

# Regions Financial Corporation NYSE:RF

## FQ1 2023 Earnings Call Transcripts

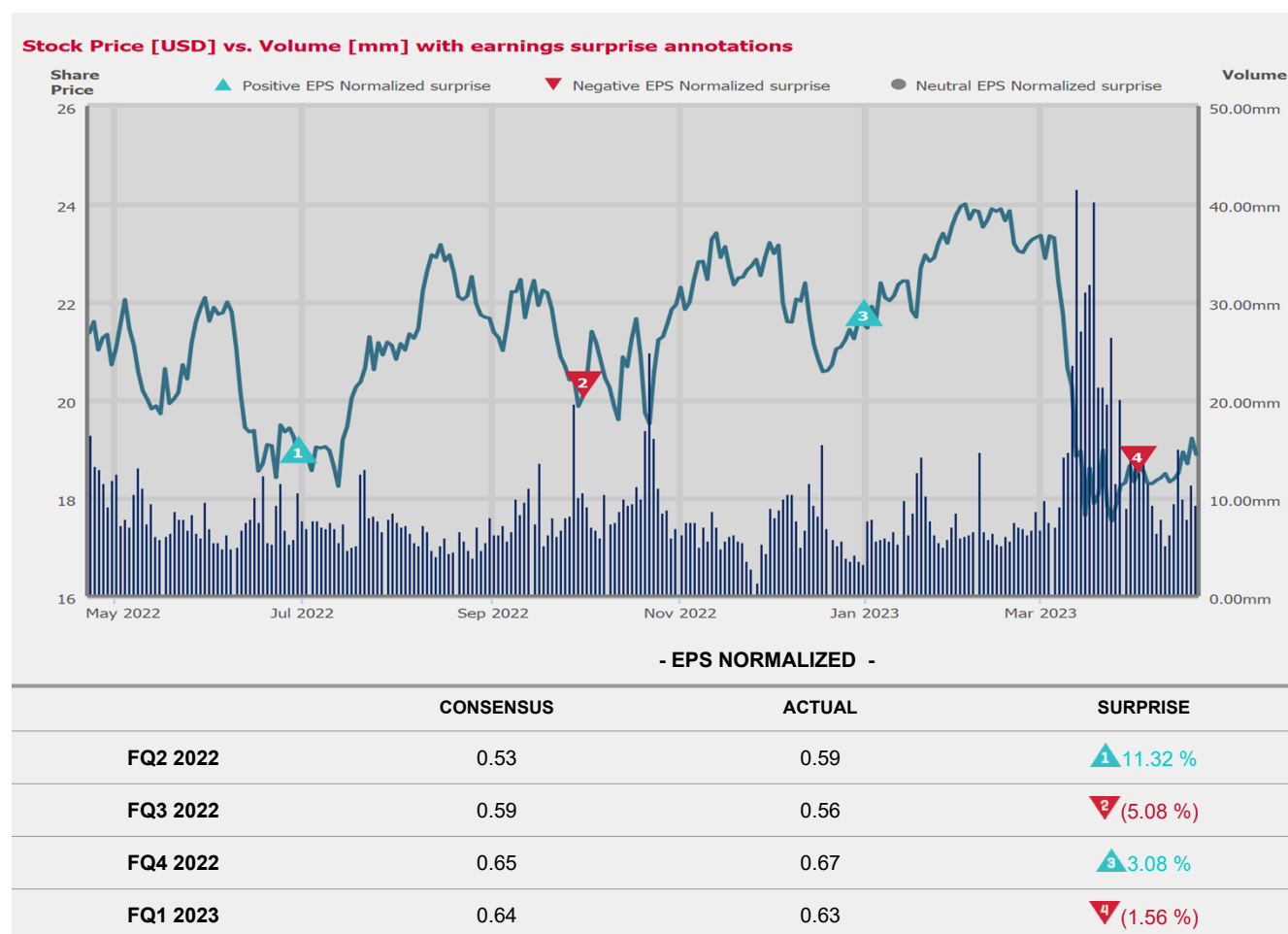
**Friday, April 21, 2023 2:00 PM GMT**

S&P Global Market Intelligence Estimates

|                | -FQ1 2023- |         |            | -FQ2 2023- | -FY 2023- | -FY 2024- |
|----------------|------------|---------|------------|------------|-----------|-----------|
|                | CONSENSUS  | ACTUAL  | SURPRISE   | CONSENSUS  | CONSENSUS | CONSENSUS |
| EPS Normalized | 0.64       | 0.63    | ▼ (1.56 %) | 0.68       | 2.43      | NA        |
| Revenue (mm)   | 1963.07    | 1964.00 | ▲ 0.05     | 1949.82    | 7698.25   | NA        |

Currency: USD

Consensus as of Apr-21-2023 5:20 PM GMT



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# Call Participants

## EXECUTIVES

**Dana Nolan**  
*EVP & Head of Investor Relations*

**David Jackson Turner**  
*Senior EVP & CFO*

**John M. Turner**  
*President, CEO & Director*

## ANALYSTS

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**Gerard Sean Cassidy**  
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**John G. Pancari**  
*Evercore ISI Institutional Equities, Research Division*

**Kenneth Michael Usdin**  
*Jefferies LLC, Research Division*

**Matthew Derek O'Connor**  
*Deutsche Bank AG, Research Division*

**Peter J. Winter**  
*D.A. Davidson & Co., Research Division*

**Ryan Matthew Nash**  
*Goldman Sachs Group, Inc., Research Division*

# Presentation

## Operator

Good morning, and welcome to the Regions Financial Corporation's Quarterly Earnings Call. My name is Christine, and I will be your operator for today's call. [Operator Instructions] I will now turn the call over to Dana Nolan to begin.

