17-Nov-2020

Regions Financial Corp. (RF)

Stephens NASH Investment Conference

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MANAGEMENT DISCUSSION SECTION

Terry McEvoy
Analyst, Stephens, Inc.

Great. Good afternoon, everyone. Let's get started with our next fireside chat with Regions Financial. Regions is headquartered in Birmingham, Alabama, ranked 17th in the US in terms of deposits. As it relates to markets, Regions has the top five or better market share in 70% of the MSAs across their 15-state footprint and 60% of these MSAs are projected to grow faster than the US national average. Assets at the end of last quarter totaled $145 billion.

With us today from Regions we have David Turner, CFO; Barb Godin, Deputy Chief Risk Officer and Chief Credit Officer; Martha Raber, Head of Financial Risk; Ronnie Smith, Head of Corporate Banking; Deron Smithy, Treasurer; and Anil Chadha, Head of Shared Risk Services & Analytics.

Before turning it over to David, I'd really like to encourage anyone who would like to ask a question to use the feature on the left side of your screen that will forward your questions directly to me, and I will do my best to get them asked and answered over the next 45 minutes.

So with that, I know David has some opening remarks, so I will turn it over to David.

David Jackson Turner
Chief Financial Officer & Senior Executive Vice President, Regions Financial Corp.

Okay. Terry, thank you. I appreciate you putting this on and everybody attending. Talk a little bit about kind of where we are. As we look at our footprint and looking at our customer base and kind of what's going on, clearly, COVID cases increasing caused us to pause a bit. But when we look at activity and we talk to people, activity is

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still quite robust. Our customers are in pretty good shape. And they're looking to make investments to grow their business, but there are some uncertainties that they want to get addressed.

One, it was the election. So the fact that we have the election, at least, executive branch dealt with and we'll get the Senate dealt with in January, the next is really COVID and the vaccine as far as all this volatility is, what's really going on with COVID and can we get that under control? And there is a lot of pent-up excitement, if you will, about businesses growing once that uncertainty gets removed. For us, we expect the Fed to be accommodative. We expect the economy to grow slowly. We expect rates to be low for an extended period of time.

We anticipated that a couple of years ago and entered into our hedging program, which we can talk about later on. But it is a differentiator for us. It added some $95 million to NII this past quarter. It will add $95 million-$97 million in the next quarter. It will be roughly at that level for the next few years. So we're excited about that. We all know we would like to have robust loan demand. We are seeing production quite nicely, but our line utilization continues to be at historical lows. And again, part of that is just uncertainty. So we can get that removed, we think we can get some draws there.

Our NII has done a little better than we had anticipated because our deposit growth has been extraordinary, and that's been in all three of our segments, retail, wealth and commercial, with commercial being the biggest single driver. And that's really proceeds that are generated by these businesses that just aren't being put to work. They're being put on deposit with us. Our NIR has done very well, driven in large part by an outperformance in mortgage.

We do continue to experience more of a purchase shop than many, so our production is really about 50% refi, 50% purchase, and that's been extremely strong. We think our production this year will be twice of what it was last year. So we are expecting the fourth quarter to be strong. And we think 2021 will be strong because we expect rates to be low, and you're going to see purchase activity continue, we suspect.

Service charges, still aren't where we were pre-pandemic, primarily because of NSF fees, that's the largest single driver. And that's really driven by cash sitting in the accounts of our customers through stimulus payments. We think our customers are really watching how they spend. So we see debit spend being actually little slightly ahead of where we were last year. Credit spend is still behind, but nonetheless, reasonably robust. Our card and ATM fees are actually ahead of where we were a year ago.

Capital markets continues to do well. There is volatility in that business. But net-net, they've done a good job, and wealth has continued to grow as well. Our goal has been on expense management to try to keep our expenses relatively stable, while making investments in technology and people to grow our business. We've been pretty successful in doing that. And we're going to continue to do that. We're not going to give you 2021 guidance, even though we'll get five questions today about it. But we're going to try and see if we can keep expenses relatively stable as we have year-over-year.

Credit, we'll talk a lot about credit today, I'm sure. But credit continues to perform slightly better than what we originally thought. But there's still uncertainty with regards to credit that I think we all need to be cautious of. We expect charge-offs – also we'll have charge-offs next quarter. We've given you a little bit of a range as to what we expect that to be this next quarter. And what provision looks like is really going to be dependent on the mix of the loan portfolio, macroeconomic variables. And we can talk more about that if you want.

