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Regions Financial Corp. (RF)

Q3 2021 Earnings Call

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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' third 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'll now turn the call over to John.

John M. Turner

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

Thank you, Dana, and good morning, everyone. We appreciate you joining our call today. We're very pleased with our performance this quarter as we achieved earnings of $624 million, resulting in earnings per share of $0.65. Adjusted pre-tax pre-provision income increased 4% sequentially, and we generated year-to-date positive operating leverage.

Our ability to keep the momentum going and deliver solid third quarter results comes from three primary factors. First, we continue to benefit from our growing footprint. Unemployment levels are improving and, in most of our markets, are well below the national level. People and businesses are continuing to move into our 15-state footprint, and that bodes well for our growth prospects for the remainder of the year and into 2022.

We'll continue to make strategic investments in core and growth markets, where we can grow new customers and deepen existing relationships. On that note, we're also pleased to share that year-to-date, net account growth has exceeded account growth has exceeded account growth for the preceding three years combined.

Second, credit quality has demonstrated incredible resiliency and continues to exceed our expectations. Businesses across all industries have found ways to adapt and prosper, despite ongoing supply chain and labor issues, and consumers continue to cautiously manage their finances. Overall, we feel very good about the health of our business and consumer customers.

Third, we continue to take advantage of opportunities to invest in talent, technology and capabilities to support growth. For instance, earlier this month, we closed our acquisition of EnerBank, a leading home improvement point-of-sale lender, a key part of our strategy to serve as a premier lender to homeowners. We also entered into an agreement to acquire Sabal Capital Partners. Sabal has a strong reputation and proprietary technology platform that will expand our real estate capital markets capabilities. Once the transition is complete, we expect to be a top five bank agency producer.

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The EnerBank and Sabal acquisitions complement our existing portfolio price and capabilities in the consumer and corporate bank. We will continue to evaluate prudent non-bank M&A opportunities that will allow us to expand our products and services and enhance our relevancy with our customers. Also, we recently launched our Bank On-certified Now Checking account. This new product has all the benefits of a traditional checking account without the concern of overdraft fees.

And finally, our investments in digital and data are positioning us for growth. Through a technology-enabled seamless experience in branches and across all platforms, customers are responding to the personalized service, advice and guidance they receive from Regions. Today, more than two-thirds of our customer transactions are digital. Further, over the last two years, active mobile banking users were up 23%, and notably, Zelle transactions have more than tripled.

We feel really good about our progress and momentum. We operate in some of the best markets in the country, have a solid strategic plan, an outstanding team and the experience to compete effectively. We focus every day on delivering products and services that are valued by our customers, while continuing to support our communities and provide an appropriate return to our shareholders.

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

David Jackson Turner

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

Thank you, John. Let's start with the balance sheet. Adjusted average and ending loans increased approximately 1% during the quarter. Although business loans continue to be impacted by low utilization rates and excess liquidity, pipelines have surpassed pre-pandemic levels. In addition, production remains strong, with line of credit commitments increasing $2 billion year-to-date.

Consumer loans reflected another strong quarter of mortgage production, accompanied by modest growth in credit card. However, consumer loans remain negatively impacted by exit portfolios and further pay-downs in home equity. Overall, we continue to 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 loan guidance, we are not including any impacts from our EnerBank acquisition, which closed on October 1, and resulted in the addition of $3.1 billion in loan balances that will benefit the fourth quarter and beyond.

So, let's turn to deposits. Although the pace of deposit growth has slowed, balances continued to increase this quarter to new record levels. The increase is primarily due to higher account balances. However, as John mentioned, we are also producing strong new account growth. We are continuing to analyze probable future deposit behavior. And based on analysis of pandemic-related deposit inflow characteristics, we currently believe approximately 30% or $10 billion to $12 billion of deposit increases can be used to support longer-term growth through the rate cycle. Additional portions of the deposit increases could persist on the balance sheet but are likely to be more rate-sensitive.

Let's shift to net interest income and margin. Pandemic-related items continue to impact net interest income and margin. Net interest income from PPP loans decreased $12 million from the prior quarter but is expected to pick up in the fourth quarter. Cash averaged $25 billion during the quarter and, when combined with PPP, reduced third quarter reported margin by 54 basis points. Excluding excess cash and PPP, net interest income grew

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almost 1.5% linked quarter and our adjusted margin was essentially stable at 3.30%. This reflects strengthening loan growth as well as active balance sheet management efforts despite a near-zero short-term rate environment.

