsors that was offset by paydowns from the sale of portfolio companies. Generally speaking, activity continues in this space, albeit at a slower pace as private equity weighs the impact of potential tariffs and interest rates on company valuations.

Activity in the tax credit business also continues in line with expectations with Q1 reductions, as mentioned by Jim, resulting from the impact of the seasonal paydown of project loans with tax credit sale proceeds. We still expect growth in this business for the full year of 2025.

Loans by region are broken out on Slide 7 with aggregate specialty lending balances reflecting my prior comments. Within the geographic regions, balances were down slightly in the Midwest, while posting growth in both Western and Southwestern regions. Our Midwestern markets of St. Louis and Kansas City experienced steady origination activity including new CRE loans for existing hospitality, industrial and multifamily clients. However, fundings were not sufficient to offset several larger paydowns tied to our continued managed rundown of the ag portfolio, client asset sales and a decision to move on from a larger C&I client whose leverage profile was shifting beyond our risk appetite.

The Southwest region posted $83 million or 19% annualized loan growth in the quarter, bolstered by continued fundings on construction projects as well as new originations on existing relationships in the Arizona market for medical office, self-storage and automotive services.

Our Western market of Southern California also had a strong quarter with $60 million or 13% annualized loan growth. New business included loans to refinance fully occupied medical and mixed-use properties in San Diego as well as a new relationship with a specialty finance company.

Moving on to deposits on Slide 8 and 9. Changes in the quarter within the core geographic portfolio reflect the typical seasonal decline in client balances of $303 million, mainly associated with distributions, bonuses and tax payments. A material portion of this reduction was offset by continued growth within the national deposit verticals, which grew $134 million or roughly 16% annualized in Q1. On a year-over-year basis, total client deposits, excluding brokered funds, are up 7.7%.

In general, the larger C&I portfolios within the Midwest and Western markets are most heavily impacted by the seasonal reductions, which typically then rebuild throughout the remainder of the year. We continue to perform well relative to retention of existing clients as well as adding new C&I relationships even as we proactively focus on gaining incremental margin in the pricing of loans and deposits. Our commercial teams are well-versed in reinforcing our key value drivers, particularly as we assist clients with strategic capital needs or target disrupted competitors.

The national deposit verticals profiled on Slide 10 continue to provide differentiated low-cost funding, while also diversifying our overall deposit base and somewhat softening the seasonality of our other channels. HOA had a particularly strong growth quarter associated with onboarding a significant number of new account relationships.

Copyright © 2025 S&P Global Market Intelligence, a division of S&P Global Inc. All Rights reserved.

Lastly, Slide 11 profiles the mix of our core deposit base, which continues to be well diversified and highly relationship-oriented with roughly 1/3 of these accounts being noninterest-bearing and 90% of them using some form of treasury management or online banking. They provide strong continuity and a solid base from which to expand other fee-generating revenue streams.

Now I would like to hand the call over to Keene Turner for his comments. Keene?

Keene S. Turner
Senior EVP & CFO

Thanks, Scott, and good morning, everyone.

Turning to Slide 12. We reported earnings per share of $1.31 in the first quarter on net income of $50 million. That's a $0.03 increase over the linked quarter for which earnings per share was $1.28. On an adjusted basis, earnings per share was relatively stable at $1.31 in the current quarter. Adjusted EPS excludes the impact of core conversion-related expenses and gains and losses on the sale of OREO and securities.

One of the highlights of the quarter was the increase in net interest income. Our disciplined pricing of loans and deposits benefited net interest income, along with growth in average loans and securities. These actions more than offset the impact of fewer days in the quarter and the repricing of variable-rate loans. Noninterest income was also strong to start the year, although it did decline from the fourth quarter, which is typically the highest quarter of the year.