## Dana Nolan

*EVP & Head of Investor Relations*

Thank you, Christine. Welcome to Regions First Quarter 2023 Earnings Call. John and David will provide high-level commentary regarding the quarter. Earnings documents, which include our forward-looking statement disclaimer and non-GAAP information 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, CEO & Director*

Thank you, Dana, and good morning, everyone. We appreciate you joining our call today. Once again, Regions delivered another solid quarter, underscoring our commitment to generating consistent sustainable long-term performance. We generated earnings of \$588 million, resulting in earnings per share of \$0.62. Despite recent events in the banking industry, we remain focused on the fundamentals and things we can control.

We've spent over a decade enhancing our interest rate risk, credit risk, capital and liquidity management frameworks. Our relationship-based banking approach, coupled with our favorable geographic footprint uniquely positions us to weather an uncertain market backdrop.

Further, balance and diversity on both sides of the balance sheet have been a key focus for years. As a result, we are well positioned to withstand an array of economic conditions. Approximately 70% of our deposits are retail deposits. These deposits tend to be granular and less rate sensitive. In fact, approximately 90% of these deposits are insured.

Our strategy focuses on primacy and customer loyalty. We want to be our customers' primary banking relationship. This strategy is evident in the fact that over 90% of our consumer checking households include a high-quality checking account, and over 60% of consumer checking deposit balances are with customers that have been with Regions for 10 years or more.

Our wholesale or business services deposits are also highly diversified from an industry, size and geography perspective, with approximately 75% of deposits that are either insured, operational in nature or collateralized. In total, approximately 75% of our deposits across all business lines are insured or collateralized by securities and our deposits are with customers we know is over 97% reside within our 15-state footprint.

Further supporting our high-quality deposit franchise, we had access to total primary liquidity of approximately \$41 billion at the end of the quarter, sufficient to cover uninsured retail and nonoperational wholesale deposits by more than a 2:1 ratio. If you include access to the Federal Reserve discount window, available liquidity increases to \$54 billion or approximately 3:1 coverage. We have a strong team of bankers and the recent disruption has given us an opportunity to connect with our customers and top prospects to answer questions and reassure them of our stability. We've experienced some deposit outflows as corporate treasurers look to diversify and sought higher interest rates for their excess cash.

However, we've also experienced deposit inflows from new and existing customers. Importantly, our total deposits at March 31 were roughly unchanged from what they were prior to the onset of liquidity concerns in the industry. The majority of the \$3 billion deposit decrease this quarter was as expected, due primarily to further normalization in corporate deposits, which had dramatically increased during the pandemic, as well as the continuation of rate-seeking behavior in certain wealth and higher balance consumer accounts.

From a lending perspective, our focus on risk-adjusted returns continues. Overall sentiment among our corporate customers remains positive. While most are forecasting strong performance in 2023, they are expecting modest declines from levels seen in 2022. While current market conditions weren't heightened caution, we believe our strong liquidity profile provides an advantage in terms of supporting our customers' borrowing needs.

In closing, despite all the industry turmoil, we feel very good about our balance sheet and strong liquidity position. And through our proactive hedging strategies, we are positioned for success in any interest rate environment. Our granular deposit base and relationship-based banking model continue to serve us well, and we're proud to continue supporting our customers' banking needs. Now Dave will provide some highlights regarding the quarter.

**David Jackson Turner**  
*Senior EVP & CFO*

Thank you, John. Let's start with the balance sheet. Average loans increased 2% sequentially. Average business loans increased 2% compared to the prior quarter, reflecting high-quality, broad-based growth across the utilities, retail trade and financial services industries. Approximately 87% of this growth was again driven by existing clients accessing and expanding their credit lines to rebuild inventories and expand their businesses.

Average consumer loans increased 1% as growth in mortgage and interbank was partially offset by continued pay downs in home equity and runoff exit portfolios. Looking forward, we continue to expect 2023 ending loan growth of approximately 4%.

From a deposit standpoint, our deposit base remains a strength and competitive advantage with balances continuing to largely perform as expected. Previously, we indicated the combination of rapidly rising interest rates and normalization of surge deposits would likely lead to \$3 billion to \$5 billion of deposit declines by midyear before we would begin to generate net deposit growth.

While the events in March created turmoil in the banking industry, we continue to believe that range is appropriate. However, we may be at the higher end of the range as we approach midyear.

The preponderance of deposit outflows this quarter occurred prior to early March and were in line with our expectations. Approximately \$2 billion of the \$3 billion outflow came from corporate deposits, reflecting normal seasonal activity. The other \$1 billion came from a continuation of rate-seeking behavior among certain wealth and higher balance consumer clients.

The same characteristics that contribute to our deposit advantage in a rising rate environment are also helpful in a time of systemic volatility. As John noted, our focus on attracting and retaining a diverse and granular deposit base with high primacy drives loyalty and trust and instills funding stability. So let's shift to net interest income and margin.

Net interest income continued to expand with market interest rates in the first quarter, reflecting our asset-sensitive profile and funding stability. Net interest income grew 1% linked quarter to a record \$1.4 billion and net interest margin increased 23 basis points to 4.22%. As the Federal Reserve nears the end of its tightening cycle, net interest income is supported by elevated floating rate loan and cash yields at higher market interest rates and fixed rate asset turnover from the maturity of low-yielding loans and securities generated through the pandemic.

At this stage in the rate cycle, we expect accelerating deposit costs through repricing and remixing. Importantly, recent trends remain within our expectation. The cycle-to-date deposit beta is 19%, and our guidance for 2023 is unchanged, a 35% full-cycle beta by year-end. We remain confident that our deposit composition will provide a meaningful competitive advantage for Regions when compared to the broader industry.