Capital continues to grow for us. We were up about 40 basis points in the third quarter, as you saw. And we're looking to continue to build that to that 9.5% to 10% range on common equity Tier 1. And then after that,

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hopefully, we can control our capital. We'd like to put it to work organically, pay a dividend, non-bank acquisitions like Ascentium, and then buying shares back if we – just as our toggle to keep that capital ratio down. So obviously, not allowed to do that today, but hopefully after this fourth quarter's stress test, we'll get a little bit more leeway in understanding as to whether our regulatory supervisors will allow us to do.

So I'll stop there, Terry, and open it up for your questions or anybody on the call.

QUESTION AND ANSWER SECTION

Terry McEvoy
Analyst, Stephens, Inc.

Q

Thanks for that, David. We'll just start with a few questions that really are coming from yesterday's news. The Southeast no stranger to bank M&A. SunTrust-BB&T is still working through their integration, and now yesterday's news of PNC and BBVA. So I guess the question is could you talk about how Regions has positioned itself [ph] after more (00:07:22) disruption over the years? What's been the result? And then what opportunities do you see coming out of yesterday's news recognizing that it's a little more than 24-hours old?

David Jackson Turner
Chief Financial Officer & Senior Executive Vice President, Regions Financial Corp.

A

Well, one – so the deal was actually announced yesterday. We suspected given the capital and cash position of PNC that they were looking at something. And we suspected it needed to be reasonably sizable, and of course, now we know it's BBVA. We have a lot of respect for PNC and BBVA. We compete with both of them, just as we competed with SunTrust and BB&T. And in both cases, we are going from two competitors to one competitor.

There's also – when you do M&A, there's a lot of disruption. And with that disruption comes opportunities to pick up people and to pick up producers to pick up customers from time-to-time as well. So they are in our footprint. We are not going to just stand by and let it happen. We're going to be out there beating the bushes like we do every day to try and grow our customer base. And we think there are going to be opportunities. We saw and it happened in the Truist merger and we think it's going to happen here as well.

Terry McEvoy
Analyst, Stephens, Inc.

Q

And then maybe one more question on that topic before we move on. Just certain of your peers are pursuing or at least talking about more national strategies right now, so what are your thoughts on building out a more national franchise versus building more density within your current markets?

David Jackson Turner
Chief Financial Officer & Senior Executive Vice President, Regions Financial Corp.

A

Yeah. So in our 15 states, we've talked about M&A and kind of how we think about it. Of course, our number one focus has been on organic growth and it continues to be. We have a good strategic plan that is focused on organic growth. And our expectation is if we'll execute against that plan, then we can get a currency that maybe puts us in position to take advantage of opportunities if they arise in the bank space later on. In a low-growth environment, low-rate environment, low-revenue growth environment, M&A has a tendency to pick up. We understand that. And as a result, we've tracked targets that we would like to look at.

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We think of M&A from a strategic standpoint being not just the financial playing cost saves but what are you going to do with the customer base? Does it starting with the right side of the balance sheet? What's the deposit franchise look like? And what we have found is when you have density in markets, density allows you to command, have a commanding presence in those markets, allows you to get the first bite at the apple, allows you to attract new customers when they migrate in. So for us, M&A in the existing footprint to get more dense would be more important to us than a coast-to-coast national-type franchise at this point.

Terry McEvoy
Analyst, Stephens, Inc.

Q

Thank you. And we'll move on here. And maybe just a point of clarity. The net charge-off outlook, 40 to 65 basis points, is that the current view for the fourth quarter for 2021 or more of a longer term range? I know I had some questions last [ph] year at (00:10:46) a similar event, I was just hoping just to clarify that please.

Barbara I. Godin
Senior Executive Vice President, Deputy Chief Risk Officer and Chief Credit Officer, Regions Financial Corp.

A

Yeah. It's Barb. Let me let me clarify that. What I meant by that in the question that preceded it was that at Investor Day, back in 2019, what do we think the loss range would be. That's what we quoted. And in fact, our losses came in 43 basis points for 2019, et cetera. We're looking at 2021 as being part of that three-year cycle. We're saying if you average that three-year cycle, between that 40 and 65 basis points. So you're going to have some quarters that are high. You're going to have some years that are higher than others. But on average, for the three years ending at the end of 2021, somewhere between 40 and 65 basis points.

