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Regions Financial Corp. (RF)

Q1 2021 Earnings Call

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CORPORATE PARTICIPANTS

Dana W. Nolan
Executive Vice President & Head-Investor Relations, Regions Financial Corp.

John M. Turner
President, Chief Executive Officer & Director, Regions Financial Corp.

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

OTHER PARTICIPANTS

Kenneth M. Usdin
Analyst, Jefferies LLC

Ryan M. Nash
Analyst, Goldman Sachs & Co. LLC

Gerard Cassidy
Analyst, RBC Capital Markets LLC

Erika Najarian
Analyst, BofA Securities, Inc.

Matthew D. O'Connor
Analyst, Deutsche Bank Securities, Inc.

John Pancari
Analyst, Evercore Group LLC

David Rochester
Analyst, Compass Point Research & Trading, LLC

Peter J. Winter
Analyst, Wedbush Securities, Inc.

Jennifer Demba
Analyst, Truist Securities, Inc.

Bill Carcache
Analyst, Wolfe Research, LLC

Betsy L. Graseck
Analyst, Morgan Stanley & Co. LLC

Christopher Marinac
Analyst, Janney Montgomery Scott LLC

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MANAGEMENT DISCUSSION SECTION

Operator: Good morning and welcome to the Regions Financial Corporation's Quarterly Earnings Call. My name is Shelby, and I'll be your operator for today's call. I would like to remind everyone that all participant phone lines have been placed on listen-only. At the end of the call, there will be a question-and-answer session. [Operator Instructions]

I will now turn the call over to Dana Nolan to begin.

Dana W. Nolan

Executive Vice President & Head-Investor Relations, Regions Financial Corp.

Thank you, Shelby. Welcome to Regions' first quarter 2021 earnings call. John and David will provide high-level commentary regarding the quarter. Earnings documents, which include our forward-looking statement disclaimer, are available in the Investor Relations section of our website. These disclosures cover our presentation materials, prepared comments, and Q&A.

I will now turn the call over to John.

John M. Turner

President, Chief Executive Officer & Director, Regions Financial Corp.

Thank you, Dana, and thank you, all, for joining our call today. We kicked off 2021 on a solid note. Earlier this morning, we reported earnings of $614 million, resulting in earnings per share of $0.63. Our ability to continue to deliver value this quarter is a testament to both the investments we've made as well as our associates' unwavering commitment to our customers and communities.

Our credit metrics continued to improve and reflect the good work we've done with our clients, coupled with the expected benefits from government stimulus. Based on this quarter's credit performance and the improving economic outlook, we reduced our allowance for credit losses by $142 million more than net charge-offs while still maintaining one of the strongest allowance-to-loan ratios in the industry at 2.44%.

Although we continue to deal with the effects of the pandemic, our ongoing conversations with customers reflect optimism about further economic recovery and growth. Vaccine distribution is improving in our footprint and businesses, for the most part, had reopened. The majority of our largest deposit states are experiencing unemployment rates significantly below those of the US as a whole, and our loan pipelines are improving as we are seeing more activity in the marketplace. We're increasingly optimistic this momentum will continue.

Throughout this recovery and beyond, we will maintain our focus on deepening relationships with our customers by providing personalized financial guidance combined with excellent technology solutions that continue to make banking easier.

Now, David will provide you with some details regarding the quarter.

David J. Turner, Jr.

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

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Thank you, John. Let's start with the balance sheet. Average and ending adjusted loans declined 1% from the prior quarter. New and renewed commercial loan production increased 5% compared to the prior quarter. However, balances remain negatively impacted by excess liquidity in the market resulting in historically low utilization levels. As of quarter end, commercial line utilization was 39% compared to our historical average of 45%. Just a reminder, each 1% of line utilization equates to approximately $600 million of loan growth.

Commercial loan balances continue to be impacted by the company's ongoing portfolio management activities and PPP forgiveness timing. Average consumer loans again reflect a strong mortgage production, offset by runoff portfolios. Overall, we expect full year 2021 adjusted average loan balances to be down by low-single-digits compared to 2020, although we expect adjusted ending loans to grow by low-single-digits.

With respect to deposits, balances continued to increase this quarter to new record levels, led by growth in the consumer segment, reflecting recent government stimulus payments. The increase is primarily due to higher account balances. However, we are also experiencing new account growth. We expect near-term deposit balances will continue to increase, particularly as recent stimulus is fully disbursed and corporate customers maintain higher cash levels.

Let's shift to net interest income and margin, which remain a significant source of stability for Regions. Net interest income decreased 4% on a reported basis or 1% excluding the impact from day count and PPP. PPP related NII declined $14 million from the prior quarter as the benefits from round two were offset by slower round one forgiveness. Two fewer days also reduced NII by $12 million. The decline in core NII stems mostly from lower loan balances and remixing out of higher-yielding loan categories.

Net interest margin declined during the quarter to 3.02%. Cash averaged over $16 billion during the quarter, and when combined with PPP, reduced first quarter margin by 38 basis points. Excluding excess cash and PPP, our normalized net interest margin remained stable at 3.40%, evidencing our proactive balance sheet management, despite a near-zero short-term rate environment. Similar to prior quarters, the impact from historically low long-term interest rates was offset by our cash management strategies, lower deposit costs, and higher average notional values of active loan hedges.

Cash management, mostly in the form of a December long-term debt call, contributed $6 million and 1 basis point of margin. Interest-bearing deposit costs fell 2 basis points in the quarter to 11 basis points, contributing $4 million and 1 basis point of margin. Loan hedges added $102 million to NII and 31 basis points to the margin. Higher average hedge notional values drove a $3 million increase compared to the fourth quarter.

At current rate levels, we expect a little over $100 million of hedge-related interest income each quarter until the hedges begin to mature in 2023. Within the quarter, we've repositioned a total of $4.3 billion of cash flow swaps and floors targeting less protection in 2023 and 2024. While there may be additional adjustments in the future, we believe the resulting profile allows us to support our goal of consistent sustainable growth.