Net interest income is projected to grow between 12% and 14% in 2023 when compared to 2022. The midpoint of the range is supported by the March 31 market forward yield curve, which projects nearly 75 basis points of rate cuts in 2023, a stable Fed funds level would push net interest income to the upper end of the range.

The balance sheet hedging program is an important source of our earnings stability in today's uncertain environment. Hedges added to date create a well-protected net interest margin profile through 2025. Forward-starting receive-fixed swaps will become effective in the latter half of 2023, and '24 and generally have a term of 3 years. Activity in the first quarter focused on extending that protection beyond 2025.

In addition to forward-starting swaps, we added a \$1.5 billion collars strategy, selling rate caps to pay for rate floors to limit exposure to extreme market rate movements. The resulting balance sheet is constructed to support a net interest margin range of 3.6% to 4% over the coming years, even if interest rates move back towards 1%. If rates remain elevated, our net interest margin is projected to remain above the high end of the range until deposits fully reprice.

So let's take a look at fee revenue and expense. Adjusted noninterest income declined 3% from the prior quarter as modest increases in service charges and wealth management income were offset by declines in other categories, primarily capital markets and card and ATM fees. Service charges increased slightly as seasonally higher treasury management fees offset declines in overdraft fees.

Excluding the impact of CVA and DVA, capital markets increased 4% sequentially as growth in real estate capital markets, loan syndications, and debt and securities underwriting more than offset declines in M&A fees and commercial swaps. We did have a negative \$33 million CVA and DVA adjustment, reflecting lower long-term interest rates, volatility in credit spreads as well as a refinement in our valuation methodology. Card and ATM fees were negatively impacted by a \$5 million increase in reserves, driven by higher reward redemption rates.

With respect to our outlook, and incorporating first quarter results, we expect full year 2023 adjusted total revenue to be up 6% to 8% compared to 2022.

Let's move on to noninterest expense. Adjusted noninterest expenses increased 1% compared to the prior quarter. Salaries and benefits increased 2%, primarily due to merit and a seasonal increase in payroll taxes. FDIC insurance assessment reflects the previously announced industry-wide increase in the assessment rate schedules.

In contrast to the prior 2 years, we expect first half 2023 adjusted expenses to be higher than the second half of the year. And we continue to expect full year 2023 adjusted noninterest expenses to be up 4.5% to 5.5%. We now expect to generate positive adjusted operating leverage of approximately 2%.

From an asset quality standpoint, overall credit performance continues to normalize as expected. Net charge-offs were 35 basis points in the quarter. Nonperforming loans and business services criticized loans increased while total delinquencies decreased. Provision expense was \$135 million, while the allowance for credit loss ratio remained unchanged at 1.63%.

The amount of the allowance increase due primarily to economic changes and normalizing credit from historically low levels, partially offset by a reduction associated with the elimination of the accounting for troubled debt restructured loans. It is worth noting the outcome of the most recent Shared National Credit exam is reflected in our results.

I want to take a few minutes to speak to our commercial real estate portfolio. Since 2008, we have deliberately limited our exposure to this space. At quarter end, our exposure totaled 15% of loans, excluding owner-occupied and it is highly diverse. This total includes \$8.4 billion of investor real estate and \$6.7 billion of unsecured exposure, of which the vast majority is within real estate investment trust. Our REIT clients generally have low leverage and strong access to liquidity with 68% classified as investment grade.

Importantly, total office represents just 1.8% of total loans at \$1.8 billion. Of note, 83% consist of Class A properties with 62% located within the Sunbelt. The office portfolio was originated with an approximate weighted average loan-to-value of 58% and we have stressed the portfolio to include a 25% discount using the Green Street commercial property price index with the weighted average resulting loan-to-value of the book approximating 77%.

It is also noteworthy that 37% of our secured office portfolio is single-tenant. While we are carefully monitoring conditions, we believe our portfolio will be able to weather the weakness in the industry.

Including first quarter results, we now expect our full year 2023 net charge-off ratio to be approximately 35 basis points. Given the recent economic uncertainty and market volatility, we may see a pickup in the pace of normalization towards our through-the-cycle annual charge-off range of 35 to 45 basis points over time.

From a capital standpoint, we ended the quarter with a common equity Tier 1 ratio at an estimated 9.8%, reflecting solid capital generation through earnings, partially offset by continued loan growth and approximately \$100 million or 7 basis points related to the phase-in of CECL into regulatory capital. Given current macroeconomic conditions, and regulatory uncertainty, we anticipate managing capital levels at or modestly above 10% over the near-term.

So in closing, we delivered solid results in the first quarter despite volatile conditions. We have balance and diversity on both sides of the balance sheet and are well positioned to withstand an array of economic conditions. We are in some of the strongest markets in the country. And while we remain vigilant to indicators of potential market contraction, we will continue to be a source of stability to our customers.

Pre-tax pre-provision income remained strong, expenses are well controlled, credit remains broadly stable, and capital and liquidity levels remain robust.

With that, we'll move to the Q&A portion of the call.

# Question and Answer

## Operator

[Operator Instructions] Our first question comes from the line of Ryan Nash with Goldman Sachs.

### Ryan Matthew Nash

*Goldman Sachs Group, Inc., Research Division*

David, maybe a question on betas and deposit balances. So you guys are one of the few that isn't increasing your deposit beta guidance given that you're at 19% and I think expectations are for 35%. Can you maybe just talk about where you expect the pressure to come from? I think you noted in the remarks, repricing and remixing, how much will each of these contribute? Are you expecting more to be in retail given the push for insured deposits? Or is it on the commercial side?

And then second, you noted that you do expect to see stabilization of growth in balances later in the year. Can you maybe just talk about what you see driving that as we move through the year?