Terry McEvoy
Analyst, Stephens, Inc.

Q

Thanks. So with that understanding around charge-offs, you mentioned in the past that ultimately the reserve should get back to that day one ratio, call it, 1.7%. And so, the question is what do you need to see to return to that more normal day one level to help us understand kind of the timeframe for when the ACL normalizes?

Barbara I. Godin
Senior Executive Vice President, Deputy Chief Risk Officer and Chief Credit Officer, Regions Financial Corp.

A

Anil, why don't you go ahead and answer that?

Anil Chadha
Executive Vice President-Head of Shared Risk Services & Analytics, Regions Financial Corp.

A

Sure. I'll be glad to. So there's two primary factors you need to think about with respect to when do you return back to more of a day one-type allowance. The first is charge-offs and the timing of it, which says charge-offs occur. So we've guided that we expect, like many do, that charge-offs will peak in mid-2021, and then there'll be somewhat of a tail on that depending upon further stimulus measures, things of that nature. So charge-off and the timing of charge-offs is an important consideration as to how the allowance is utilized in terms of those charges.

The other important factor is uncertainty. And David lead off with this that despite the fact that we're seeing some optimistic news with respect to the vaccine, there's still a lot of uncertainty that is existing in the market today. And so, we really need to see both the timing of charges come to fruition as well as these remaining sources of uncertainty being resolved before you can expect to be back closer to that day one-type of allowance-to-loan ratio.

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Terry McEvoy
Analyst, Stephens, Inc.

Q

And then a question that just came in just to continue the topic. With multiple vaccines now moving forward, how does that impact the loan loss provision? I think you just addressed that. So maybe I will add that economic adjustment in a CECL world is that the variable that will drive the provisions and the need to build or release reserves?

Anil Chadha
Executive Vice President-Head of Shared Risk Services & Analytics, Regions Financial Corp.

A

Yeah, a couple of things. With respect to both an economic forecast as well as a vaccine, I would focus less on the vaccine and focus more on the time between a vaccine and when it's widely available because what we're really talking about here is economic activity returning to the point that we have greater confidence that the economy is on a firm footing. So again, it's wonderful news that we have multiple vaccines in place, but we know it's going to take a period of time for that to be widely distributed such that you have a return to strong economic activity. And so, I think that's really what we need to be focused on.

With respect to the economic forecast, the economic forecast is a good gauge in terms of how do we think the economy is improving. But let's also remember, we're a good six, seven months into this pandemic. We have a good understanding of where we see risk in our portfolios. And so, it's really managing that risk, staying on top of that risk. That's going to be a good internal guide for us as to how we're progressing.

I would say that economic variables are good outside looking-in indicator as to what do we think the overall economy is looking like. But it's really now becoming more a story of where we're seeing stress in our portfolio, how are we managing that, staying on top of that and ensuring we continue to have an appropriate reserve there.

Terry McEvoy
Analyst, Stephens, Inc.

Q

And maybe a question for Ronnie. Ronnie, there's a Bloomberg article out last week with the title, American Companies Are Stockpiling Cash Before COVID Winter Hits. And the theme was more on corporate America raising cash. Are you seeing that among your corporate clients and you think we could see commercial line draws like we saw earlier in the year?

Ronald G. Smith
Senior Executive Vice President & Head of Corporate Banking Group, Regions Financial Corp.

A

We are clearly seeing the increase in cash, both on the clients' balance sheet and ultimately ours. David mentioned a little bit earlier, we're the ones that are really driving the deposit growth at this point. It started with defensive line draws. But in majority, Terry, those line draws have been paid back. But we're seeing, and you would think in a logical way that that would mean our cash balances would be coming down. But the opposite has actually happened. And we've seen deposits continue to move up even though those defensive line draws have been paid down.

So as we talk to our clients, what we learn is, number one, they're doing a better job on managing their current asset days, inventory days receivable and just generating more cash. And they're being much more efficient in their operations. We are all going to learn things coming out of COVID, and for our client base at large, that's no exception. So what do I think about – well, I think your question was what happens in the future? I think we'll see clients lean back into their cash before advancing back on their lines of credit. So we are anticipating that line utilization will remain in that 40%, 41% range for the immediate future until things get back to normal.