Specifically, we are positioned to benefit from the steepening yield curve and increases in short-term interest rates in the future while protecting NII stability to the extent the Fed is on hold longer than the market currently expects. A potential for loan growth only enhances our participation in a recovering economy. Looking ahead to the second quarter, we expect NII excluding cash and PPP to be relatively stable.

While recent curve steepening has helped asset reinvestment levels, long-term rates will remain a modest near-term headwind. Deposit cost reductions, one additional day, and hedging benefits will support NII in the quarter, while loan balances are expected to remain relatively stable. Over the second half of the year and beyond, a

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strengthening economy, a relatively neutral impact from rates, and the potential for balance sheet growth are expected to ultimately drive growth in NII.

Now, let's take a look at fee revenue and expense. Adjusted non-interest income decreased 2% from the prior quarter, but reflects a 32% increase compared to the first quarter of 2020. Capital markets delivered another strong quarter as customers continued to respond to interest rate changes and potential regulatory and tax headwinds. Fees generated from the placement of permanent financing for real estate customers and securities underwriting both achieved record levels, and M&A advisory services also delivered solid results. While we expect capital markets revenue to remain solid over the remainder of the year, some activity was pulled forward. Looking ahead, we expect capital markets to generate quarterly revenue in the $55 million to $65 million range on average, excluding the impact of CVA and DVA.

Mortgage delivered another strong quarter as we continue to focus on growing market share and improving our customer experience. Mortgage income increased 20% over the prior quarter, driven primarily by agency gain on sale and favorable MSR valuation. Production for the quarter was up 89% over the prior year, setting the stage for another strong year of mortgage income. Service charges were negatively impacted by both seasonal declines and increased deposit balances. While improving, we believe changes in customer behavior as well as customer benefits from enhancements to our overdraft practices and transaction posting are likely to keep service charges below pre-pandemic levels.

Although we expect the impact of these changes will be partially offset by continued account growth, we estimate 2021 service charges will grow compared to 2020, but remain approximately 10% to 15% below 2019 levels. Card and ATM fees have recovered, up 10% compared to the prior year, driven primarily by increased debit card spend. Given the timing of interest rate changes in 2020 combined with exceptionally strong fee income performance, we expect 2021 adjusted total revenue to be down modestly compared to the prior year, but this will be dependent on the timing and amount of PPP loan forgiveness and loan growth.

Let's move on to non-interest expense. Adjusted non-interest expenses decreased 1% in the quarter, driven by lower incentive compensation, primarily related to capital markets and mortgage, which was partially offset by a seasonal increase in payroll taxes. Of note, base salaries were 4% lower compared to the fourth quarter as we remain focused on our continuous improvement process. Associate head count decreased 2% quarter-over-quarter and 4% year-over-year, and excluding the impact of our Ascentium Capital acquisition that closed April 1, 2020, head count was down 6%.

We will continue to prudently manage expenses while investing in technology, products, and people to grow our business. In 2021, we expect adjusted non-interest expenses to remain stable compared to 2020 with quarterly adjusted non-interest expenses in the $880 million to $890 million range. And while we face uncertainty regarding the pace of economic recovery, we remain committed to generating positive operating leverage over time.

From an asset quality perspective, overall credit continues to perform better than expected. Annualized net charge-offs were 40 basis points, a 3-basis-point improvement over the prior quarter reflecting broad-based improvement across most portfolios. Non-performing loans, total delinquencies, business services criticized loans all declined modestly. Our allowance for credit losses declined 25 basis points to 2.44% of total loans and 280% of total non-accrual loans. Excluding PPP loans, our allowance for credit losses was 2.57%. The decline in the allowance reflects charge-offs previously provided for, stabilization in our economic outlook, and improved credit performance, including the impact of the $1.9 trillion stimulus bill approved in March.

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The allowance reduction resulted in a net $142 million benefit to the provision. Our allowance remains one of the highest in our peer group as measured against period-end loans or stress losses as modeled by the Federal Reserve. Future levels of the allowance will depend on the timing of charge-offs and greater certainty with respect to the path of the economic recovery. As we look forward, we are cautiously optimistic regarding our credit performance for the year. While net charge-offs can be volatile quarter-to-quarter, based on current expectations, we believe the peak is behind us and we expect full year 2021 net charge-offs to range from 40 to 50 basis points.

With respect to capital, our Common Equity Tier 1 ratio increased approximately 50 basis points to an estimated 10.3% this quarter. As you are aware, the Federal Reserve extended their restrictions on capital distributions through the second quarter of 2021. The Federal Reserve also indicated these restrictions are expected to be lifted beginning in the third quarter, subject to capital remaining above required levels in the ongoing 2021 CCAR cycle for firms participating.

We have opted into this year's CCAR, and assuming capital levels remain above required levels and the Fed's Stress Test, we should be back to managing capital distributions against the SCB requirements beginning in the third quarter. However, our plan is to begin share repurchases in the second quarter, subject to the Fed's earnings-based restrictions. Based on our internal stress testing framework and amount of capital we need to run our business, we are updating our operating range for Common Equity Tier 1 to 9.25% to 9.75% with the goal of managing to the midpoint over time.

So, wrapping up on the next slide, our 2021 expectations which we have already addressed. In summary, we feel really good about our first quarter results and anticipate carrying the momentum into the remainder of 2021. Pre-tax pre-provision income remains strong, expenses are well controlled, credit quality is outperforming expectations, capital and liquidity are solid, and we are optimistic about the prospects for the economic recovery to continue in our markets.

With that, we're happy to take your questions.

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QUESTION AND ANSWER SECTION

Operator: Thank you. The floor is now open for questions. [Operator Instructions] Your first question is from Ken Usdin of Jefferies.

John M. Turner
President, Chief Executive Officer & Director, Regions Financial Corp.
A

Good morning, Ken.

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

Ken?