### David Jackson Turner

*Senior EVP & CFO*

Sure. So as we've mentioned before, we had \$41 billion worth of surge deposits. We didn't think those would stay with us as long as they actually have stayed with us. And we furthermore said as rates continue to increase that people would be seeking higher returns than we were offering at the time. And so you can see our cumulative beta, as you mentioned, at 19%, well below everybody else.

We do understand that we're going to end up -- there's going to be a shift of deposits into CDs, more expensive deposits. And so we do also expect some continued runoff. We had given you the guide of \$3 billion to \$5 billion. We're down \$3.3 billion. We expect to be at the upper end of that by the end of the second quarter. And a lot of that is putting money to work in businesses, but also some seeking higher rates.

And so the combination of where we are relative to our deposit costs relative to the peers would imply that we would be increasing some of that over time, and that's going to drive our beta, and we still believe 35% is the right number by the end of the cycle, which we're calling the end of this year.

### Ryan Matthew Nash

*Goldman Sachs Group, Inc., Research Division*

Got it. And maybe as a follow-up, so you guys are now expecting losses at the high end of your previous guidance. It looks like the increase this quarter was driven by C&I. And I think, David, I think you just noted you could see a pickup in the pace of normalization. Can you maybe just talk about, one, what is driving the incremental pressure? And what are you expecting to be the higher driver of charge-offs, both for the rest of this year and then the pace of normalization that we could see?

### David Jackson Turner

*Senior EVP & CFO*

Well, so as we've, I believe, stated many times, the charge-off level is below normal. And that we said it would be normalizing over time. We've furthermore set our normalized loss rate based on the risk profile we maintain is 35 to 45 bps. As we get through the end of this year, we're trying to give you the message that, that could kind of lead you into a run rate towards that 35 to 45 bps by the end of the year. We're already at 35 this quarter, which would imply we expect a reduction in charge-offs in the second and/or third quarter.

But all in, we still think we're going to be at 35 basis points, which is below normal. So we have a lot of confidence in that. We had certain things that happened in the first quarter we don't think will repeat. And so I think our 35 bps is a pretty good number.

### John M. Turner

*President, CEO & Director*

Yes. Ryan, I'd just add to the question about where we're seeing the stress. We've identified a couple of areas on previous calls where we are experiencing some stress in the portfolio. That would be health care, where we're seeing rising costs and pressure on labor. Transportation, particularly on the smaller end of the transportation sector where customers are competing in the spot market to move product.

Consumer discretionary, where consumers are changing their buying patterns and moving away from more discretionary items towards services where we're seeing some pressure, office obviously and then senior housing, which is a sector that we believe is improving but still not returned to occupancy levels that we experienced prior to the pandemic. And again, it's a sector where labor is a factor in the operations of those businesses and driving cost up. So those are all areas where we are seeing more pressure than in the rest of the portfolio.

And I would finally comment, I think we'll see some additional "movement" toward normalization. But we've probably gotten there a little faster than I think we thought we would. So we don't expect a whole lot of additional deterioration as we move towards normalization.

**Operator**

Our next question comes from the line of Erika Najarian with UBS.

**Erika Najarian**

*UBS Investment Bank, Research Division*

My first question is for David. You continue to have that line about a long-term NIM of 3.6% to 4%. I think investors are starting to think about rate cut in 2024, and [indiscernible] always ask about 2024, but I think investors are thinking about how inexpensive bank stocks are really right, trying to evaluate them on what could be trough earnings next year. So if the Fed cuts, can you still stay within that range? And I think nobody is expecting a cut to 0, but perhaps walk us through the scenario of that range in the scenario of like a 200 basis point cut over 1 year?

**David Jackson Turner**

*Senior EVP & CFO*

Yes. So the bottom line answer is yes, we do feel comfortable under any scenario as we mentioned that we would operate in that 3.60% to 4% range. Clearly, our guidance is based on the market. I mean, on the March 31 forward that has 3 cuts, 75 basis points worth of cuts after one increase. So to the extent that were to happen, we will still be within that range. If it stays higher than that, then we'd be at the upper end of the range.

And we have some receive-fixed swaps that actually come on board in the second half of the year to protect us from lower rates. We're not saying that the rates will be cut. That's what the market says. I personally don't see that, that will happen at that pace. But we wanted to be able to center the discussion on what the market is saying, and that's why we gave you that and then we gave you some sensitivity around it. So we feel very good about the range.

Where we are in the range? There are a whole lot of factors. The pace, the timing of cuts would take us down even if we had a couple of hundred basis points of cuts, then '24, we're still in the range. So does that get you what you wanted?

**Erika Najarian**

*UBS Investment Bank, Research Division*

Yes. And as we think about perhaps a more measured pace of cut, how would you anticipate being able to normalize your deposit costs in that backdrop?

**David Jackson Turner**

*Senior EVP & CFO*

Say that again, how would we? Say it again, Erika.

**Erika Najarian**

*UBS Investment Bank, Research Division*

Yes, how quickly could you lower deposit costs in an environment where the Fed is cutting in a measured pace? I'm just trying to think about the other side as I think about your sort of your long-term NIM target range?

**David Jackson Turner**

*Senior EVP & CFO*

Yes. Well, so you can see our deposit cost relative to our peers is 19% [indiscernible] lagging. And so the ability to cut, we have to be competitive. We have to offer a fair price to our customer base. And I think to the extent you start seeing a pause and/or cuts coming

from the Fed. The beta that we just mentioned could change and may not be as severe. What happens is the increase in deposit cost lagged the last increase of -- that the Fed is going to have. So it will take some time for that to manifest itself.