The provision for credit losses decreased from the linked quarter due to lower growth in a net recovery on loans. As Jim noted, while nonperforming loans have increased due to the relationships in bankruptcy, we did not reserve for those loans as we fully expect to collect related balances. Noninterest expense was slightly higher in the quarter as a seasonal increase in compensation and benefits was mostly offset with the decrease in conversion costs related to the core system migration in the fourth quarter.

Turning to Slide 13 with more details to follow on 14. To me, the highlight of the first quarter is how well we were able to manage net interest income. First and foremost, we were able to mitigate 2 fewer days in the quarter. There isn't one single factor that led to this performance. However, we were able to largely replace seasonal deposit outflows to maintain the size of the balance sheet. For the last several quarters, the investment rate for securities has been favorable, and we've been adding to those balances in order to strengthen our earnings profile.

Also, from a business perspective, we have had success in repricing loans better than we had anticipated, while also improving the pricing on our deposit balances. The origination rate for new loans was 7.12% in the quarter, and we were able to drive deposit rates down another 10 basis points to 1.82% at the end of the first quarter. The combination of those factors has led to better than planned net interest margin in this first quarter. Starting off the year with a 4.15% net interest margin has set the stage for slightly stronger net interest income performance for 2025.

With that said, we do expect to see modest erosion of margin during this year. With recent variability in interest rates in recent weeks, it's difficult to assume that we would face the same strength in reinvestment rates throughout 2025. However, we will continue our efforts to mitigate expected pressure on net interest margin with continued discipline on pricing performance on both sides of the balance sheet. As for net interest income dollars, day count is now in our favor for the remainder of 2025.

Slide 15 reflects our credit trends. We had a net recovery of $1.1 million compared to net charge-offs of $7.1 million in the linked quarter. The provision for credit losses declined to $5.2 million in the period compared to $6.8 million in the linked quarter due to changes in loan growth and the net recovery.

Nonperforming assets were 72 basis points of total assets compared to 30 basis points at the end of the year. The temporary increase in the nonperforming asset ratio was primarily related to 2 relationships with common general partners that went into bankruptcy due to a business dispute. We are well secured with collateral and individual guarantees and fully expect to collect each of the underlying loans, and we expect NPAs to return to normalized level in the next couple of quarters.

Copyright © 2025 S&P Global Market Intelligence, a division of S&P Global Inc. All Rights reserved.

Slide 16 presents the allowance for credit losses. The allowance for credit losses represents 1.27% of total loans or 1.38% when adjusting for government guaranteed loans. Of note, we moved allowance to total loan coverage up slightly to further reflect potential for erosion of economic conditions.

On Slide 17, first quarter noninterest income of $18 million included a $1.9 million gain on the sale of SBA loans. This helped partially offset the decrease in tax credit income from a seasonally high fourth quarter. Depending on levels of planned growth and activity in the SBA space, we may take the opportunity to sell more SBA loans as the year progresses.

Turning to Slide 18. Noninterest expense of $99.8 million increased less than $1 million from the fourth quarter. The increase was primarily in compensation and benefits due to seasonal payroll tax impacts and merit increases that went into effect on March 1. These increases were offset by the $1.9 million in core conversion costs in the fourth quarter that did not reoccur.

Deposit costs were relatively stable as well, reflecting the strength of the average balances offsetting improvement in the earnings credit rate. Core efficiency improved to 58.8% compared to 57.1% for the linked quarter -- sorry, efficiency increased, not improved.

Our capital metrics are shown on Slide 19. We are executing our disciplined capital allocation strategy, evaluating various opportunities, including share repurchases and M&A with focus on creating shareholder value. We repurchased 192,000 shares at an average price of $55.28 for approximately $11 million of capital return. We have approximately 1.2 million shares remaining outstanding under our current repurchase plan. Our tangible common equity ratio was 9.3%, up from 9.1% in the linked quarter. On a per-share basis, tangible book value was up by 14% on an annualized basis to $38.54. We also increased our quarterly dividend by $0.01 to $0.30 per share for the second quarter of 2025.