Kenneth M. Usdin
Analyst, Jefferies LLC
Q

Sorry, guys. Is that open to me, Ken Usdin?

John M. Turner
President, Chief Executive Officer & Director, Regions Financial Corp.
A

Yeah.

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

Yes.

Kenneth M. Usdin
Analyst, Jefferies LLC
Q

Oh, my bad. Sorry. I thought I lost you for a second. Thank you. Yeah. David, just wondering, you made the points clearly about starting to reposition that longer-term swaps portfolio and to position for potentially higher rates. How are you – how do you help us think about how that changes the longer-term trajectory of recognized income versus just the hope that rates go the right way and loans are better, presuming the economic recovery? And in terms of just how you make future decisions on future – on other potential terminations? Thank you.

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

Yeah. So, Ken, we never anticipated for all the derivatives to go to term. We wanted protection and our goal is not to turn the derivatives into a trading asset, but to have it help us manage the volatility of NII and that's worked extremely well for us. As we think about the future, we obviously look at all the data points to try and figure out when the Fed may move. And as we continue to have economic progress, we're thinking that there is more likelihood of an increase in short rates and probably loan rates to follow, starting in the back half of 2022 and into 2023 and 2024. We wanted to participate in that and not have our NII being muted. So, we terminated the $4.3 billion worth of derivatives. You take whatever gain you have and you have to spread that over the life, you don't get a onetime gain. So, we will continue to evaluate the economic recovery and we'll make adjustments as we go

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along. We still have protection though for 2021 and 2022, no change there. It's just out the curve – I mean out the term a little bit in terms of really 2023 and 2024.

Kenneth M. Usdin
Analyst, Jefferies LLC

Q

Okay, got it. And along the way, obviously, you're still sitting on this big excess cash position as you showed to us in your core NIM. Can you just talk to us about how you're thinking about staging incremental use of that cash versus the hopes for loan growth that you and the rest of the industry are hoping for anticipating?

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

A

Yeah. We – like many folks, we had a nice deposit growth. We've had $16 billion of average cash at the Fed, $23 billion at the end of the quarter. We constantly challenge ourselves, Ken, on whether or not put that to work in the securities book when – of course, we want to make all the good quality loans we can, that's been elusive for the industry thus far. And so, some have deployed that in the securities book, we've done a little bit, but we're reluctant because, I was talking to our Treasurer yesterday, there's no free lunch here, you just can't – you can't hide from the risk that you take, if you try to take duration risk right now and deploy in that in the securities book. It will help you short-term in NII, but you will pay for that dearly down the road and we're playing the long game. We're not about trying to generate short-term NII growth for that sake. So, that being said, we are challenging ourselves, and as we make different decisions to get that deployed, you should not expect wholesale investment in the securities book, but you may see some around the edges.

Kenneth M. Usdin
Analyst, Jefferies LLC

Q

Okay. Thanks for that, David.

Operator: Your next question is from Ryan Nash of Goldman Sachs.

John M. Turner
President, Chief Executive Officer & Director, Regions Financial Corp.

A

Good morning, Ryan.

Ryan M. Nash
Analyst, Goldman Sachs & Co. LLC

Q

Hey. Good morning, guys. So, maybe to dig in a little bit on revenues, you're off to a nice start to the year, I think revenues are up over 9% year-over-year with both NII and fees up. So, can you just maybe talk through the revenue outlook a bit and where could there be sources of upside just given the fact that the guide implies a pretty strong deceleration from the first quarter and it looks like mortgage and capital markets could remain strong?

And then, second, it just seems like PPP is one of the potential swing factors. Can you maybe just help us understand what are you assuming for balances and forgiveness for the rest of the year? And then, I have a follow-up.

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

A

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Okay. So, to start with the top of the house, so our guide on total adjusted revenues is down modestly, obviously, continued to have pressure and reinvestment of fixed rate assets throughout the year. We do have some, obviously, protection on NII through our hedging program, so we're excited about that. From a loan growth standpoint, we are in some great markets, so we expect to benefit over time as our economies continue to open and we get some loan growth. We have some headwinds in terms of – again, we continue to have capital markets at $100 million every quarter, we guided you to $55 million to $65 million, so who knows, I mean, if we continue to have capital markets should be robust, M&A should be robust, and we might be able to outperform there, but we gave you the guide of $55 million to $65 million.

We think mortgage will continue to be strong. Our teams are performing very well in terms of mortgage and we think there could be some upside there, but who knows. We have to see what happens with the rate environment. I think in terms of PPP, we have $4.3 billion of PPP loans outstanding. We originated $1.5 billion under the PPP2 program and we forgave about $700 million in the first quarter. The timing of that forgiveness is a big determinant, right, in terms of ultimate income for us. We think that's back-end loaded and literally in the fourth quarter before you start seeing real forgiveness. As a matter of fact, we'll have a little bit of pressure on PPP-generated revenue in – from first to second quarter as we disclosed a little bit and that's only because of timing. The point is, if you got $4.3 billion, the fees and interest we earn off, that's a little over 3%. It's just timing, when is it coming in, and your guess is as good as ours on that, but that will be – that's a pretty big swing factor in terms of where we end up on our guide on revenue for the year.

Ryan M. Nash
Analyst, Goldman Sachs & Co. LLC

Q

Got it. Okay. And then, in terms of capital, you just announced the 9.25% to 9.75%. Yeah. You put out a release the other day announcing a $2.5 billion buyback. And if I look at market expectations for earnings, it implies a pretty steep decline in the capital level. So, can you maybe just talk about expectations for utilizing the buyback, assuming the Fed continues to ease restrictions? And where do you see you actually running with the cap story? I heard you said to run in the middle, but given that we're entering a period of strong economic growth, potential for rates rising at some point in time, could we move towards the lower end of that over time? Thanks.