Similar to prior quarters, the impact on NII from historically low long-term interest rates was completely offset by balance sheet management strategies, lower deposit cost, and higher hedging income. During the third quarter, we repositioned an additional $5 billion of receive-fixed swaps. We shorten the maturities from 2026 to late 2022.

The repositioning locked in the associated gains that will be amortized over the remaining life of the interest rate swaps and will allow for more NII expansion when rates are projected to increase. Further, with the inclusion of EnerBank's fixed rate loan portfolio, less hedges will be needed to protect NII and the net interest margin profile from falling rates.

The cumulative value created from our hedging program is approximately $1.6 billion. Roughly 75% of that amount has either been recognized or is locked into future earnings from hedge terminations, reflecting the dynamic management of our hedging strategy. Excluding EnerBank and PPP, adjusted net interest income should be relatively stable in the fourth quarter, after excluding the non-recurring interest recovery in the third quarter. Including PPP and the EnerBank acquisition, linked quarter net interest income is expected to grow between 5% and 6% in the fourth quarter.

As illustrated on the slide, over a longer horizon, a strengthening economy, the ability to benefit from higher rates and organic and strategic balance sheet growth are expected to ultimately drive net interest income growth.

Now, let's take a look at fee revenue and expense. Adjusted non-interest income increased 8% from the prior quarter, primarily attributable to strong capital markets activity, including record loan syndication revenue and solid M&A advisory fees. We expect capital markets to remain strong in the fourth quarter, generating revenue in the $60 million to $70 million range, excluding the impact of CVA and DVA. We'll provide more specificity regarding 2022 expectations in January.

Other non-interest income also increased during the quarter due to an increase in the value of certain equity investments, as well as increased gains associated with the sale of certain small dollar equipment loans and leases. Mortgage income decreased quarter-over-quarter, primarily due to mortgage servicing rights valuation adjustments, partially offset by improved secondary market gains.

Service charges remained relatively stable compared to the prior quarter, but we continue to expect they will remain 10% to 15% below pre-pandemic levels. We attribute the decline to changes in customer behavior, as well as customer benefits from enhancements to our overdraft practices, including transaction posting order.

Card and ATM fees remained stable compared to the second quarter. Debit and credit card spend remain above pre-pandemic levels as we continue to benefit from elevated account growth and increased economic activity in our footprint. Given the timing of interest rate declines in 2020 and excluding the fourth quarter benefit from our EnerBank acquisition, we expect 2021 adjusted total revenue to be up modestly compared to the prior year. But this will ultimately be dependent on the timing and amount of PPP loan forgiveness.

Let's move on to non-interest expense. Adjusted non-interest expenses increased 3% in the quarter as higher salary and benefits and professional and legal fees were offset by a decline in marketing expenses. Salaries and benefits increased 4% primarily due to higher variable-based compensation associated with elevated fee income as well as one additional day in the third quarter. Associate head count also increased by 149 positions during the

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quarter, with the vast majority of those within revenue-producing businesses. Further, exceptional performance, particularly in credit, is also contributing to higher incentive compensation.

We will continue to prudently manage expenses, while investing in technology, products and people to grow our business. Excluding approximately $35 million of core run rate expenses associated with our fourth quarter EnerBank acquisition, we expect adjusted non-interest expenses to be up modestly compared to 2020. And we remain committed to generating positive operating leverage over time.

From an asset quality standpoint, we delivered an exceptionally strong quarter as overall credit continues to perform better than expected, reflecting continued broad-based improvement across virtually all portfolios and continued recoveries associated with strong collateral asset values, annualized net charge-offs decreased 9 basis points during the quarter to 14 basis points, representing the company's lowest level on record post our 2006 merger of equals.

In addition to lower charge-offs, non-performing loans and business services criticized loans also improved, while total delinquencies remained unchanged during the quarter. Our allowance for credit losses declined 20 basis points to 1.8% of total loans and 283% of total non-accrual loans. Excluding PPP loans, our allowance for credit losses was 1.83%.

The decline in the allowance reflects better-than-expected credit trends and the continued constructive outlook on the economy. The allowance reduction resulted in a $155 million benefit to the provision. Future levels of the allowance will depend on the timing of charge-offs, greater certainty with respect to the resolution of remaining risk to credit losses, as well as the integration of EnerBank.