I'll echo Jim's comments, we started the year with a lot of momentum. Our earnings profile is strong, the balance sheet is strong, and we're adding further to our earnings and growth profile with the strategic branch acquisition that Jim outlined. We believe that combined with our differentiated commercial relationship model, we will continue to deliver top-tier financial performance for the foreseeable future.

I appreciate your attention today, and I'll turn it back to Jim before we open the line for Q&A.

James Brian Lally
President, CEO & Director

Thank you, Keene. In addition to the announcement regarding our Arizona and Kansas City expansion, yesterday, we also announced that Scott Goodman has decided to transition to a part-time nonmanagerial role as part of our orderly succession planning process and thus will step down from his position as President of Enterprise Bank & Trust later this year. Thankfully, Scott has decided to stay with the company as a strategic adviser to me, while also working with our teams and our most important clients.

Subsequently, Doug Bauche will be promoted to the newly created role of Chief Banking Officer, where he will lead all of our commercial, specialty and business banking businesses. Kevin Handley, a 30-year industry veteran, the last 7 with Enterprise, will succeed Doug as our company's Chief Credit Officer. These moves will all be effective later this year and we are well positioned with our succession planning preparation to ensure a smooth transition.

I would like to publicly acknowledge and thank Scott for his tremendous contributions that he's made to our company over the last 23 years, the last 12 as President of Enterprise Bank & Trust. We would not be the successful organization that we are without his great leadership and strategic guidance. I also like to congratulate Doug and Kevin on their promotions and look forward to working closely with them in their new roles.

Lastly, I would like to thank all of our enterprise associates for their hard work and dedication to serving our clients every day.
With that, I would now like to open the line for questions.

Copyright © 2025 S&P Global Market Intelligence, a division of S&P Global Inc. All Rights reserved.

Question and Answer

Operator

[Operator Instructions] And your first question comes from the line of Jeff Rulis with D.A. Davidson.

Jeffrey Allen Rulis
D.A. Davidson & Co., Research Division

Any of the terms of the branch deal that you're willing to disclose? Was this cash? Just trying to get a sense for the purchase price.

Keene S. Turner
Senior EVP & CFO

Yes, Jeff, it's an assumption, right? So we're bringing on roughly net $450 million of cash that largely, after the loans, we'll invest in securities at, call it, a 5% rate. So all in all, I think we expect the deal pro forma comes on at a similar to slightly improved margin. It will further -- the balance sheet at this point is pretty neutral when you factor in ECR and tax credit. So it'll have a chance that if we would like to, making net interest income more neutral or the balance sheet slightly liability-sensitive overall. And then expenses kind of come in from a run rate perspective in the low 50%. So call that 52% to 54%. So modeled pretty conservatively in terms of what we announced for the accretion and you sort of start with mid-single-digit EPS accretion, and that improves as you assume you lend out some of the securities over time.

Jeffrey Allen Rulis
D.A. Davidson & Co., Research Division

And maybe just to follow on, the expectation for pro forma capital levels post close and then does that -- would that alter, I guess, in the interim or even after kind of the buyback or other M&A appetite, just more on the capital side?

Keene S. Turner
Senior EVP & CFO

Yes. I would say, Jeff, pro forma capital is right at our targets, which is good. Of note, we did not execute the call on our sub debt, given equity market valuations. We've got a senior piece lined up if we want to replace that. So I think we can continue to be modestly offensive with share repurchases in these next couple of quarters here in addition to the transaction. Given the risk-weighted asset profile, low risk-weighted assets, we've got a lot of leverage ratio to give, and it doesn't materially impact total capital ratio or risk-based ratio. So I feel like there's an opportunity to continue to do a little bit of all of the above.

Jeffrey Allen Rulis
D.A. Davidson & Co., Research Division

Got it. And one final one, if I could. I believe the Arizona piece of that, what was the old Great Western had some dairy exposure. Any comments on -- maybe that's runoff. And it's a pretty diminish amount on a relative sense. But just sector-wise, was there any industry exposures up from the loans brought over, again, just $200 million?