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We feel like the cash is where our clients feel the safest. But as more confidence builds, and David I think you said that in your earlier comment says, client confidence builds, we do feel like that we'll see more line utilization at that point.

Terry McEvoy
Analyst, Stephens, Inc.
Q

And then a follow-up there. Back-to-back vaccines, the elections two weeks away, have you picked up a more upbeat tone from any of your clients given news on the vaccines? Or is it still too early and uncertainty is still the theme of the day?

Ronald G. Smith
Senior Executive Vice President & Head of Corporate Banking Group, Regions Financial Corp.
A

Yeah. I think the answer is, yes. We've seen more upbeat tone but measured. Everyone's more upbeat because there appears to be a solution. The biggest concern as it would be for the general public is how quickly can it be effective and what do we see occurring once the vaccine is rolled out? Tempering that that upbeat tone is the fact that we're seeing more spikes right now. And so, you hear both sides of the concern.

Terry McEvoy
Analyst, Stephens, Inc.
Q

Okay. And then circling back to a question here on capital that came in. Any updates on the next round of CCAR and how is Regions prioritizing capital return in 2021, specifically buying back stock? And I know David you addressed the topic, but maybe prioritizing if you put the capital return question.

David Jackson Turner
Chief Financial Officer & Senior Executive Vice President, Regions Financial Corp.
A

Deron, do you want to address that?

Deron Smithy
Executive Vice President & Treasurer, Regions Financial Corp.
A

Yeah. Sure. So I would say our priorities for capital really haven't changed. First, we need to build our capital levels back to what we think are appropriate. And certainly in this environment, capital levels are going up just reflecting the uncertainty. And so, we'll initially let our capital levels build back to 9.5% to 10%, probably closer to the upper end of that range. And then after that, it's – remains as it's always been. We'll focus on opportunities to grow the business. Some of those may be strategic in nature, like you've seen us do with the Ascentium acquisition and other bolt-on type acquisitions that we think enhances our ability to serve customers and build the gap in our product or service set. We want to keep the dividend at an appropriate level and keep it growing, commensurate with earnings.

And then, finally, share repurchase is sort of the third in line there. But I wouldn't anticipate share repurchases returning until, a, we get back to our capital targets first; and then, b, we've got to have a good line of sight as to the path forward with the economy and the environment. And so, all of those things have to come together for us to feel like it'd be appropriate to be returning capital in that manner.

With respect to the stress test, as you know, we just recently submitted that. We don't have a lot of incremental insight as to how things go from here. We think we'll find out the results of that stress test or the Fed piece of that

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by the end of the year. But in terms of what the downstream implications of that are with respect to SCBs and the like, we don't have a lot of insight on that.

Terry McEvoy
Analyst, Stephens, Inc.
Q

Thank you. And another question that came in, I guess, there's two parts to it to address, the currency meaning Regions' valuation is relatively high versus peers today. Why not pursue a bank acquisition to offset the headwinds from the hedge roll-off in 2022? So maybe the first part of the question maybe talk about the headwinds on the hedging side, maybe put some numbers behind that. And then the second part is acquisition to offset those headwinds.

David Jackson Turner
Chief Financial Officer & Senior Executive Vice President, Regions Financial Corp.
A

Deron, why don't you take the headwinds and I'll do the other.

Terry McEvoy
Analyst, Stephens, Inc.
Q

Thank you.

Deron Smithy
Executive Vice President & Treasurer, Regions Financial Corp.
A

Agreed. So David's talked about, at the outset, the hedge contribution and it's been steadily growing throughout 2020. And in fact, there's still a marginal piece to come online. But we'll be fully hedged by the beginning of 2021. And then it's a four-year period, roughly, thereafter that the hedge will cover protection against low rates. And the contribution that David mentioned is in the mid-90s, $95-ish million per quarter recently. We think that grows up to around $100 million. And then it is roughly $100 million run rate benefit per quarter to net interest income assuming that the rates stay at current levels.

David Jackson Turner
Chief Financial Officer & Senior Executive Vice President, Regions Financial Corp.
A

Yeah. So...

Deron Smithy
Executive Vice President & Treasurer, Regions Financial Corp.
A

And then there is a staggered – there's just a staggered roll-off, most of it is in place for at least the next four years.