Year-to-date net charge-offs are 25 basis points and we expect full-year 2021 net charge-offs to approximate that same level, which includes the impact of EnerBank and excludes the benefits of any future recoveries that may occur.

With respect to capital, our common equity Tier 1 ratio increased approximately 40 basis points to an estimated 10.8% this quarter. As previously noted, we continue to prioritize the utilization of our capital for organic growth and non-bank acquisitions like EnerBank and Sabal that propel future growth. Beyond that, we use share repurchases to manage our capital levels.

Share repurchases were temporarily paused ahead of the EnerBank closing, which absorbed approximately $1 billion of capital in the fourth quarter. We anticipate being back in the repurchase market this quarter and expect to manage common equity Tier 1 to the midpoint of our 9.25% to 9.75% operating range by year-end.

So, wrapping up on the next slide, our 2021 expectations, which we've already addressed, in summary, we are very pleased with our third quarter results and are poised for growth as the economic recovery continues. 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 pace of the economic recovery 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 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 ask about the loan growth. And I was wondering if you could just talk about where the loan growth is coming from on the commercial side and is it more a function of the new account growth that you're seeing?

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

A

Yeah. So, I'd say a couple things. And first of all, we are beginning to see a little improvement in line utilization. Line utilization was up 30 basis points in the quarter, and that trend is continuing through the first couple of weeks of the fourth quarter. Production is up to levels consistent with pre-pandemic levels, so essentially two times what we were experiencing about a year ago. Commitments are up by over $2 billion. And that's largely the result of new relationships that we're adding resulting from disruption in markets that we're operating in and talent we've been able to acquire.

Growth is occurring in some of our specialized industry businesses: transportation, healthcare, financial services, technology and defense are all generating and finding new opportunities. And our pipelines are, again, back at pre-pandemic levels and two times essentially what they were about a year ago, so good activity. Despite labor shortages, supply chain issues constraining the economy a bit, our markets are doing well. Our customers have a positive outlook on the economy and the future. And as a result, we are beginning to experience some loan growth and feel good about the prospects for 2022.

Peter J. Winter
Analyst, Wedbush Securities, Inc.

Q

Great. That's helpful. Can – I wanted to ask about deposit betas. In your asset sensitivity model, can you just talk about what you're assuming for deposit betas today versus how that compares to last time the Fed was raising rates?

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

A

Well, Peter, this is David. So, our deposit betas would have been kind of through the cycle last time kind of upper 30s, 40% range, maybe a little above that. And right now, what we're trying to gauge is the surge deposits, we had some $35 billion to $36 billion of surge deposits, where we said 30% of those, we think, can be put to work. The other 70% is likely to either run off or come at a much higher cost.

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When you think about the 70% of surge deposits, that beta is going to be substantially higher than our core. We would peg that closer to 75% on that component part. But just remember, when – in the last rate cycle, we were one of the lowest deposit betas, and that's the value of our franchise, low-cost, low volatile deposit side and we're looking to extract value out of as we get a more normal rate environment.

Peter J. Winter
Analyst, Wedbush Securities, Inc.

Q

Got it. Okay. Thanks for taking my questions.

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

A

Thank you.

Operator: Thank you. Your next question is from Ken Usdin of Jefferies.

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

A

Morning, Ken.

Ken Usdin
Analyst, Jefferies & Company

Q

Hey, thanks. Good morning, guys. David, I just wanted to ask you to expand a little bit more on your – just how you're thinking about that long-term repositioning. I saw in the deck that you've now locked in or realized 75%. And so, there's always a back and forth here between keeping that income and positioning for higher rates. So, as you think forward and as we get closer to hopeful rates going up, what do you – where do you want to be positioned at that point in terms of the asset sensitivity profile?

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

A

Well, so, our goal is never really to take a lot of interest rate risk and try to win because we've taken big bets. We're trying to gauge where we think rates are going to be. Obviously in 2018, we anticipated rates declining. We put on our forward starting swaps to protect us in the down rate. As we get more confidence that the economy can reopen and that the Fed is likely to raise rates, we want to take some of that protection off, which we've done, and that's what the repositioning of the $5 billion did.

Today, we have about $20 billion of notional protection, receive fixed swaps in particular. We have some others in floors. But for the most part, they're in swap form. And that protection goes through 2022, where we start gauging the fact that there's a little bit more probability of rates starting to rise towards the end of 2022. And we want to participate in that rate environment. So, our slide on page 8 was trying to demonstrate how we hand off from the protection that we have in the low rate environment to let the rates carry us up as the swaps either terminate on their own or because we terminated them as we did with the $5 billion, we locked in that gain and we'll enjoy that benefit through the remainder of the swap period.