James Brian Lally
President, CEO & Director

Jeff, this is Jim. We had the opportunity to really look at what's attractive to us. And so we're not picking up any dairy exposure in this transaction.

Operator

Your next question comes from the line of Andrew Liesch with Piper Sandler.

Copyright © 2025 S&P Global Market Intelligence, a division of S&P Global Inc. All Rights reserved.

Andrew Brian Liesch
Piper Sandler & Co., Research Division

Just kind of sticking with the theme of the deal here. Just curious if you kind of model out some of the book value dilution that's going to come, how quickly you can earn that back.

Keene S. Turner
Senior EVP & CFO

Yes, Andrew, relative risk/reward, it's -- some of it depends on how quickly we lend it out. I think as I noted, our assumptions are fairly conservative both in the amount of employees that will stay on and will grow with us and then we have also planned some additions to the market in the run rate there. So let's just say that if share repurchases are a 5-year earn-back and a full bank M&A is 3, it's way closer to the 3 than the 5.

Andrew Brian Liesch
Piper Sandler & Co., Research Division

Got it. Okay. That's helpful. And then just on organic loan growth. Obviously, some portfolios is a little bit stronger here in the first quarter and some optimism for certain types as we move on through the year. But I mean, how are you looking at loan growth for 2025, given that this rate wasn't all that strong in the first quarter overall?

James Brian Lally
President, CEO & Director

Yes, Andrew, I'll look at it this way. So we really focus on balance sheet growth, first and foremost. And I'm not going to shy away from that mid-single-digit growth for that. Given some of the uncertainty in the economy and what have you, we certainly have been out talking to our clients, and they're not quite sitting on their hands, but they are waiting and seeing what's going on out there. So we had thought maybe we'd see the lift in the second half of the year, and that may bleed to 2026. But nonetheless, we're out attracting new relationships, growing the balance sheet, doing it the right way. And to the extent that something breaks free and relative to the U.S. trade partners that then avails us to the appropriate loan growth, we'll seize it.

Operator

Your next question comes from Damon DelMonte with KBW.

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

Hope everybody is doing well today. Just a question on the margin and the outlook. Keene, I think you noted that the margin is likely to trend lower here in the coming quarters. But can you kind of help us think about NII outlook there and your ability to kind of defend current levels even though the margin will be coming down?

Keene S. Turner
Senior EVP & CFO

Yes. Damon, I would say the only thing that really changed with margin is my comments around the sub debt that flips to variable rate here in the quarter and has a pretty double-digit or near double-digit rate versus we were planning on replacing that with senior. And I think that's a short-term trade for long-term capital management opportunity that exists. So I'd say that we expect margin to potentially step down maybe 5 basis points sequentially in the quarter. But all of my margin from here on out in a 5-quarter look is stable, and that's got 75 basis points of Fed fund cuts in it. And absent the transition from 4Q to 1Q '26 on day count, net interest income dollars grows quarterly, whether we grow the balance sheet a whole lot or not.

Copyright © 2025 S&P Global Market Intelligence, a division of S&P Global Inc. All Rights reserved.

So I think we feel pretty good about that. And just worth pointing out, when we look at it inclusive of noninterest expense, we're pretty neutral to slightly positive. So it depends on how some of those balances and complexions move, how the -- what part of the curve is moving. But I think we've done a pretty good job of neutralizing out the curve. And I think when you look back 1Q '24 versus current quarter, pretax pre-provision revenue contribution is fairly stable when you neutralize tax credit. So I think we feel pretty good about that. And obviously, the branch transaction, as we noted, gives us a chance to further improve the balance sheet flexibility and net neutrality of it as we move forward.

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

Got it. That's helpful. And then could you just kind of help us think about like the quarterly cadence for expenses? I know obviously, the branch transaction comes on in the fourth quarter. But if you look at the level of the first quarter, kind of deposit costs were a little bit higher and comp and benefits were higher for the start of the year. But how do we kind of think about that quarterly cadence?