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

A

Well, so we had – our last goal was closer to 10%. We changed our operating range to 9.25% to 9.75% and said we'd operate in the middle over time. That range can change as economic conditions continue to improve and we still have uncertainty out there. So, we believe that's an appropriate range and an appropriate midpoint of that at 9.50% is the right place for Regions at this time. As conditions get better, we can adjust accordingly, or if they get worse, we'll adjust that way. We're at 10.3% today, so that's 80 basis points from the middle, round numbers, that's $800 million worth of capital. We'll continue to – we didn't have buybacks in the first quarter. As I mentioned, we will have some in the second quarter.

But let's go back and remember, our capital, we want to use to grow our business. That's its priority. We'd love to have more loan growth out there and use it that way. We're going to pay a dividend in the 35% to 45% of our income, so that we have a sustainable dividend. We like to use that capital for nonbank acquisitions like we did on Ascentium Capital is a good example. So, that's our preference. We will then – the last effort we will use buybacks to maintain and optimize our capital at that 9.5% Common Equity Tier 1. So, we'll be restricted on how much we get to do in the second quarter. We think we'll have a very good CCAR submission which gives us more flexibility to manage that to that 9.5% starting in the third quarter and you should expect us to get there and fairly quickly.

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Ryan M. Nash
Analyst, Goldman Sachs & Co. LLC

Q

Thanks for all the color.

Operator: Your next question is from Gerard Cassidy of RBC.

John M. Turner
President, Chief Executive Officer & Director, Regions Financial Corp.

A

Good morning, Gerard.

Gerard Cassidy
Analyst, RBC Capital Markets LLC

Q

Good morning, John, and good morning, David.

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

A

Good morning.

Gerard Cassidy
Analyst, RBC Capital Markets LLC

Q

David, can you touch on – you gave us some good color on the loan loss reserves and I know we've talked about this in the past about your day one reserves back in January of 2020. What's the likelihood that you guys could get to that level or maybe even something less if the economy is even better going forward, let's say, 18 months from now than it was back on January 1, 2020, and the mix of business is less risky than possibly was back then as well?

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

A

Well, you kind of answered your own question there I think, Gerard, and that is you're exactly right. We're sitting here today at 2.44% coverage or 2.57% if you exclude PPP. Our day one was 1.71% and that's more akin to the 2.44%, by the way. And so, the question is, when can you get back to there? And I would just say we really don't think of it as back to there. We think of what's the appropriate reserve we need to have based on the risk inherent in our portfolio. That can change based on your profile and to the extent the profile is better than it was that January when we adopted, if the environment that we expect through the whole life of the loan is better, then the reserves can go below that. But it's all dependent on what the facts and circumstances are at each balance sheet day.

And so, we see the economy getting better. As we've mentioned, it's better, faster than we thought. We're still cautiously optimistic about where this goes. We need to get the vaccine out, we need the economies to continue to open, and if all that happens, you would expect reserves to come down. But right now, we can only take it – we can only adjust reserves based on what we see today. If next quarter it's better, then you would expect it to come down. So, there's no magic in that day one. That day one was based on the facts and circumstances that existed at January, and if they're better, then you would expect reserves to be lower. If it's worse, you would expect them to be higher.

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Gerard Cassidy
Analyst, RBC Capital Markets LLC

Q

Very good. Thank you. You gave us some good color on the hedging program in both your prepared remarks and answering an earlier question. On the $100 million that you're generating currently at the present time, how could that number – or what interest rate environment would you need to see, to see that $100 million maybe get to $120 million or vice versa or fall to $80 million? Can you give us some color about that particular amount and how it's impacted by rates?

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

A

Well, clearly, the – so, we're receiving fixed swaps and we have floor. So, you earn more to the extent rates are lower than where we are today, and that's pegged off of LIBOR. So, LIBOR, it's pretty [ph] doggone (28:07) low. So, you would have to see that go to almost zero. We don't have any new derivatives where we begin the notional. We had some this first quarter a little bit. I think really as you think about – hello? Are we still there?

John M. Turner
President, Chief Executive Officer & Director, Regions Financial Corp.

A

[indiscernible] (00:28:31)

Gerard Cassidy
Analyst, RBC Capital Markets LLC

Q

Still here.

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

A

Oh, I'm sorry. Okay. So, I think you should think about the contribution really as a stabilizing factor in terms of NII. It wasn't meant to help us increase NII. It was to keep us protected in case we had an extraordinarily low rate environment like we do. So, being able to have $100 million to $103 million, $105 million each quarter is really what it's about, not trying to get it to be $120 million and $130 million.

Gerard Cassidy
Analyst, RBC Capital Markets LLC

Q

Very good. Thank you.

Operator: Your next question is from Erika Najarian of Bank of America.

John M. Turner
President, Chief Executive Officer & Director, Regions Financial Corp.

A

Good morning, Erika.

Erika Najarian
Analyst, BofA Securities, Inc.

Q

Good morning. I wanted to ask a little bit about the expense outlook. So, we've been getting questions from investors recently. Some of your peers [indiscernible] (00:29:26) had announced higher expectations for expense growth due to accelerated investments. And as I look at slide 7 and that very consistent 1% CAGR, John, I'm

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wondering if you can assure investors on how you've been able to keep expense growth at these low levels and invest back in the company. In other words, is there going to be a potential surprise with regards to expense growth going forward, especially as we look forward to a stronger revenue growth environment?

John M. Turner
President, Chief Executive Officer & Director, Regions Financial Corp.

A

No. No surprises, Erika. We, as you know, announced an initiative now a couple years ago, we characterize to Simplify and Grow. We talk now about it as being about continuous improvement. It was largely designed as a way to focus on how we simplify our business, how we flatten the organizational structure, reduce expenses to make investments in people, in technology, and additional capabilities and products. And I think we've successfully done that, to your point, we've been able to keep expenses generally flat while providing increased compensation every year for the teams that remain with us, investing significantly in our business, hiring additional bankers and other associates who are working actively in our technology function and risk management, other parts of our business, and we'll continue to do that.