Ken Usdin
Analyst, Jefferies & Company

Q

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Yeah. Great. That was good – that is a good new slide. And just on EnerBank to that point about it, can you just help us understand like what you think the originations could be as you look forward to the next couple of years, like what the pace of origination could look like? I know it's going to depend on the environment. But it seems like you can definitely continue to take share as you build that book up.

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

Sure. So, as we've discussed before, that industry is about $175 billion industry annual production each year, very fragmented. EnerBank had represented about 1% of that or call it $1.7 billion of production. I think the top five players in the industry account for right at 10% of the industry. So, it's a – there's a great opportunity for us to really leverage their technology. And we think we can grow that faster than they did. But right now, we're looking at, at least, having that kind of production of $1.7 billion on top of that.

If you look at the yield on the portfolio today, you didn't ask this question, but I'll add to it just so you understand – everybody understands that the yield on that is right at, call it, 6% because of the – we had to mark that $3.1 billion book to market. So, we don't get the fee that's paid by the dealer, which is deferred and amortized as a yield adjustment over time. Our new production, on the other hand, will get that. And so, you're looking at going from a 6% to 9%, 9.5% yield on the new production.

If we could start growing that just a little bit faster than they have, we're going to – this is going to be a nice growth engine for us. And that's what we try to depict a bit on slide 8.

Ken Usdin
Analyst, Jefferies & Company
Q

Perfect. Thanks, David.

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

Thank you.

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 Demba
Analyst, Truist Securities, Inc.
Q

Good morning. Thanks. So, a question for you, on one of the slides, you have a comparison of your loan growth over the last several years versus your peers, which is substantially below your peers. I wanted to know where you want to have it. Are you happy with the level of loan growth that you produced over those years or would you like it to be a little stronger while still maintaining lower loan losses?

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

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Yeah. So, you're referring to slide 21, Jennifer. This is David. And, no, we aren't interested in being second to slowest growing on – as depicted on the page. What we're trying to demonstrate is we had a shift strategically several years ago to focus on improving our risk-adjusted return on capital because we think that's what shareholders wanted. We've gone from second to last in terms of return on tangible common equity. We'll see where we finish, but it'll be four – number four or five this year. And so, it's worked and we've reduced our risk profile dramatically over time.

So, we've exited businesses. So, an example would be our auto businesses. We've gotten out of loan-only relationships that didn't give us the full relationship value that we need and want and where we weren't being paid for the risks that we were taking in things like real estate. So, we did – we've had this massive shift and we've worked through virtually all of that. There's always areas to prune, but we're ready to leverage our markets. We're in fabulous markets that we think are going to grow faster than most, every part of the country. And so, as we – the economy continues to reopen, we have the liquidity and the capital to put to work. And we much rather do that by our stock back. And so, I think, we're looking to improve our loan growth quite substantially relative to what you see on page 21.

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

A

Yeah. And I would just add, I mean, I think we've been pretty consistent to say that we expect over time, assuming that we're not working through exit portfolios and other things, to grow at the rate of the economy as the economy grows, plus a modest amount given the competitive position we have in a lot of markets that we operate in. We ought to get a little more than our fair share, but I don't expect us to grow at an outsized rate relative to the economy over time, there will be periods of time when we can. But in general, we want to grow with the economy [indiscernible] (26:29) and manage our business and a sound profitable way that produces consistent, sustainable and resilient outcomes for our shareholders.

Jennifer Demba
Analyst, Truist Securities, Inc.

Q

Okay. Second question is on capital markets. You said it's going to be probably $60 million to $70 million in fourth quarter. What do you think the revenue opportunity for that business is for Regions over time? I mean, what inning are you in terms of growing the business line?

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

A

Well, it continues to evolve. If you go back to 2014, when we began to emphasize the importance of capital markets and began to acquire and develop capabilities to serve our customers, it really was making very, very modest, almost nominal contribution to the company. And that's obviously changed over the last seven years as we've continued to make investments in the business, we've acquired talent, new capabilities, we've acquired businesses, and we'll continue to do that.

I don't know that there's an upward limit on what the contribution can be. We're certainly very satisfied with the results we've achieved to-date. We've announced earlier this year that we've been approved for a Freddie license to go with our Fannie DUS license. The acquisition of Sabal, which is a fee-based generating business, brings with it additional HUD capabilities, small-balance Fannie and Freddie capabilities to enhance our ability to generate placement revenue.