Keene S. Turner
Senior EVP & CFO

Yes. I think we didn't have any rate moves here in the quarter. So the earnings credit rate improved, but we continue to have good success in that business. So that -- the deposit costs will probably grow in line there. And I expect we typically trade merit for seasonal payroll 1Q to 2Q, maybe inclusive of some working day stuff. So I don't think I have a really assertive improvement in run rate. But to the extent that we continue to grow the balances in the deposit verticals, that will grow net interest income dollars and will largely offset or slightly improve profitability.

So there's really no big move coming. We will have, what I'll say, is fairly material transaction-related expense on legal and those types of things in the coming quarters, but we'll point those out. Those aren't a huge item here with the type of the transaction.

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

Okay. And then did you say that the kind of efficiency ratio of the branch operations that you're taking on are like the 52% to 54% range. So from that, we can kind of back into what the expense impact is.

Keene S. Turner
Senior EVP & CFO

That's correct. There's a minimal amount of fees that are -- that we expect to recur with the branches. So it's largely margin and expenses. So more in line with our traditional branch-only core banking efficiency ratio and then obviously, the deposit verticals add to that a little bit. So yes, that's 52% to 54% depending on how everything settles out.

Operator

Your next question comes from David Long with Raymond James.

David Joseph Long
Raymond James & Associates, Inc., Research Division

You mentioned -- Keene, you mentioned that a little bit of pressure on the NIM here in the second quarter, but then thereafter, even with 75 basis points of rate cuts, did you say NIM still stable in that environment?

Keene S. Turner
Senior EVP & CFO

Yes, I would say generally. We've had good success in repricing deposits here. The early data is fairly in line with what the results were and slightly better than we had modeled. And as the time passes, David, when we get repricing of CDs and things like that, we expect that, that will improve to sort of

Copyright © 2025 S&P Global Market Intelligence, a division of S&P Global Inc. All Rights reserved.

the maximum data that we have when rates were rising. So those things help to stabilize margin as do the proactive steps we took on boosting the size of the investment portfolio and getting some durable earnings there. So we feel pretty good about stable margin. And I would say the margin declination that I referred to is self-inflicted, but an opportunity to manage the share count and equity part of the capital stack here in the coming couple of quarters.

David Joseph Long
Raymond James & Associates, Inc., Research Division

Got it. Great. No, I appreciate that color. And then on the credit side of things, Keene, I think you called these new nonperforming loans temporary. What is the timing of the process to exit these credits? Or what's your best guess on how that plays out to exit those without any losses?

Douglas N. Bauche
Senior EVP & Chief Credit Officer

Yes. David, it's Doug Bauche. I'll comment on that. And listen, due to the bankruptcy, I think it's difficult for us to predict the specific timing of the resolution of these particular loans. I think what we can just do is kind of reiterate, right, our position that we're in today relative to loan to values and recourse to these sponsors and our confidence to be able to collect. I can tell you, David, I went out, personally visited each and every one of these properties. And then we've, of course, engaged independent third-party appraisals that we just got here in March.

So listen, absent a dispute, these properties, these loans would be well performing. They're occupied. They're well positioned. They're in a very attractive Laguna Beach market. So this dispute was unforeseen. It's unfortunate. But we'll have to let things play out here in the bankruptcy proceedings and in due process, due time, I think we're going to have a very favorable outcome.

Operator

[Operator Instructions] And our next question comes from Brian Martin with Janney.

Brian Joseph Martin
Janney Montgomery Scott LLC, Research Division

Keene, it sounds like just fair to say, given your -- the outlook on margins, just even into next year, if we're kind of thinking about things where rates are and maybe a couple of cuts here and the margin is still well above 4% in terms of even longer term than kind of the near-term comments you've made. Does that seem fair based on kind of the positioning of the balance sheet and kind of your rate outlook today?

Keene S. Turner
Senior EVP & CFO

That is accurate.