David Jackson Turner
Chief Financial Officer & Senior Executive Vice President, Regions Financial Corp.
A

I think that page that shows you by quarter – we didn't put it in this deck, It's in a earlier version of our – one of our decks. But in this particular deck on page 15, you can see the contribution that the hedge has to NII, and also the remaining term and ours is much higher than our peers, which we think gives us a competitive advantage to fight that low rate environment Terry that you're talking about.

And as I mentioned earlier I think low rates revenue challenges really increase the desire on many to enter into some form of acquisition to grow revenue, to grow markets at a time where organic growth is tough. I think that's

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the case for all of us. While we haven't been fixated on M&A and are not currently, we do acknowledge that if we will execute our plan and get our share price up where we think it ought to be, it creates an opportunity for us to take advantage of opportunities should they arise to do bank M&A perhaps in 2021 and beyond.

We don't know that we're there yet, but we're getting closer and I think for us is, we don't need to just do an acquisition just to do an acquisition and we need to do it because it's strategic. Gets back to your question, you asked me earlier why and where would you be looking to do it. And building out our footprint density is important to us. And so, our industry has not been as disciplined as it should have been when acquisitions started going in the early days it was just like everybody needed to get on that train. We're not in that position. We want to do what's right for our shareholders over the long haul and be very thoughtful about putting their capital to work and we do that internally every day as we challenge ourselves on returns on capital for the businesses that we're in. So, M&As can be and probably will be a bigger part of our industry I think going forward, but I think in a measured way.

Terry McEvoy
Analyst, Stephens, Inc.

Q

And then maybe one more interest rate question before we move on to credit. Could you just talk about the headwinds to NII or in the net interest margin from the re-pricing of fixed rate loans and securities? And really how much of a benefit you see from the recent steepening of the yield curve?

David Jackson Turner
Chief Financial Officer & Senior Executive Vice President, Regions Financial Corp.

A

Yeah. Sure. So as we've mentioned, we think the hedges have roughly neutralized the impact for short rates. And but we do have a continued re-pricing of the balance sheet, both in securities and fixed rate loans either renewals and/or new business originations. And that is in the $12 billion to $14 billion annually is the amount that is re-pricing. And previously, we had masses that we were losing roughly 100 basis points through that reinvestment.

Obviously, the recent back up in rates is helpful to that. And I would say it's you know in the mid-80s today. And so it's certainly helpful. It's helpful on two fronts. It's on the reinvestment front, but it's also helpful with respect to mortgage rates in that it does slow prepayments a bit and the related premium amortization. And really that that headwind from a re-pricing standpoint it makes it tough to grow net interest income year-on-year just solely on the rate front.

And so, we're going to need growth in the balance sheet to overcome that. Obviously, loan demand has been somewhat tepid here in the short run and we would expect that to be the case here in the near-term. But over time, as the economy continues to improve and certainly as we look into next year, we would expect that there will be opportunities perhaps in the latter half of the year to begin to grow the balance sheet and to offset some of that headwind from a net interest income standpoint.

Terry McEvoy
Analyst, Stephens, Inc.

Q

Thank you. Moving on to credit, last quarter, the uptick in non-performing loans was investor CRE within retail and energy, which has been around. Though the comments on the call were quite positive with regard to the health of retail CRE, I was wondering if COVID cases rising and just talk of select shutdowns, what are your updated comments on retail CRE?

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Barbara I. Godin
Senior Executive Vice President, Deputy Chief Risk Officer and Chief Credit Officer, Regions Financial Corp.
A

Yeah. We are still feeling pretty good. I'm going to ask Ronnie as well to join in. We're still feeling pretty good about retail CRE. Malls is the spot where there's going to be more pressure on any of the malls. Grocery anchored malls, we feel good about, they're strong, they're doing well. They're back 80% to 90% of what they were previously. But malls that are in Class B space or malls that don't have grocery anchored, clearly, they're under some pressure. We anticipate that they will continue to be under some pressure.

The thing about a lot of the space that's available in CRE is that a lot of the leases are five to seven-year leases. So, this is going to be a problem that's going to kind of slowly develop. We hope that the economy catches up with that timing as well. But we do anticipate that we're going to have to spend more time. Looking at those portfolios, which we have been, we've tightened our credit box as well. And we really don't have as much CRE. Thank goodness as we did in The Great Recession. In the Great Recession, our overall commercial real estate was significant. It's way down now was made up of land back then. It isn't now in our industrial estate as well. So, I'm feeling much better about the real estate portfolio.