So if you look at the retail side, the retail side is very slow to react. But on the commercial side, it's almost instantaneous as treasurers look to lock in the best yield that they can. We have some index deposits that move with changes in Fed funds. So that will react pretty quickly, which I think is a benefit to us in that scenario.

#### **Operator**

Our next question comes from the line of John Pancari with Evercore.

#### **John G. Pancari**

*Evercore ISI Institutional Equities, Research Division*

In terms of your maintaining the cumulative or through-cycle beta at 35%, I hear you where you're trending down 19% in your confidence. But I'm just curious how the liquidity crisis through March and how it really impacted that outlook. We saw a number of other banks increased their deposit beta expectations given the intensifying pressure around deposit costs as well as broader funding costs. So how has the liquidity crisis impacted your view? And how does that not influence an increase in how you're thinking about the through-cycle data? If you could just walk us through that.

#### **David Jackson Turner**

*Senior EVP & CFO*

Yes, John. So our -- this is our competitive advantage is our deposit base. And so we haven't had to react at the pace that others. So if you look at the incremental beta of our core peer group, that was some 73% this quarter. And ours was 40%, 41%. So we just haven't had to move at the pace and I still think based on how we fund ourselves, the core retail, 70% of our deposits being retail really has helped us from being able to keep that beta where it is at 35%.

So as we think about some of the larger customers that are seeking rates, seeking returns, that's where there's been more competitive pressure and we saw some of that being put to work in the first quarter. And we called for some of that. That's part of the \$3 billion to \$5 billion that we're talking about. As a matter of fact, in our beta assumption, we had all that coming out of noninterest bearing. That wasn't quite what we saw, but we gave it -- we assumed noninterest-bearing because that was more conservative to give you the guidance.

And so if you take all that into consideration, I think that's why you didn't see us change our cumulative beta to 35%. And being at 19%, there's a long way to go from 19% to 35%. We understand that, but if we miss it, maybe it's a tad underneath that, which is why we gave you also some guidance on our Slide #7, that would show you if beta was a little bit better than 35%, how much it might be.

#### **John G. Pancari**

*Evercore ISI Institutional Equities, Research Division*

Got it, David. That's helpful. And then separately on the capital front. I know you increased your target to 10% -- and just if -- or 10% or just above, I believe you said. If you could maybe give us a little bit more color in terms of the rationale. And then could that allow for buybacks at some point? How are you thinking about deployment and the pace of where you -- the timing of when you get to around that 10% range?

#### **David Jackson Turner**

*Senior EVP & CFO*

Sure. So you saw our Common Equity Tier 1 increase from 9.6% to 9.8%, and that's after absorbing about 7 basis points due to the CECL impact for the first quarter. So we're generating 20 to 30 basis points worth of CET1 every quarter. After loan growth, we first and foremost want to be here as a source of strength for our customers and be able to make all creditworthy loans we can make.

And we're open for business and ready to do that. That's what our job is. We want to make sure we pay our shareholders a fair dividend, 35% to 45% of our earnings in the form of a dividend, and we have been at the lower end of that. But -- and then we've used our capital for other nonbank acquisitions and mortgage servicing right acquisitions, which we'd like to continue. And then to optimize our capital, we'll buy stock back from time to time.

Given the uncertainty that's in the market, obviously, there's a lot of review going on to what happened in the month of March, and there's going to be some reports coming out from our regulatory supervisors on what may change. And we just want to be prepared for

that, and we think it would be inappropriate at this time to be buying our stock back when we have this kind of uncertainty. You'll lop on top of that the uncertainty in the economy and monetary policy.

So there's just a lot of noise, which caused us to rethink, let's just wait, let us accrete up to that 10%, maybe slightly over that. And to the extent things settle down, then we'll optimize capital, and we'll use share repurchases as a mechanism to do so.

**Operator**

Our next question comes from the line of Matt O'Connor with Deutsche Bank.

**Matthew Derek O'Connor**

*Deutsche Bank AG, Research Division*

How are you thinking about managing liquidity going forward? Obviously, like with a very strong deposit base, you've been less reliant on wholesale borrowing. But both in light of current conditions and then just kind of the way the regulation might be moving. What are you thinking about in terms of borrowings and then also both cash and securities. And again, like you've got a smaller AFS book than others, which has worked well given the moving rates. But what's the outlook on both the funding and asset side?

**David Jackson Turner**

*Senior EVP & CFO*

Yes. So we still believe in growing customer relationships, core checking accounts and operating accounts of businesses. It's the basis of our whole business, and we'll continue to do that from -- to help us from a liquidity standpoint. Clearly, some things have changed. We've given you a list of our total primary liquidity and also liquidity at the discount window should we need it. What we've learned, I think, over this, is that it can move much quicker than we all had anticipated the world has changed a bit.

And so we've had one of the largest cash balances of anybody in the peer group the lower securities book. And we did that intentionally because we were not clear on the surge deposits on the pace that they would move out. So we'll probably maintain a bit more cash than we historically have been. Obviously, there's -- currently, there's a new term bank facility that the Fed created that's temporary.

I hope there's some thinking about how to maybe keep some of that in place. But we did not use that, as you can tell from our disclosures. But we tested it after quarter end, just to make sure the pipes were worked up and I think we borrowed \$1,000 and repaid it quickly. But posting collateral to something like that, that you can get access to quickly. Clearly, the Federal Home Loan Bank is still our primary source we go to. We have a little bit outstanding there at quarter end, a couple of billion dollars.

And so just having access to multiple levels, if we learned anything, it's diversification. And you need to make sure your funding side is diverse. And within your deposit base, it needs to be diverse. So if you end up with a concentration, you end up with a problem. So I think that's a big lesson learned for everybody and staying as diverse, so we can a little more cash on hand I think, is in order.