Brian Joseph Martin
Janney Montgomery Scott LLC, Research Division

Got you. Okay. Perfect. And then just in terms of the pro forma cap, I think you said with the transaction, where is your expectation in terms of where the TCE lands in the fourth quarter? I think -- I don't remember if you said what that was.

Keene S. Turner
Senior EVP & CFO

Yes. Brian, it's going to be dependent on how much we're after the common stock, but sort of 8.5% is where we think it is. It leverages TCE roughly 100 basis points and the other capital ratio is sort of around the same amount, just slightly under. So we think it's a really nice way to rightsize capital and also strategically expand the business and add to EPS, all that stuff. So -- and that's, in my opinion, with where we're seeing pricing and opportunities gives us a chance to still manage some share count.

Copyright © 2025 S&P Global Market Intelligence, a division of S&P Global Inc. All Rights reserved.

Brian Joseph Martin
Janney Montgomery Scott LLC, Research Division

Yes. Okay. Got you. And I think did -- you said you also sold some tax credit loans in the quarter. Was that...

James Brian Lally
President, CEO & Director

No, Brian. Let me explain this. This is Jim. In normal course of business, what happens, there's significant sales of the credits in the fourth quarter, which then comes in the cash comes to pay down the loans. And so that's just part of the seasonal flow of the business.

Brian Joseph Martin
Janney Montgomery Scott LLC, Research Division

Okay. I guess -- okay. So that's just the normal course of business. The timing was...

James Brian Lally
President, CEO & Director

Yes. And given the size of the portfolio and where many of these projects are in process, that will rebuild over the rest of this year. This is a seasonal decline. If we're rebuilding, as Scott mentioned in his comments, we'll see growth in that business throughout 2025.

Brian Joseph Martin
Janney Montgomery Scott LLC, Research Division

Got you. And then we see a similar pattern next year maybe when you -- and you execute in the fourth quarter, we'll see a follow-through in the first quarter with maybe a little bit of a drift down like we did this quarter.

James Brian Lally
President, CEO & Director

That is exactly right.

Brian Joseph Martin
Janney Montgomery Scott LLC, Research Division

Got you. Okay. And I think, Keene, I don't know maybe, I'm not sure who said it, but as far as building the reserve this quarter, that's just uncertainty with regard to the tariffs. I mean it certainly wasn't the credits you talked about this quarter, but just trying to understand what was driving the reserve build this quarter and thinking about that.

Keene S. Turner
Senior EVP & CFO

Yes. Well, tariffs very clearly happened in the second quarter. So I think there just started to be a lot of turbulence as we looked at the forecast and we're always more weighted towards the downside in our qualitative reserves. And so it just felt like overall, from a trend perspective that we didn't want to miss an opportunity here with a strong earnings quarter to be a little bit more conservative in the overall reserve level.

So we're -- we think that's the right position to be in here, and we'll continue to evaluate it at the end of the second quarter and to the third quarter and just make sure that with the balance sheet and the earnings profile, we also are putting things away for reserves if the economy looks like it's starting to cloud up a little bit.

Brian Joseph Martin
Janney Montgomery Scott LLC, Research Division

Copyright © 2025 S&P Global Market Intelligence, a division of S&P Global Inc. All Rights reserved.

Yes. Okay. And did you give, Keene, the expense add from branch deal? Or do you have a ballpark of what that is? If not, we can -- I'll take a look at what your comments were earlier.

Keene S. Turner
Senior EVP & CFO

I didn't. I gave an efficiency ratio. I said it was like 52% to 54% marginal efficiency on the modeled net interest income and the margin on the assets coming over was roughly in line with expected margin at closing. So as we get closer here, I'll give you a sort of line item details. But for right now, I think that should get you pretty close to the mid-single-digit 2026 accretion. And for the year, you'll have a little bit of earnings in the fourth quarter from the opportunity, but it -- and it probably outearns the one time costs modestly in 2025.