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We're looking at other opportunities within capital markets to make acquisitions. So, we're going to continue to make investments there. We know that our customers have needs and we want to make sure that we have the capability to meet those needs. And I would expect that that capital markets contribution to non-interest revenue and to the overall profitability of the company will continue to grow over time. I don't see a particular upward limit on that.

Jennifer Demba
Analyst, Truist Securities, Inc.

Q

Thank you.

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

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

A

Morning, Dave.

David Rochester
Analyst, Compass Point Research & Trading LLC

Q

Hey, good morning, guys.

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

A

Hey, good morning.

David Rochester
Analyst, Compass Point Research & Trading LLC

Q

I just wanted to hit capital real quick. I mean, it sounds like you're poised for a pretty sizable buyback this quarter if you're going to wrap up the year at CET1 of 9.5%. So, I just wanted to confirm that that's what you're seeing. And if you could give a rough range around what that could look like from a dollar perspective, that'd be great.

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

A

Well, so we're at 10.8% on common equity Tier 1. Just to remind you, we're going to use about $1 billion of that in the purchase of EnerBank, which closed October 1. So...

David Rochester
Analyst, Compass Point Research & Trading LLC

Q

Yeah.

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

A

...that's a 1 percentage point. So, now you're at 9.8%. Now, you have to put your mind on what we're going to earn back [ph] out to (29:23)...

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David Rochester
Analyst, Compass Point Research & Trading LLC

Q

Yeah.

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

A

...dividend and that's the capital we have left to either; A, invest, John talked about Sabal Capital Partners as a place to use some of that capital. We have other non-bank things we're working on. And we are going to prioritize investments in those non-bank acquisitions before our share repurchase. That being said, our goal is to be at 9.5% by year-end. So, if we don't get a particular deal closed during the quarter, then we'll buy our stock back, because we think 9.5% is an optimum level for our risk profile that we have in the company.

David Rochester
Analyst, Compass Point Research & Trading LLC

Q

Okay. Appreciate that. And then maybe just switching to the liquidity strategy, it sounds like you've got a lot of momentum on the loan growth front, so some of this will, obviously, go towards funding that. But you still have what seems like a lot of excess cash on the balance sheet. So, I was just wondering if you could talk about how the back-up in interest rates that we've seen recently may have impacted how you're thinking about growing that security flows, if at all. And where you're seeing reinvestment rates today on what you're buying?

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

A

Yeah. So, I would [ph] grant you (30:36) we've gotten a better position today than we did at the end of last quarter. But sitting today or at least right now at [ph] 166, 10 (30:45), we would had hoped that would be closer to 2% before we started to redeploy some of that excess cash, because you're just not being paid appropriately for the duration right now. So, our securities – the cash flows we put to work today are going on at a [ph] 1.30%, 1.40% (31:03) spot and they're coming off at about [ph] 1.70% to 1.80% (31:08).

We acknowledge we have a lot of cash. We just, right now, want to be patient, because we think there – if we're patient enough, there's going to be a better opportunity to put that cash to work. What we don't want to do is stretch trying to make a short-term gain and really get ourselves in a pickle because we're upside down in the trade and that's just not who we are. So, being patient, I think, is our best game right now.

David Rochester
Analyst, Compass Point Research & Trading LLC

Q

Okay. Maybe one just – one last one on the funding side. I know you guys have already made a lot of headway on reducing the high-rate borrowings you have. I was just wondering if you see any other opportunities worth mentioning to do that over 2022.

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

A

We really don't. We challenge ourselves all the time and one never knows, I mean, this is – when you have a volatile rate environment, things – opportunities can present themselves as we did last – I mean, this quarter, where we took some expensive debt out. We don't really see that opportunity right now, but we'll keep an eye on it. And if there's a trade there that makes sense for us, we'd do it.

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David Rochester
Analyst, Compass Point Research & Trading LLC

Q

All right. Great. Thanks, guys.

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

Hey. Good morning. Okay, I have a really basic question around just the loan sales that you did, I think, in the quarter. And I know that a lot of what you're investing is in driving future loan growth, so I was a little surprised to see that. Maybe if you could give me some color as to what you're doing there.