**Matthew Derek O'Connor**

*Deutsche Bank AG, Research Division*

And then specifically on the securities book, how would you think about that relative to assets kind of near or longer term with the current framework?

**David Jackson Turner**

*Senior EVP & CFO*

We've historically been in that 20% range of earning assets, and we don't see that changing dramatically. I think we need to be careful. There's been a lot of discussion about shortening up maturities and things of that nature. And we need to be real careful because there could be broad implications of that. The banking system is a big buyer of mortgage-backed securities, and we need to support the mortgage industry and the housing industry and consumers that way. So we are forced to go too short. There are much broader implications to the economy. So we're going to be careful of that.

We'll see what the policymakers come up with and we'll adapt and overcome as we see fit. But right now, I think having a book about where we've been, which is a little lower than others, I think, is the right spot for us based on our -- again, our funding profile.

**Operator**

Our next question comes from the line of Gerard Cassidy with RBC.

**Gerard Sean Cassidy**  
*RBC Capital Markets, Research Division*

John or David, or both of you, obviously, Regions has derisked its balance sheet dramatically from the '08, '09 time period. And so I think you guys are in a good position to maybe handle this question, specifically for commercial real estate, can you guys share with us the differences that you are seeing in the current commercial real estate market in your portfolio versus what it was like in '08, '09. Now granted, I know you've lowered the exposure. So that's a major difference. But in terms of the cap rates, obviously, have moved up, the refinancing risk is here. But can you share with us how you guys could handle that more -- I'm assuming more easily today than what happened in '08, '09.

**John M. Turner**  
*President, CEO & Director*

Yes. Gerard, this is John. I would say we rebuilt our business beginning in kind of the '09, '10 time frame, recognizing that it's very much a specialized business. And we've built it around professional real estate bankers who are working with professional real estate developers. Generally, they are either regional or national developers. They have strong capital positions, good access to liquidity, strong track records. They're operating in some of the primary markets across the U.S.

We rebuilt our business with a focus on concentration risk management. So it's well distributed portfolio is across different segments of the industry as well as across geographies. We have built a business, I think, very conservatively from a structural standpoint requiring good equity in projects.

And we're constantly stressing our exposure. It's a relationship business for us. We're transacting with customers who maintain deposit relationships with us, who use our capital markets capabilities. We're very close to those customers. And as a consequence, I think we have a very good handle on the exposure that we have across the business.

And we have the benefit of operating in some of the best markets in the country as well. If you look at markets like Dallas and Houston, Orlando, Charlotte, Atlanta and Nashville, where we're doing business and where the majority of our portfolio resides. We have good underpinning economy to help support the projects as well.

**Gerard Sean Cassidy**  
*RBC Capital Markets, Research Division*

And maybe, David, on a technical question regarding the commercial real estate, how does the elimination of TDRs now help or hinder your guys working out with some of your customers that may inevitably have an issue with their property?

**David Jackson Turner**  
*Senior EVP & CFO*

Well, we're not going to let an accounting change, change what we're going to do for our customer if we need to have a restructuring then that's what we'll do. And we'll let the accounting is what it is. So I don't think that will impact us at all, Gerard, from moving forward just like we always have.

**Gerard Sean Cassidy**  
*RBC Capital Markets, Research Division*

Very good. And then just as a follow-up question, another technical one for you, David. Can you just remind us about the CECL being phased into capital, just the time range and how that may affect your capital ratios going forward?

**David Jackson Turner**  
*Senior EVP & CFO*

It's roughly the same number you just saw. It's almost a straight line number over, I think, it's 4 periods. So we've got 3 more of these coming. It's \$100 million in round numbers in the first quarter of each of the next 3 years, about 7 points -- I'm sorry, 2 more years. And so it will be about a 7 basis point hit to us each of the next 2 years.

**Operator**

Our next question comes from the line of Peter Winter with D.A. Davidson.

**Peter J. Winter**  
*D.A. Davidson & Co., Research Division*

You guys had pretty solid average loan growth this quarter and did maintain the period-end outlook. Can you just talk about loan demand? And then secondly, if there's any areas maybe where you're tightening underwriting standards or being more selective at this stage?

**John M. Turner**  
*President, CEO & Director*

Yes. So we -- obviously, in this economy, we want to be thoughtful about any new relationships that we acquire and any new credit that we book. I think -- I would like to think that we're not changing our underwriting standards that they are consistent across all economic cycles. But at the same time, when you think about allocation of capital and lending into this environment, we want to be thoughtful and prudent.

We want to make sure that any new business we get as a result of calling activity that's been ongoing for some time. We understand the relationship potential and opportunity that we have a good plan. The bulk of the loan growth that we've experienced in the wholesale business has been loans to existing customers. And in the last quarter, a good bit of the growth was in our industry verticals, particularly in power and utilities, energy and the industrial space.

We're also seeing a little growth within our Regions Business Capital business, asset-based lending business during this period of time. And then on the consumer side, mortgage grew and Interbank grew as a result of putting mortgage because we're generating some arms during the period on balance sheet arms in a period like this. I think loan growth, clearly, or loan pipelines, I should say, on the wholesale side of the business are down.

And I think that reflects caution on the part of customers as well as projects, just the economy is slowing a bit as a result of rising rates and increasing cost. We still believe, given sort of our view of the future and known projects that are either underway or will get underway. There is -- we have an opportunity to grow loans, I think we're guiding to about 4% between now and end of the year and should see growth in the same categories that I just described.

**David Jackson Turner**  
*Senior EVP & CFO*

I think, Peter, I'll add to that, that part of the growth outlook is because of the markets that we operate in. We've been the recipient of a lot of migration of people and businesses into where we operate. And so our economy here is a bit different than certain other economies around the country. And I think that's given us some confidence that our 4% loan growth is reasonable.