Operator

There are no more questions. I will now turn the conference back over to Jim for closing remarks.

James Brian Lally
President, CEO & Director

Thank you, Pam, and again, thank you for all of you joining the call this morning. I appreciate your interest in our company, and we'll talk with you at the end of the next quarter. Have a great day.

Operator
Ladies and gentlemen, that concludes today's call. Thank you all for joining. You may now disconnect.

Copyright © 2025 S&P Global Market Intelligence, a division of S&P Global Inc. All Rights reserved.

Copyright © 2025 by S&P Global Market Intelligence, a division of S&P Global Inc. All rights reserved.

These materials have been prepared solely for information purposes based upon information generally available to the public and from sources believed to be reliable. No content (including index data, ratings, credit-related analyses and data, research, model, software or other application or output therefrom) or any part thereof (Content) may be modified, reverse engineered, reproduced or distributed in any form by any means, or stored in a database or retrieval system, without the prior written permission of S&P Global Market Intelligence or its affiliates (collectively, S&P Global). The Content shall not be used for any unlawful or unauthorized purposes. S&P Global and any third-party providers, (collectively S&P Global Parties) do not guarantee the accuracy, completeness, timeliness or availability of the Content. S&P Global Parties are not responsible for any errors or omissions, regardless of the cause, for the results obtained from the use of the Content. THE CONTENT IS PROVIDED ON "AS IS" BASIS. S&P GLOBAL PARTIES DISCLAIM ANY AND ALL EXPRESS OR IMPLIED WARRANTIES, INCLUDING, BUT NOT LIMITED TO, ANY WARRANTIES OF MERCHANTABILITY OR FITNESS FOR A PARTICULAR PURPOSE OR USE, FREEDOM FROM BUGS, SOFTWARE ERRORS OR DEFECTS, THAT THE CONTENT'S FUNCTIONING WILL BE UNINTERRUPTED OR THAT THE CONTENT WILL OPERATE WITH ANY SOFTWARE OR HARDWARE CONFIGURATION. In no event shall S&P Global Parties be liable to any party for any direct, indirect, incidental, exemplary, compensatory, punitive, special or consequential damages, costs, expenses, legal fees, or losses (including, without limitation, lost income or lost profits and opportunity costs or losses caused by negligence) in connection with any use of the Content even if advised of the possibility of such damages. S&P Global Market Intelligence's opinions, quotes and credit-related and other analyses are statements of opinion as of the date they are expressed and not statements of fact or recommendations to purchase, hold, or sell any securities or to make any investment decisions, and do not address the suitability of any security. S&P Global Market Intelligence may provide index data. Direct investment in an index is not possible. Exposure to an asset class represented by an index is available through investable instruments based on that index. S&P Global Market Intelligence assumes no obligation to update the Content following publication in any form or format. The Content should not be relied on and is not a substitute for the skill, judgment and experience of the user, its management, employees, advisors and/or clients when making investment and other business decisions. S&P Global Market Intelligence does not act as a fiduciary or an investment advisor except where registered as such. S&P Global keeps certain activities of its divisions separate from each other in order to preserve the independence and objectivity of their respective activities. As a result, certain divisions of S&P Global may have information that is not available to other S&P Global divisions. S&P Global has established policies and procedures to maintain the confidentiality of certain nonpublic information received in connection with each analytical process.

S&P Global may receive compensation for its ratings and certain analyses, normally from issuers or underwriters of securities or from obligors. S&P Global reserves the right to disseminate its opinions and analyses. S&P Global's public ratings and analyses are made available on its Web sites, www.standardandpoors.com (free of charge), and www.ratingsdirect.com and www.globalcreditportal.com (subscription), and may be distributed through other means, including via S&P Global publications and third-party redistributors. Additional information about our ratings fees is available at www.standardandpoors.com/usratingsfees.
© 2025 S&P Global Market Intelligence.

Copyright © 2025 S&P Global Market Intelligence, a division of S&P Global Inc. All Rights reserved.