You know we underwrote CRE this time around to 60% to 70% loan to value. More importantly loan to cost. And whereas in the Great Recession, it was 75% to 85% and lot more equity upfront in these deals as well. So all-in long answer to say, all-in we're feeling better, very cautious about that area and we'll continue to be cautious about that area. Ronnie, anything you want to add?

Ronald G. Smith
Senior Executive Vice President & Head of Corporate Banking Group, Regions Financial Corp.
A

I don't think I can add much to that. Terry, just would draw everybody's attention to slide 35. You probably have taken a look at the breakdown of the exposures. And the team did a good job of breaking out where our exposure sits with IRE retail non-essential. And it also shows the unsecured retail. So when you think about the outstanding balances there the REITs are obviously strong and cash-rich at this point.

You know most of the owners, sponsors that I've talked to on the IRE retail side are seeing renewals, but renegotiated renewals providing enough cash flow to move them to what's projected to be the other side of the pandemic. But, Barb, to your point, if there is a prolonged piece we could continue to see stress on those particular borrowers. So Terry, we're cautiously. And I would underline cautious more than optimistic about that particular portion of the portfolio. But for right now as Barb said, we feel good about what has been accomplished and the limited exposure that we have in that space.

Terry McEvoy
Analyst, Stephens, Inc.
Q

Thank you.

Ronald G. Smith
Senior Executive Vice President & Head of Corporate Banking Group, Regions Financial Corp.
A

Sure.

Terry McEvoy
Analyst, Stephens, Inc.
Q

I really like page 33 the significant expansion of portfolio risk indicators. So my question there is, did the speed at which COVID kind of impacted borrowers allow you to kind of test those portfolio performance metrics and in early

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warning indicators or, did things happened so quickly that it just didn't give you that opportunity to test everything that's kind of listed on that page there?

Barbara I. Godin
Senior Executive Vice President, Deputy Chief Risk Officer and Chief Credit Officer, Regions Financial Corp.
A

Martha, why don't you go ahead first and I can jump in after?

Martha Raber
Executive Vice President & Head - Financial Risk, Regions Financial Corp.
A

Sure. I know that the metrics that we put in place are key risk indicators as well as our early warning indicators did start sounding to us and alerting us to emerging pockets of risk across the portfolio. So it worked exactly as we expected it to do. And so, we started to see metric start to signal early in the first quarter and then that continued. And it allowed us to really pivot and direct our oversight to those industries and subsectors and products, where we were starting to see rising risk and work very closely for example with Ronnie and his leadership team and all of the relationship managers to proactively go out to the clients in those areas start to have conversations and get better insights as to the drivers of risk that they were seeing and then take the appropriate action to ensure that they could perform during the cycle. And we felt comfortable with their strategies.

And as Barb has talked about in many of these forums, as we had those conversations, we were not also – we were not relying on trailing 12 and historical information we were working with the clients on current information as well as forecasts, and then calling the risk as we saw it and taking the appropriate actions. But, to your point, that was a longwinded answer. The metrics worked exactly as we wanted them to work.

David Jackson Turner
Chief Financial Officer & Senior Executive Vice President, Regions Financial Corp.
A

Yeah Barb, yeah Martha I may just add just from practical standpoint, Terry, we meet with our risk partners once a month all material loans. We define that as $5 million and more are individually reviewed by the business and by our risk partners Martha, Matt, Barb, Anil, all are in the room feeding information back. And to Martha's point, we're looking at real time data versus historical. Because if you just take the trailing 12, you obviously get interference on more positive outcomes than what we should be considering and so it's been a really strong partnership and it's been that way for a long time that COVID didn't cause that to occur, it just caused it to have a brighter spotlight shed on it at this point.

Terry McEvoy
Analyst, Stephens, Inc.
Q

Incoming question here, if we go back pre-COVID, there was a lot of talk and emphasis on leverage lending. Could you just talk about how that portfolio has performed throughout COVID, and I appreciate the disclosure all the disclosures [ph] that we did (00:33:08) along the way.

Barbara I. Godin
Senior Executive Vice President, Deputy Chief Risk Officer and Chief Credit Officer, Regions Financial Corp.
A

Definitely, Martha, why don't you go ahead again.