David mentioned this morning we're committed to holding expenses essentially flat. There may be some increases from time to time if revenue rises, and that revenue is associated with a variable compensation, like capital markets, like mortgage. But otherwise, our core run rate of expenses should be flat and we believe that we can continue to make investments in our business while holding those expenses flat.

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

A

Yeah. Erika, that $880 million to $890 million number that we have guided to, we have embedded in that the investments we want to make, as John mentioned.

Erika Najarian
Analyst, BofA Securities, Inc.

Q

Perfect. Thank you. And, David, second question is for you. I'm guessing that you opted in to the 2021 CCAR to optimize your stress capital buffer lower. What can you do to be able to better direct the results closer to 2.5%?

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

A

Yeah. So, if you were to look at the resubmission that we had in December, you would have seen our degradation there would have put us underneath the floor of 2.5%. We ran our model based on the assumptions, the CCAR assumptions in the first quarter. We believe the results will again show that we will be underneath the floor of 2.5%. So, part of the reason we wanted to participate is because of that.

The other part of it is our credit has continued to improve pretty dramatically, even relative to our peers, and this gives us an opportunity to show you and the rest of the world that our credit has continued to improve as a result of our derisking strategy, our capital allocation strategy. We feel very good about that. This gives an opportunity for an independent third party, in this case, the Federal Reserve, to show everybody what our losses are relative to peer. So, we're excited about participating. We think it will show well. We feel very good about our credit as we've mentioned in the call, and we have robust reserves and capital levels on top of that. So, we're well positioned and I think this can help us from a credit rating agency as well.

Erika Najarian
Analyst, BofA Securities, Inc.

Q

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Understood. Thank you.

Operator: Your next question is from Matt O'Connor of Deutsche Bank.

John M. Turner
President, Chief Executive Officer & Director, Regions Financial Corp.
A

Good morning, Matt.

Matthew D. O'Connor
Analyst, Deutsche Bank Securities, Inc.
Q

Hi. Good morning. Just a clarification on the expenses, for the full year, obviously, it implies a drop down for the rest of the year. Is that just lower incentive comp related to capital markets and mortgage revenues or are there any other drivers as we think about the drop down from 1Q?

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

Yeah. Matt, it's that, but it's also as John mentioned, our continuous improvement program which is – we're focused on this every day. And so, we continue to make adjustments in leveraging technology and processes and talked about head count, that's part of how the head count is down as we're leveraging technology. So, we just have an intense focus on, one, making appropriate investments to grow our business. That's number one. We have to figure out how to pay for that, so we can keep our expenses relatively flat. So, every part of the organization is focused on expense control, so that we can make that investment. And I think you're going to see our expenses, as I mentioned, should come down to that $880 million to $890 million for the remainder of the year.

Matthew D. O'Connor
Analyst, Deutsche Bank Securities, Inc.
Q

Okay. And then, separately as we think about loan growth picking up exiting the year, obviously, there's the PPP running off and the exit portfolios, but what do you think will be the drivers of growth for you guys, I think, this year and into next year?

John M. Turner
President, Chief Executive Officer & Director, Regions Financial Corp.
A

Yeah. Matt, this is John. Our customers are increasingly optimistic about the economy. We operate in some – as David said, some really good markets and most of the states that we operate in were some of the first to reopen their economies. As a result, unemployment rates in states like Alabama, Tennessee, Georgia, Florida are better than national average. And so, we see businesses expanding. Our pipelines today are 50% larger than they were this time last year, and that is broad-based across geography and sectors. We expect to see growth as companies work through the excess liquidity they're holding, begin to rebuild inventories, make investments in property, plant, and equipment as their businesses expand. So, I think there is opportunity to grow. The question will be the timing of that.

And as David mentioned, we are experiencing historically low levels of line utilization. We expect our customers will get back into their lines of credit once they work through the excess liquidity that they're holding. You just don't know what the timing of that will be. It's largely a function of, obviously, economic growth. We're confident that as the economy expands, we will grow loans. Separately, I think we'll continue to see good mortgage production on

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the consumer side and we've got some other initiatives underway related to consumer lending that we think could have an impact as well.

And finally, we're a small business, we're very pleased with our acquisition of Ascentium Capital, we think that equipment finance is an important part of potential growth, particularly in late-2021 and 2022. And so, believe all those things can be drivers of some loan growth to offset, to your point, the headwinds we face with PPP and some of the exit portfolios.

Matthew D. O'Connor
Analyst, Deutsche Bank Securities, Inc.

Q

[indiscernible] (00:37:00) pipeline is up 50% year-over-year. Obviously, COVID was starting to be a drag in the comp a year ago. Do you happen to have that before COVID?

John M. Turner
President, Chief Executive Officer & Director, Regions Financial Corp.

A

Yeah. It's pretty close to – so, the range kind of – if I think back 14 months or so, pipelines would be reasonably comparable, not quite back to late-2019, but pretty near there.

Matthew D. O'Connor
Analyst, Deutsche Bank Securities, Inc.

Q

Okay. Perfect. Thank you.

Operator: Your next question is from John Pancari of Evercore ISI.

John M. Turner
President, Chief Executive Officer & Director, Regions Financial Corp.

A

Good morning, John.

John Pancari
Analyst, Evercore Group LLC

Q

Good morning. Back to the capital discussion, I know you had indicated in terms of capital deployment, potential M&A interest on the nonbank side. Wanted to see if you can elaborate a little bit on what areas on the nonbank side you will consider deals. And then, separately, if you could just talk about potential interest in whole bank deals, clearly, we've seen a fair amount of activity in the Southeast and a lot of banks moving towards bulking up on scale. So, just want to get your updated thoughts there. Thanks.

John M. Turner
President, Chief Executive Officer & Director, Regions Financial Corp.