**Peter J. Winter**  
*D.A. Davidson & Co., Research Division*

Got it. Very helpful. And if I could ask about the guidance on the deposit service charges, still \$550 million. Question is, how should we think about the second half of the year from the impact of that grace period? Will it step down to, I guess, around \$120 million. And could you offset some of that with just account growth and cross-selling treasury management services?

**David Jackson Turner**  
*Senior EVP & CFO*

Yes. So you can see that our -- if you annualize where we ended up in the first quarter, we would be above the \$550 million, and that's an acknowledgment that our last change of 24-hour grace actually goes in beginning of the second -- of the third quarter. And so you're going to see that step down more so in the third and fourth quarter than you have seen because we hadn't made the change.

One of the things that we've been the recipients of is our treasury management investments we've made on people and technology have really helped offset to some degree, at least, the decline we're seeing from the consumer service charges, and we expect that to continue. So we're up some 8% there in TM. And if this continues at that pace, we might have a better answer for you next earnings call. But right now, we're calling for \$550 million with a step down in the second half of the year.

**Operator**

Our next question comes from the line of Ken Usdin with Jefferies.

**Kenneth Michael Usdin**  
*Jefferies LLC, Research Division*

I just have a follow-up also on the fee side. I know, obviously, it's been a tougher start to the year in capital markets and you're reiterating that 60 to 80 zones that you kind of were in, in the first quarter. Just maybe can you give us color on just how the business is feeling and acting in terms of pipelines and expectations and whether or not you anticipate there being a -- is there a bounce built into your expectation in the second half?

**John M. Turner**  
*President, CEO & Director*

Yes, we do -- can't expect the business to pick up in the second half of the year. It's still I would say, modestly improving, but the second quarter will probably look a lot like the first is our guess. Our business is -- a good bit of our business is built around real estate capital markets and our real estate customers, and that business has just been really, really slow.

And if you look at the component parts of our business, generally speaking, whether it's syndication revenue, revenue generated from fixed income placement or derivative sales has been pretty good over the course of the first quarter. But real estate capital markets has been very soft. M&A was pretty good in the first quarter. We expect that to be true through the balance of the year. So I think we're guiding to pick up in the second half of the year, and we believe that's very possible.

**David Jackson Turner**  
*Senior EVP & CFO*

And just for clarification, make sure, Ken, that when John said you should expect the second quarter to look like the first quarter, that's ex CVA and DVA. So we're talking about the lower end of -- probably in the middle of the 60 to 80 range is about where we would expect that. And we don't expect to have a CVA DVA adjustment, quite as volatile as you just saw this quarter.

**Kenneth Michael Usdin**  
*Jefferies LLC, Research Division*

Appreciate that. Yes. And second question, just on the loan side. As far as the outlook goes, when you think about just the combination of either your supply of credit and the demand of credit? And this changing environment that we're in, just what's happening on the lending side of things in terms of how the environment is changing that? Are you guys tightening up at all? Is it more about the end client that's changing their demand functions?

**John M. Turner**  
*President, CEO & Director*

Well, naturally, in a softening economy, if you will, we are going to probably be a little more conservative, even though I would say that we like to -- as I said a few minutes ago, we like to think that our underwriting standards don't change from economic period to economic period. We are in some very good markets, as David pointed out, and while pipelines are softer, we see people that are -- still have opportunities.

We want to be smart about client selectivity all the time, probably even more so during periods like this. We want to support our existing customers and some 90% -- almost 85% in round numbers of loan growth we've experienced in the last quarter was to existing customers. So we are acquiring some new customers but being very thoughtful about that.

And then separately, while our economies are good, and we do see some opportunity, pipelines are down because of, I think, customer caution related to still difficulty acquiring labor. There are 2 open jobs in the Southeast for every 1 person looking for a job. So labor market is still tight. And costs while moderating have risen fairly significantly, including interest costs, obviously, which puts pressure on projects.

So I think for the balance of the year, we'll probably see pipelines will have moderated and stayed fairly muted, but we believe we can deliver the loan growth that we're projecting despite that.

**Operator**

Our next question comes from the line of Betsy Graseck with Morgan Stanley.

**Betsy Lynn Graseck**  
*Morgan Stanley, Research Division*

In the past, you've talked a little bit about the fact that you're not going to need debt financing for, I don't know, several quarters. And I just wanted to see if you could give us an update on how you're thinking about that, especially as you -- even though your size doesn't

come into the current TLAC expectations there is the potential for that to happen over time. And I wanted to hear how you're thinking about that.

**David Jackson Turner**  
*Senior EVP & CFO*

Yes. So from a debt financing standpoint, we borrowed a little bit from the FHLB as you saw. But the larger term financing, we said we'd push off probably until the second half of the year. We don't know what the regime is going to be, if there will be any change pushed down to us from a TLAC standpoint. At some point, whether we had that or not, we need some more term financing, some term debt that we'll put on. And so I think that we can make sure we deal with that over time.

Betsy, I would say that the changes that are at least being banded around right now. You can't move too fast because we all can't go out there and raise a bunch of debt at the same time. It would be tough for the market to absorb. So I think any change that might be coming relative to that would be over time. And I still think there's going to be some tailoring what that looks like, what that means. We'll have to find out and see what our regulatory supervisors and policymakers decide.

But outside of something like that, and we have a little bit of term debt that we need to get done, and that's really pointed towards the back half of this year. And that's included in our guidance.

**Betsy Lynn Graseck**  
*Morgan Stanley, Research Division*

Right. And that was something that you had been talking about for a while. Just wondering if it's feasible to give us a sense as to size, if that's reasonable or not?