Martha Raber
Executive Vice President & Head - Financial Risk, Regions Financial Corp.
A

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Sure. So in your deck, you do have a slide there for leverage lending and it has performed well during this pandemic. We are seeing reductions. I think, year-to-date, we've seen somewhere around 5% reduction, but we're pleased. This is not a strategy that we follow. This is something that we do to support our best clients. And when we name our tax something leverage, it's based on a credit event. So, they are taking action where it results in leverage on a senior and total basis of greater than 3x4. And from a collateral basis, there is a collateral shortfall. In those numbers, we have both investment both investment grade as well as non-investment grade clients. Again, with all of these clients, we are staying very, very close to them. It is well-diversified. I wouldn't say that there is any outsized exposure in any specific area. Many of these clients also have a very strong sponsor support.

Any other questions on that, Terry?

Terry McEvoy
Analyst, Stephens, Inc.

Q

No, let them – thank you very much. Let's shift gears. I'm wondering, if you could comment on deposit growth so far in the fourth quarter. And after purchasing $3 billion of securities last quarter, what's the strategy today on managing excess liquidity?

David Jackson Turner
Chief Financial Officer & Senior Executive Vice President, Regions Financial Corp.

A

[ph] Dan (00:34:50), do you want to take that?

A

I'll take. I will. We continue to see very robust deposit activity. I think, it's continuing trend. Despite what we thought, it might lead to at least a flattening of deposits with some of the assistance programs ending. But quite frankly, I think customers or clients, both own the retail and the business sides, put a priority on maintaining liquidity and has done a good job of managing their savings in a way that's leading to continued deposit growth.

We do expect that trend continues into next year certainly if we get additional stimulus it would only add to that. And so, as we've talked about is leading to record cash levels that we're holding we decided to put some of that to work in securities you referenced the $3 billion in the most recent quarter. I think we'll continue to look for opportunities incrementally there. We were looking for a better entry point thought that conditions were favorable for the curve perhaps to steepen a bit. And so, we're looking for rate levels a bit higher than where we are today to make incremental investments.

But I think we'll do some marginal investing if we achieve those levels. Nothing dramatic. I do want to point out though that's the more visible way that we've put a lot of that cash to work. Perhaps less visible, but certainly impactful is all of the reductions on the liability side to wholesale borrowings and we've been able to pay off all of our wholesale borrowings. We've tendered for debt. We've called debt and we'll continue to look for opportunities to manage overall funding costs down we did a lot of this excess cash as well. But we do expect just given the outlook for deposits in relatively soft loan demand here in the short run. The cash balances will remain elevated. And again look for some opportunities put that work to work in securities. But we're going to be cautious and somewhat selective about that.

Terry McEvoy
Analyst, Stephens, Inc.

Q

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Moving on part of the focus on increasing risk adjusted returns was investing in Corporate Banking, Wealth Management. The question is, what's the outlook for fee income particularly Wealth Management capital markets? And I think David I think you touched on card fees earlier on that in the chat here.

David Jackson Turner
Chief Financial Officer & Senior Executive Vice President, Regions Financial Corp.

A

Yeah. So Wealth Management I think we can continue to grow there benefiting from some new hires we made at the about the middle of last year. And as they really come on have now been here approximately a year continuing to grow relationships, I think, will be important. So we think we can get incremental lift there.

Capital markets again this type of environment, it's not only M&A in the banking world, but it's just M&A in general when you have access to this type of capital to be able to do transactions. And I think you'll see our capital markets division do very well. Again, that business and there are I don't know five sub businesses inside of capital markets. They do have a tendency to be a bit volatile. So, it's not quite as smooth as we'd like to see quarter-to-quarter, but that's the nature of the beast. We do expect capital markets to have a good finish and we think it can have a robust 2021.

We think service charges has some room to improve, but I don't know that we'll get back to the pre-pandemic levels. I think, there could be a paradigm shift in terms of how people really manage their money. There's more cash sitting in the deposit or accounts so they're able to avoid the service charge. They're not having NSF incidences like they did before. And so, I wouldn't count on that. And that's cost us it's in the $10 million per month range relative to the fourth quarter 2019, so pre-COVID level. And while that's gotten a couple of million dollars better than last time, we haven't seen it moving appreciably.