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

A

Yeah. Betsy, it's – I wouldn't get, too – and this was not that large. There were some loans that were certainly sitting in Ascentium Capital that didn't really meet our risk profile, that didn't – just wasn't the type of credit we really wanted to have. We had a pretty good bid. We tapped the bid. We made $3 million, so it wasn't all that dramatic. But that's why we did it. If we see things from time to time that we want to offload from a credit risk management standpoint, we'll do it.

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

Q

Okay. And so, the follow-up here is regarding the underlying growth that you see ex-PPP in the C&I and the CRE book. And we know about the supply chain constraints and all of that, but we see some nice growth in some of the services businesses. Maybe you could give us a sense as to where there's an opportunity to deliver on accelerating loan growth as this PPP rolls off or is this current level of non-PPP in C&I, CRE likely just go sideways from here? Just any color there would be helpful.

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

A

No, I think we expect expansion, Betsy. I mean, we're – again, we've seen an increase in unfunded commitments, customers who are contemplating either expanding their business, making investments, other things that would result in growth and loan growth across multiple industries. Similarly, historically, we're going to run in about a 45% rate of line utilization. We ended the quarter just below 40%. And we're, as I said earlier, beginning – we are continuing to see a little bit of increase through the start of the fourth quarter. So, our expectation is that we will experience loan growth across our books of business in the wholesale business in 2022 as labor becomes more available, supply chain issues begin to work themselves out, and customers can put additional capital to work.

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

Q

Okay. And then when you think about the consumer side of the book, what's your [audio gap] (35:05) on that?

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

A

We also think there's a lot of opportunity there, and we talked about EnerBank and our focus on lending around the homeowner. We hadn't talked a lot about strategically why that's important to us, but we know that homeowners maintain 75% higher on average deposit balances. They use more financial services, which result in homeowners providing 62% to 63% more revenue-generating opportunities because they have more basic financial needs. And so, our focus on mortgage, on HELOC and on point-of-sale lending to the homeowner, we think, is a really important strategic initiative. We see EnerBank in particular as an opportunity to grow our consumer lending business; also expect some expansion in card. And related to other activities we have, we think that consumer business will grow again in 2022 and beyond.

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

Q

Okay. Thanks [indiscernible] (36:08).

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

A

Hey, Betsy. This is David. I need to clean up one of my – I told you the gain on sale was $3 million. That number should be closer to $10 million. So, I just want to make sure that got corrected.

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

Q

Okay. All right. Thank you.

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

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

A

Hey, Gerard. Good morning.

Gerard Cassidy
Analyst, RBC Capital Markets LLC

Q

Good morning, John. Good morning, David.

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

A

Good morning.

Gerard Cassidy
Analyst, RBC Capital Markets LLC

Q

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David, coming back to your comments about deposit betas, can you share with us that 70% of the surge that you've put a higher deposit beta on, what gives you the confidence to say that maybe those deposits aren't as sticky as that other 30%? And second, what would make you – or not make you, but what would give you confidence to lower the deposit beta on that 70%? What do you need to see to maybe have a different expectation as we look out over the next 24 months?

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

A

Well, the biggest driver is about the 30%. So, what we've done is we've captured the nature of those deposits and the types of accounts that those deposits have gone in. And we've looked at history, and the nature of the deposit categories implied, some would be retained longer than others. If we miss it, we get that – we will capture more of that 70% than we're thinking. If we started to see in our discussions with our commercial customers in particular that they want to maintain higher levels of liquidity than we think they will, that would be an indicator of being able to put some of that 70% to work longer. We think we're being conservative with that level, but we just need to see how the economy continues to improve. We need to have good conversations with our customers about how they're thinking about it. And there's still uncertainty out there. So, most of the surge is going to be run off is related to business services versus consumer.

Gerard Cassidy
Analyst, RBC Capital Markets LLC

Q

Very good. I appreciate the color there. And then the second, I know there's going to be a number of variables in your answer to this question, you've talked about a moment ago not wanting to extend outside cash on the balance sheet, which is understandable. You talked about your margin, how it's being negatively affected by this excess liquidity. So, the question is, what are you – what type of rate environment do you need to see where that margin degradation is eliminated from your liquidity or is it loan growth where you could reposition some of that liquidity into loans, and therefore reducing it, and at the same time driving up the yields in the portfolio?