A

Yeah. Okay. Well, with respect to nonbank, we've been active over the last several years acquiring capabilities in capital markets, low-income housing, tax credits, capabilities, equipment finance, obviously, with Ascentium Capital, in wealth management, Highland Associates or Highland Capital in the mortgage business, mortgage servicing rights, all those things reflect the kinds of interest that we still have. So, to the extent we can acquire portfolios, acquire capabilities that we think will allow us to provide additional services to customers to grow and diversify our revenue, we're active and interested and we'll continue to be.

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With respect to bank M&A, our views still hasn't changed. We think we have a very solid plan. We want to continue to execute that plan. We believe if we do that, we can deliver real value for our shareholders. We'll see the benefits in our stock price and the strengthening currency. And so, we're watching the activity that's occurring. We're evaluating it, trying to learn from it. But our focus is on executing our plans in the markets that we operate in and we think there is a lot of value creation associated with that for our shareholders.

John Pancari
Analyst, Evercore Group LLC

Q

Okay, great. Thanks, John. And then, my second question is around operating efficiency. I know you indicated that your goal is to continue to produce positive operating leverage over time. Your adjusted operating efficiency ratio came in around 56.8% this quarter. Where do you see that going for the full year 2021 and maybe beyond that? Interested in what your thoughts are for 2022. Where is a fair level where that could reach and what's a good run rate? Thanks.

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

A

Yeah. So, you're right, we stay focused on generating positive operating leverage over time. We do that by both growing the revenue and because of the investments that we're making and watching our costs. We feel good about where we are with our efficiency ratio, especially compared to our peer group. Obviously, that gets more challenging as the year goes, as the low interest rate environment and the reinvestment risk puts more pressure on revenue.

You asked about 2022, I haven't gotten to 2022 yet, but if you think about the industry, I think we've got all work towards getting underneath that 55% in time and lower, but you can't do that until you get kind of normalized environment where you have normalized revenue, and if you did that, being under 55% is going to be I think expected. So, in the interim, you get as efficient as you can, but you still have to make the investments to grow revenue and that's what we're doing. So, we've got a number of initiatives in our continuous improvement program that will continue to help us from the cost standpoint, and hopefully, those continuous improvement efforts also help us grow revenue. So, I know I didn't give you a specific point, John, but we'll continue to work to get that number down over time.

John Pancari
Analyst, Evercore Group LLC

Q

No. Thanks, David. That's helpful.

Operator: Your next question is from David Rochester of Compass Point.

John M. Turner
President, Chief Executive Officer & Director, Regions Financial Corp.

A

Good morning.

David Rochester
Analyst, Compass Point Research & Trading, LLC

Q

Hey. Good morning. Good morning, guys. On the liquidity discussing earlier, can you just talk about where your purchase yields are today in securities? And then, what you need to see on the rate front to get you feeling more

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comfortable with shifting more of that excess cash into the securities book over time? And it sounds like you don't have much of that at all in your NII or revenue guide at this point, is that right?

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

That's right. We've said around the edges, we may deploy some of our excess cash. If you go into your general mortgage-backed day, you may pick up 130 basis points. We're still having pressure on the front book, back book of about 40 basis points between loans and securities. So, that's what weighs on us. We really need to see that 10-year getting to [ph] 2%-plus too (00:42:27) and kind of stay there and feel convicted on that before we take the duration risk, because we just don't want to. Again, we don't want to make a short-term play for NII and feel bad about that six months from now, because rates got away from us, and I think we're all seeing the economy improve, but the pace of that we can debate and where that should come a higher rate environment over time. So, in the interim, we're just going to be cautious. We may pick, like I said, a little bit of our excess cash and put it to work, but you should not expect wholesale changes through an investment in the securities book at this time.

David Rochester
Analyst, Compass Point Research & Trading, LLC
Q

Yeah. Okay, great. Appreciate the color there. And then, for whatever reason, you don't end up seeing the loan growth pan out as you expect in 2Q and maybe even into the back half of the year and the cash continues to build, can you just talk about how that situation might impact that investment strategy if at all, and then what are the steps you could take to offset some of that lost revenue? Thanks.

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

Yeah. We continue to, as John mentioned, looking for portfolios and things to really put not only our capital to work, but put our liquidity to work, too, to the extent that deposits continue to come in at the pace they are, one, it'd be surprising, because the growth that we saw primarily this quarter in consumer came from the $1.9 trillion stimulus program that we got in the quarter. So, I don't think we'll continue to see it grow at that pace. But to the extent that it does and we end up our $23 billion into Fed grows materially from that, then we may make different decisions. But I don't think that's a very high probability, we'd much rather again find loan growth by portfolios and put a little bit of it to work in the securities book.

David Rochester
Analyst, Compass Point Research & Trading, LLC
Q

All right. Great. Thanks.

Operator: Your next question is from Peter Winter of Wedbush Securities.

John M. Turner
President, Chief Executive Officer & Director, Regions Financial Corp.
A

Good morning, Peter.

Peter J. Winter
Analyst, Wedbush Securities, Inc.
Q

Good morning. I wanted to follow up on the deposit growth. What I thought was interesting was all the growth came from consumer, and the commercial side was down a little. And do you think that could be an indicator that

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maybe in the second quarter, you start to see commercial deposits coming down and maybe you get that line draw that you're looking for in the second half of the year as the indicator?

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

Peter, I think in the second quarter to see that all of a sudden happen, I don't know, we talk to our customers one-on-one, we believe over time that they're going to probably maintain more liquidity today than they did pre-pandemic. We'll see when we get there, but that's what we're hearing. I think the consumer growth you saw, again, it was based on the stimulus that hit during the quarter. So, I don't expect it to have that kind of growth every quarter, although we're growing customer accounts, too, and we're very pleased about new customer acquisition.

On the business front, in terms of second quarter growth though, I think it's more pushed to the second half of the year as these balances get worked through, their liquidity gets worked through, and as John mentioned, we're in very good markets. We're excited about the growth potential here. So, it's just a matter of time before we see the loan growth. I just don't think you're going hit that breakthrough in the second quarter.