Card and ATM fees, we're a little ahead of where we were a year ago as I mentioned. We think we can see some growth there as we continue to grow accounts. So we are growing, checking accounts, we're growing cards in the hands of people and we think card utilization is going to continue to improve across the United States and our industry. We think card utilization will be up as that goes up interchange will be up as well.

And then mortgage I guess is our last big area and fees, mortgage is like I said it's going to have a very robust year. We think it can have a good 2021. We're not yet to give you guidance on total NIR yet for 2021, but I think it'd be challenging to get back to the level in 2021 in mortgage that we will have in 2020, but we said the same thing about 2020 versus 2019 and look what happened in 2020. So one never knows what goes on with it. The rate environment stays low longer. We still have we think a lot of purchase activity that we can take advantage of. There'll be some refi opportunities as well, but not nearly as much in 2021 as we have seen in 2020.

Ronald G. Smith
Senior Executive Vice President & Head of Corporate Banking Group, Regions Financial Corp.

A

David, maybe one thing to add from a capital market standpoint, we have made investments in that business and we continue to do that on a select basis. When we think about how we support our existing client base, one thing that may be of interest is that early in the pandemic we did see a lot of interest rate derivative type activity. But as we've moved to the fall of the year, there are green shoots around M&A advisory type of services that we're beginning to see and so hopefully that is a sign of positive things to come and more confidence out as clients start thinking about how do they expand their own business.

Terry McEvoy
Analyst, Stephens, Inc.

Q

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A question on expenses. Since simplifying growth you've done a great job managing the expense growth. There's a statement in the presentation that talks about evaluating digital and technology spend priorities given the changes in customer behavior. And I'm not quite sure how to interpret it better. Are you suggesting that the spend could increase going forward and I know you don't want to talk about 2021, or are you saying you're going to balance that investment spend with other types of actions like branch closures?

David Jackson Turner

Chief Financial Officer & Senior Executive Vice President, Regions Financial Corp.

A

Yeah. So it's more of the latter. We acknowledge that we need to continue to make investments in technology, whether it'd be our core platform whether it'd be mobile, whether it'd be online, digital. And we've done that and we're proud of those investments. We get third-party reports that that spend is really working for. So our mobile rating for instance is up to 4.8 on a scale of 5, which is pretty exciting and we get good feedback on online. And we can see that digital transactions have increased markedly. So, we have to keep making investments there.

We also have to keep our expenses relatively stable in order to do both of those things and you have to cut somewhere else. And for us, that's been really in salaries and benefits. It's 55% of our expense base and kind of the number one area there has been in our branch world we've been able to change the job family to one real main job family in our branch. So we've reduced the number of people in the branches but we've also reduced the branches through consolidation. And I think you'll see consolidations continue to be robust for us. The exact number we're continuing to work through each and every day.

And we have a tendency to consolidate more than we even tell you or ourselves. And so, the idea is to continue to evolve and to see how this paradigm shift if that's what it's going to be, the people are going to really start banking more digitally and the branches aren't as relevant, then we need fewer of them or we need smaller ones. And so, we do believe in the branch model, it's important to us. It drives our retail network. It drives our brand. But we also know that people are banking with us differently.

So today our number one sales channel is our branch channel. We see over time that that could change and probably will change. The pace of that is what we're struggling with trying to figure out exactly what that looks like. So, I think you'll see the same thing, Terry. I think you'll see investments in digital and branch consolidations among other expensed areas like square footage in the back office, in the headquarters buildings and leveraging this new normal and working remotely I think could be of benefit to us as well.

Terry McEvoy

Analyst, Stephens, Inc.

Great. Well, I think we'll ready to cut off right now so I want to thank David and Dana I apologize I didn't mention your name earlier. I see at the table there. So thanks for your help as well. And appreciate everybody's time. And thanks for everybody in the audience for your time as well.

David Jackson Turner

Chief Financial Officer & Senior Executive Vice President, Regions Financial Corp.

Thank you, Terry.

Barbara I. Godin

Senior Executive Vice President, Deputy Chief Risk Officer and Chief Credit Officer, Regions Financial Corp.

Thanks, Terry.

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Martha Raber

Executive Vice President & Head - Financial Risk, Regions Financial Corp.

Thank you.

Anil Chadha

Executive Vice President-Head of Shared Risk Services & Analytics, Regions Financial Corp.

Thanks, Terry.

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