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

A

Yeah. It's important. I mean, just strategically, we use our investment portfolios as a – to manage our liquidity, not to drive yield. We don't have a lot of credit risk at our investment portfolio. It's lower than most peers. And we've neutralized really the short-term impacts of rates. What we want to do is get back to what our business is, taking deposits, making loans. And we think we're in great shape and great markets to really leverage that liquidity into loan growth. That's where the driver of improvement in margin will be. We've stabilized our margin for the most part, ex-PPP in cash at 3.30%. And we think that over time, obviously we can grow that and get back to a much higher margin over time.

An example of that is we're going to spend – we have $3 billion of EnerBank loans that we're booking in the first quarter. As I mentioned, that has a carry of about 6% on them. And our new production, consumer guys will add on in a year of $1.7 billion plus, we'll have closer to 9%. So, that and our Ascentium acquisition, which is also fixed rate is performing extremely well. We just continue to just stick to our knitting and execute our plan and our margin will move accordingly, and so will NII.

Gerard Cassidy
Analyst, RBC Capital Markets LLC

Q

Great. Thank you.

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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 ISI

Q

Good morning. On the M&A side, I know you mentioned it a couple of times in terms of non-bank interest, particularly in your capital discussion, maybe can you just elaborate a little bit around the non-bank areas that you're interested in specifically, and then maybe if you can also talk about potential whole bank deal interest as well? Thanks.

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

A

Yeah. So, with respect to non-bank, we've obviously been active particularly in the capital market space. We, within capital markets, announced Sabal. We want to continue to add to our capabilities, whether it be an M&A or in providing access to the capital markets to our commercial customers through a variety of different platforms. Don't have anything specifically in mind, but we're always looking for opportunities.

Mortgage servicing rights has been an area where we've been acquisitive and we want to continue to be. Wealth management, we think there are potentially some opportunities, although lately multiples have been awfully rich. But we want to continue to look for ways to grow that business and other fee income-generating businesses that we think allow us to grow and diversify our revenue and importantly provide capabilities to customers.

With respect to bank M&A, I think we've been consistent in saying that bank M&A is not a strategic priority. We think that bank M&A can be very disruptive. We have a solid plan. We want to continue to focus on executing our plan. The economics of bank M&A have not looked terribly favorable in the past given where our stock traded, continue to experience improvements. So, that changes the economics. We revisit the idea with our board every year as part of our strategic planning process and just come to the conclusion that we think we can generate top quartile returns for our shareholders by being focused on executing our plan, active in the non-bank M&A space. And so, whole bank M&A has just not been a priority for us.

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

A

And, John, this is David. I'll add to the non-bank deal. So, as I mentioned, the prioritization to really focus our capital allocation on growing our bank, the corporate development group works with each of our segment leaders to identify capabilities that they would like to have, companies that they have products and services that we'd love to have to serve our customers.

It's interesting after you do a couple of deals that we've had, you get into the deal flow a little bit more than you would before, and so we get more opportunities. We're going to be prudent about that capital allocation there and make sure things are really accretive for our shareholders as we seek to grow our business, and ultimately our risk-adjusted returns.

John Pancari
Analyst, Evercore ISI

Q

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Great. Thanks, David. And then on the capital markets business specifically, I know – given that you're still investing in that business heavily, what is – and but also given the size it is now, what is the efficiency ratio you're achieving or the comp ratio that you're seeing in that business right now?

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

Well, capital markets is full of about four or five different sub businesses. Some of them have quite nice – nicely up efficiency ratios; others are not so high. We don't really think of it that way. We think of it as much as the capability we need to have that leverages all the other things that we're doing in our business services segment. So, we really look at that together.

Fee-based businesses generally aren't as efficient, but that's okay. And I think as long as they're complementary and we're making sure we're as efficient in delivering those products and services, then we'll be okay. And if you look at our efficiency ratio over time, this quarter, we're the second best in terms of efficiency ratio at 56.6% and looking to improve that over time, even though we're adding some of these other businesses that are less efficient.

John Pancari
Analyst, Evercore ISI
Q

Yeah. Got it. If I could ask one more related thing just about on the comp expense linked quarter, up $14 million. I know on slide 10, you indicated that the performance of the fee business was part of that, plus the day count. How much of that linked quarter increase was purely from the fee performance?

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

Well, we had a – so our – year-to-date, our base salary number is down. Quarter-to-quarter, our base salaries were up just marginally. Most of that was really driven by incentives. And we also had about $5 million in the salary benefit line related to the HR asset valuation that's offsetting expense – I'm sorry – offsetting income, about $5 million. I think if you look through the slide, you'll see that. So, you need to break that out, too, or deduct that, too.