**David Jackson Turner**  
*Senior EVP & CFO*

No, we haven't done that yet. So we're still working out what that needs to look like and precise timing, too. But we don't expect it this first half of the year.

**Betsy Lynn Graseck**  
*Morgan Stanley, Research Division*

Okay. And then separately, could you just give us a sense on the expense outlook that you've got for 2023, the kind of levers that you have to keep the expense guide in the range that you've got 4.5% to 5.5%. And if there's anything in particular that you could point us to in terms of opportunities for efficiency improvements from here.

**David Jackson Turner**  
*Senior EVP & CFO*

Yes, it's a great question. We tried to -- not tried, we gave guidance that our first quarter was going to be a high watermark. I'm not sure that made it into everybody's expectations, but it is what it is. We've now given you guidance again that we think the first half of the year will be higher than the second half of the year. We had some things that we knew were coming in the first half, including we moved our merit month, our merit increase up a month from April to March.

So you've seen that in our first quarter. And in any event, I think when you look at the way to work on expenses. The first thing are salaries and benefits and making sure that you've got the right people, right, a number of the right people doing the right things. And I think that's always a challenge and we continue to look at process improvement, leveraging technology so that when we have attrition, natural attrition, perhaps we don't have to backfill as people if we can move that at the same time.

We've looked at our occupancy. I do think return to work is still trying to find its way and but we likely have more square footage than we need, whether it be in the branch space or the office space. And so we have a team constantly working on square footage, which is our second highest cost. From a technology standpoint, we're having to make room to go through our transformation we're working on right now. And so those costs are going up, and we're able to have cuts in other places to pay for it.

Vendor spend is another area where we really make sure that we limit our use of consultants or contracts with vendors. We just make sure we get the best deal we can, and we have a team working on that. So there is a cost pool in this company that's not going to go through some type of challenge during this year because you don't have a tailwind in '24 for rates. So you've got to do -- start working on your expenses today to help '24, and we're doing that. And so we have pretty good confidence in our expense number that 4.5% to 5.5% right now for this year.

## Operator

Our final question comes from the line of Stephen Scouten with Piper Sandler.

### Stephen Kendall Scouten

*Piper Sandler & Co., Research Division*

I just wanted to ask a little bit about the adjusted revenue guidance. Obviously, I can appreciate that would be down a little bit given the funding pressures industry-wide. But as I look at your results from this quarter, it kind of feels like they were within guidance from last quarter, and the NIM was exceptionally high. So it just feels like you might be ahead of schedule versus having to pair that guidance back. So I'm wondering if you can walk me through the main drivers of that reduction?

### David Jackson Turner

*Senior EVP & CFO*

Well, there are 2 primary drivers. The first is we used in our guidance the March 31 forward curve that had 75 basis points worth of cuts in the year. with 1 increase. So you're down into the \$450 million range by the end of the year. So we then tried to sensitize that. We told you if that wouldn't quite there, how much that may mean. And you can see that on Page 7 of the deck. So that was number one.

Number two, we just had our capital markets was down quite a bit in the first quarter, primarily driven by -- or at least a good portion of it driven by the CVA/DVA adjustment. We don't think that will repeat at that level, but nonetheless, it's in the number. And so you're already down that. So we didn't carve that out as an adjusted item. That's in our core number. Some people adjust it some people don't. What we do is provide that and let you do what you want with it. But when we're giving you guidance, it is in our number -- in our core number.

And so those are the 2 big drivers. We've already given you guidance that our service charge number is likely to go down because we're going to offer a 24-hour grace, and we're not exactly sure what that will mean, but we've taken an estimate, and we've given you the \$550 million for service charges and we'll update as we learn. But those are probably the big 3.

### Stephen Kendall Scouten

*Piper Sandler & Co., Research Division*

Okay. Very helpful, David. And then I guess just one maybe high-level kind of question. I mean it feels like your business model is really proving itself out right now. I mean you're in just a phenomenal position from a deposit perspective and you've diversified your loan book so much over the last few years. I guess, as you look at the environment today, is there anything you would have done differently or anything you would have structured differently, knowing what, I guess, we've learned since March 8 or what have you? Or do you feel like you've done what you would have wanted to do regardless?

### David Jackson Turner

*Senior EVP & CFO*

Stephen, I think we really -- our core of our franchise are our customers and the people that work here, and we have a fabulous customer base, deposit base. We've said that for many, many years, even when rates were 0, virtually 0. And you didn't see the benefit of that rising rates and of course, having a liquidity challenges all proves the business model out.

So we certainly wouldn't change that, and we wouldn't change our focus on thinking of a customer on the right side of the balance sheet in the form of a checking account or an operating account, that's really worked well for us. We brought on some really talented people in our company, in particular, in our technology area. We brought on some very good people in the revenue areas that are doing a great job for us.

And so I just think sticking to fundamentals of banking is what we've done, that's what John has asked us to do. We're not trying to take big bets on anything. We're just trying to keep it down the fairway. And to me, steady as she goes, has been the way and may not be flashy, but it seems to be paying off for us. And I think if we just stay on that soundness, profitability and growth, those are the 3 words John asked us to use in that order. And if we stick to that, we're going to have a pretty good franchise. It's going to be less volatile than many of our peers and certainly less volatile than we used to be pre-crisis.

So I don't see a lot of change. We need to get better and leverage technology in some areas where we're using human capital, and that's just -- that's on the to-do list, and we're trying to get after it.

### John M. Turner

*President, CEO & Director*

Thank you. Well, I know it's been a busy week for everybody. I appreciate your participation today, and thank you for your interest in Regions. We'll end the call. Thanks very much.

**Operator**

Ladies and gentlemen, this does conclude today's teleconference. You may disconnect your lines at this time. Thank you for your participation, and have a wonderful day.

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