Peter J. Winter
Analyst, Wedbush Securities, Inc.
Q

Okay. And then, just on the premium amortization expense, it was stable quarter-to-quarter at $50 million. If the 10-year were to increase closer to about 2% level, where does premium amortization expense go down to?

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

Yeah. I think if we were to be that high, we're probably down $5 million, maybe $10 million-ish, somewhere there in there.

Peter J. Winter
Analyst, Wedbush Securities, Inc.
Q

Okay. Thanks very much.

Operator: Your next question is from Jennifer Demba of Truist Securities.

John M. Turner
President, Chief Executive Officer & Director, Regions Financial Corp.
A

Good morning, Jennifer.

Jennifer Demba
Analyst, Truist Securities, Inc.
Q

Thanks. Let's go back to everyone's favorite question on M&A. What would compel you to change your stance on the whole bank M&A? Would it be that you can't get below that 55% efficiency ratio over the medium- to long-term or is there something else that you think could compel you to change your attitude there?

John M. Turner
President, Chief Executive Officer & Director, Regions Financial Corp.
A

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Yeah. I think if our view out over the next three years, that's our strategic planning horizon, was that we couldn't continue to deliver improving returns for our shareholders, that we weren't going to perform relative to our peers well, then I think we would have to consider a variety of alternatives. But today, when we think we see a path to continue to grow revenue, we believe we can continue to make meaningful investments in our business while holding our expenses relatively flat. And we think all that is a path to generating nice returns for our shareholders.

And so, our perspective is unchanged, but to your question, it's possible, and that's why we continue to follow the market, try to understand what others are doing and how transactions get structured. So, we're not totally – it's not as if we're not paying attention, I guess, would be my point.

Jennifer Demba
Analyst, Truist Securities, Inc.

Q

Okay. Second question is on credits. Just can you give us some color on how your more COVID-sensitive borrowers are doing now [indiscernible] (00:48:23-00:48:31)?

John M. Turner
President, Chief Executive Officer & Director, Regions Financial Corp.

A

Yeah. Again, in the markets that we operate in, those economies are open and people are beginning to move around. There's a lot of pent-up demand. And as a result, we see hospitality sector, whether it be restaurants or hotels continuing to – their performance continuing to improve. Probably the biggest challenge they face is workforce and hiring people to work. Heard a number of stories sort of anecdotally over the last two-plus weeks about restaurant service being slow in so many places because restaurant owners are having difficulty bringing in their workforce back. But people are getting out and there's I think significant indicators that people are going to be traveling a lot this summer.

And so, again, thinking about the markets we operate in, that bodes well for those economies. The energy sector is doing better for sure. So, all in all, credit continues to improve, and based upon what we know today, we'd expect that trajectory to continue.

Jennifer Demba
Analyst, Truist Securities, Inc.

Q

[indiscernible] (00:49:46).

Operator: Your next question is from Bill Carcache of Wolfe Research.

John M. Turner
President, Chief Executive Officer & Director, Regions Financial Corp.

A

Bill. Good morning.

Bill Carcache
Analyst, Wolfe Research, LLC

Q

Thank you. Good morning, John and David. Can you give us an update on how Regions is thinking about the use of its balance sheet in conjunction with partnerships with finance technology players? How important is it for Regions to own the customer relationships versus what's your willingness to give certain parameters for the kinds of loans that you're interested in originating to finance technology partners and letting them originate those loans for you?

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John M. Turner
President, Chief Executive Officer & Director, Regions Financial Corp.

A

Yeah. Very important to us to own the relationship and we have experimented with partnerships, and in every case, what we were seeking to determine was could we leverage that partnership back into a relationship. And where you see us beginning to exit those partnerships, it is because we awfully concluded that they weren't relationship-building opportunities. We are looking consistently to expand our capabilities to think about how we potentially acquire platforms that we would own that would allow us to originate credit, as an example, to companies or individuals who hopefully could become, would become customers, and Ascentium Capital is a great example of that.

That company had some really good technology, a platform to originate credit, made it easy for customers. We liked it, we saw it as an opportunity to acquire the technology and the capabilities that that very experienced team had to help us grow into the small business space to – with companies that could potentially become Regions' depository customers, Regions' wealth management customers. And so, that's I think the way you'll see us continue to use our balance sheet is to build relationships.

Bill Carcache
Analyst, Wolfe Research, LLC

Q

Understood. Separately, your rationale behind wanting to get your stress capital buffer below 2.5% makes sense simply because of what it signals in terms of credit quality relative to your peers. But can you discuss from a practical perspective, what the significance is given your intention is to run with around 9.5% CET1? So having the 2.5% stress capital buffer on top of your 4.5% minimum would set your minimum capital level at 7%, but since your intention is to run with around 9.5% anyway, is it really that big of a deal to have a little bit higher SCB? Maybe you're looking longer term to a goal of lowering your CET1 target over time, just if you could speak to that would be helpful.

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

A

You get the prize of the question of the day, and you're exactly right. In today's environment, the SCB for us really doesn't come into play. Because there's no way in the world we'd have our spot capital below 7%. I think, as an investor, most investors would have a conniption fit if we did that. So, that was just a piece of it because – but it sends a message when your peers are all under the floor of 2.5% and you're at 3%, it kind of sends this message that your credit quality is worse. We don't believe that and we wanted a very public opportunity to demonstrate that. And that's really what this was all about.

So, I wouldn't say that that gives us an opportunity to run our capital lower. We think our 9.5% in the middle of our range is the right number for us at this time based on the risk we see in our business. If over time risk changes, the outlook changes, we might operate lower than that. But from a practical standpoint, we're not going to get anywhere close to the 7% spot. And so, you're exactly right, it wasn't done just for that purpose.

John M. Turner
President, Chief Executive Officer & Director, Regions Financial Corp.

A

The only other thing I'd add is, every time we participate, we learn something, and I think it helps us continue to develop our thinking about how we manage the risk in our business, the composition of our business, the impact of various stress scenarios on our portfolios, all those things are constructive. And in addition to David's point, I think it's – we have an opportunity to sort of reset and we want to do that. We believe that's appropriate.