John Pancari
Analyst, Evercore ISI
Q

Got it. Got it. All right. Thanks, David.

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

Yes.

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

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

Morning, Matt.

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

Q

Good morning.

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

A

Hey.

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

Q

Slide 8 has a medium-term potential, not [ph] just income (46:10) growth, but I think it's really helpful and all the drivers and a lot of that's been touched on on the call here. If we were to think about how that might look for fees and expenses, any thoughts on that, either big picture or box some numbers around it?

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

A

Well, you're getting ahead of us a little bit, Matt. We're going to give you good numbers on that in January in terms of what the next few years are, kind of as you wrap up, the expense tied to all this revenue change, our – we've steadily been committed to positive operating leverage, and we've done a really good job of controlling our expense base. We've been around 1% compound annual growth rate on expenses over the last four or five years.

We are seeing a bit of inflation that'll impact us some and our industry, we suspect, in 2022. We've got to find ways to overcome it. And so, we'll give you exactly what that commitment is in January. But the bottom line is we're growing our business. We're going to grow revenue. We're going to work on controlling our expenses and improving returns over time.

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

Q

And then I guess in fees, maybe specifically there, I mean you've talked about a couple of bigger categories in terms of service charges as well as the capital markets, but anything else to comment on kind of medium term for those categories like card and payments and [indiscernible] (47:46)?

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

A

Yeah, I think if you go down a couple line items, the card and ATM fees continue to grow nicely for us. We're up some 12% year-over-year. A big part of that's volume is up. Volume is up because there's more transactions per owner and we have more owners. You have more – when you grow checking accounts, this is what you get. You get usage, in particular debit card usage for us. And so, that's why we get so fixated on making sure the investments we make in the faster-growing markets really help us grow customers and it's paying off. So, you see it in the card and ATM fees.

We've added wealth advisors to help us grow wealth management income. You can see we're up almost 12% year-over-year. And now, part of that's driven by the market. Market's had a nice run, too. And then mortgage income, mortgage has been a little volatile. We've had nice production this year and this past quarter. But 2022, it's probably not going to be as strong as it was in 2021 and 2020.

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Now, we said that for 2021 relative to 2020, and we've had a really nice year. So who knows? But just proud of the fact that we've got a lot of different non-interest revenue sources that work in multiple different economies and rate environments, and our goal is again to continue to grow our total revenue, control expenses and control credit, and we have nice returns to the shareholders.

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

Q

Okay. Thank you.

Operator: Your final question is from David Konrad of KBW.

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

A

Hi, David.

David Joseph Konrad
Analyst, Keefe, Bruyette & Woods, Inc.

Q

Good morning. Hey. I just had a...

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

A

Good morning.

David Joseph Konrad
Analyst, Keefe, Bruyette & Woods, Inc.

Q

Good morning. I had a follow-up question on the securities portfolio, and thanks for the color on the front book, back book. But it looks like securities yields actually went up a couple of basis points this quarter. So, curious if that was lower bond premium amortization and maybe the future benefits of higher rates that you could draw from lower expense there.

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

A

Yeah. I mean, premium amortization is about $50 million. We've benefited a little bit from that. We think next quarter could be a tad lower than that. So, just around the edges, we could see some improvements there. My whole point on that was we're just not going to take risk to juice a quarter or six months. We really want to invest for the long haul and we just don't see putting our cash to work more than we have. Now, we get a different rate environment. We get a little steepness to the yield curve where we get paid for the risk and we might change our mind.

David Joseph Konrad
Analyst, Keefe, Bruyette & Woods, Inc.

Q

And any color on what bond premium amortization was, looking back in 2019, was it significantly lower than $50 million or is it not that material?

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

A

Yeah. Yeah. I don't remember the numbers off the top of my head. We were closer to the $40 million per quarter range. But I hadn't committed that to memory.

David Joseph Konrad
Analyst, Keefe, Bruyette & Woods, Inc.

Q

Okay. Thank you. Appreciate it.

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

A

Okay.

Operator: There are no further questions.

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

Great. Okay. Well, thank you. Appreciate it. We're really proud of the results that we reported this quarter. I think what you see is a reflection of a lot of important decisions we've made over the last few years to strengthen our business, to build a bank that's going to be more consistently performing, resilient, generates sustainable returns, and so we expect to experience more of that in the coming quarters. Appreciate your interest in our company. Thank you.

Operator: Ladies and gentlemen, this concludes today's conference call. You may now disconnect.

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