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Bill Carcache
Analyst, Wolfe Research, LLC

Q

That's very helpful, John and David. Thank you for taking my questions.

John M. Turner
President, Chief Executive Officer & Director, Regions Financial Corp.

A

Thank you.

Operator: Your next question is from Betsy Graseck of Morgan Stanley.

John M. Turner
President, Chief Executive Officer & Director, Regions Financial Corp.

A

Good morning, Betsy.

Betsy L. Graseck
Analyst, Morgan Stanley & Co. LLC

Q

Hi. Good morning. Just a little follow-up on that, I'm still trying to understand the board approval which, I assume, you requested the size of the buyback that you requested, because when I run that through the model, I'm getting to an ultimate CET1 that's below the range that you indicated today. So, is that board request a function of the max potential that you might anticipate in an environment where the loan book is not growing or I'm just trying to square that, the board request versus the CET1 guide versus the loan growth outlook?

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

A

Yeah. So, the main driver right now would be the CET1 guide. The $2.5 billion that we – or that our board authorized, grants us the flexibility to manage our capital as we see fit without having to go back to the board for another authorization. So, it's going to be a function of how much we make, what's the environment look like, what's our capital levels look like, there are whole host of things that go into that, and that was the level that we felt comfortable that we could run with it and it gives us flexibility to manage accordingly. That's all it's about.

Betsy L. Graseck
Analyst, Morgan Stanley & Co. LLC

Q

And what's the expiry date on that authorization?

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

A

Yeah. It's an open – there's not a date.

Betsy L. Graseck
Analyst, Morgan Stanley & Co. LLC

Q

Yeah. So, it's longer tailed. Okay. And then, the second question just has to do with ESG and the reason I'm asking is that, recently, we've seen several institutions put out their 2021 plans and goals, and we all know what's going on with regard to carbon footprint emission, goals that the global industry has or politicians, et cetera? So, the question here has to do with, how you're thinking about your climate goals as it relates to your work with your customers? You're in an energy-intensive footprint and I know for yourself, you've been very clear on your

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climate-oriented goals and how far along you are for yourself. But I'm wondering, how do you think about working with your customers on this, is this something you would be embracing or give us a sense as to how you're thinking about that? Thanks.

John M. Turner
President, Chief Executive Officer & Director, Regions Financial Corp.
A

Yeah. I think about it from a couple different perspectives. One is just managing the credit risk that's in our book today and the potential impact of climate change and transition on the industries that we bank. We're talking to our customers. We're very aware of potential impacts. We understand the exposure we have within our portfolio. And so, we're actively managing that. We believe that it's important that the banking industry be part of a transition and participate in financing the transition that will occur to a more climate-friendly environment. And so, we want to be actively participating.

We have a very good, as an example, solar capabilities and capital markets capabilities associated with solar, and we are continuing to look for opportunities to develop capabilities that would support the transition to a more climate-friendly environment. And so, we think that's a business opportunity. Beyond that, we have real governance, good governance around, and we spent the last two days in board meetings talking about ESG and our overall ESG plan. We will file our TCFD report midsummer, so that to be in compliance and I think you'll find in our disclosures around ESG to be very broad and on point, so.

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

Yeah. Betsy, I'll add to that. So, we started with our own emissions kind of in Scope 1 and then we went into the vendors that we used and how are they thinking about ESG. We're going into customers and how they do that. So, this is an ongoing process that we'll stay committed to getting that done over time.

I do want to clarify that I misspoke on the share repurchase. That runs through next year, through the first quarter of next year. So, it is not open, it's basically a year.

Betsy L. Graseck
Analyst, Morgan Stanley & Co. LLC
Q

Okay. All right. Yeah. That's why I was a little bit like confused around the messaging you were trying to send with regard to the size of the buyback versus the CET1 range, and I guess, your messaging is, hey, we wanted max flexibility.

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

That's correct.

Betsy L. Graseck
Analyst, Morgan Stanley & Co. LLC
Q

Okay. Thanks.

John M. Turner
President, Chief Executive Officer & Director, Regions Financial Corp.
A

Thank you.

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Operator: Your final question is from Christopher Marinac of J Montgomery Scott.

Christopher Marinac
Analyst, Janney Montgomery Scott LLC

Q

Thanks. Good morning. Just want to circle on the difference between your new loan yields and what was on balance sheet this quarter?

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

A

Yeah. Our total loan, our front book, back book, between securities and loans is about 40 basis points. From a loan standpoint, I think that component is pretty close, it's maybe 10 basis points, 15 basis points, a little more on the securities book.

Christopher Marinac
Analyst, Janney Montgomery Scott LLC

Q

David, as you look at this type of environment, what causes that to narrow or change in the future? Is it something that's possible or will it take a while?

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

A

No, it can change. Your mix – the mix has a lot to do with it, in terms of what you're putting on versus what's rolling off. We have different portfolios we've invested in and we see growth in our small business through our newly acquired Ascentium Capital, does have a tendency to have higher yields that could be helpful. But we are seeing some of our customers access the capital markets and that puts a little pressure on loan growth, and when those clients leave, it's tough to get that replaced at the yield that we had them on. So, as the economy opens, we think we see more activity and we think the rate environment will improve a bit commensurate with that increased economic activity.

Christopher Marinac
Analyst, Janney Montgomery Scott LLC

Q

Great. That's helpful. Thanks very much for all your comments.

John M. Turner
President, Chief Executive Officer & Director, Regions Financial Corp.

A

Thank you.

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

A

Thank you.

John M. Turner
President, Chief Executive Officer & Director, Regions Financial Corp.

Okay. Well, that concludes I think all the question-and-answer. So, thank you very much. I appreciate your participation today and your interest in Regions.

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Operator: Ladies and gentlemen, this concludes today's conference call. Thank you for your participation. You may now disconnect.

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