Event Name: (CIVB) Civista Bancshares, Inc., Third Quarter 2023 Earnings Call
Event Date: Friday, October 27, 2023, 1:00 PM Eastern Time

Officers and Speakers
Dennis Shaffer; President and Chief Executive Officer
Richard Dutton; Senior Vice President and Chief Operating Officer
Charles Parcher; Senior Vice President and Chief Lending Officer
Paul Stark; Senior Vice President and Chief Credit Officer

Analysts
Nick Cucharale; Hovde Group
Terry McEvoy; Stephens
Tim Switzer; Keefe, Bruyette & Woods
Manuel Navas; D.A. Davidson
Daniel Cardenas; Janney Montgomery Scott

Presentation

Operator: Before we begin, I would like to remind you that this conference call may contain forward-looking statements with respect to the future performance and financial condition of Civista Bancshares, Inc., that involve risks and uncertainties. Various factors could cause actual results to be materially different from any future results expressed or implied by such forward-looking statements. These factors are discussed in the company's SEC filings, which are available on the company's website. The company disclaims any obligation to update any forward-looking statements made during this call.

Additionally, management may refer to non-GAAP measures, which are intended to supplement, but not substitute, the most directly comparable GAAP measures. The press release, also available on the company's website, contains the financial and other quantitative information to be discussed today, as well as the reconciliation of the GAAP to non-GAAP measures.

This call will be recorded and made available on Civista Bancshares' website at www.civb.com.

[Operator Instructions]

At the conclusion of Mr. Shaffer's remarks, he and the Civista management team will take any questions you may have.

Now I will turn the call over to Mr. Shaffer.

Dennis Shaffer: Good afternoon. This is Dennis Shaffer, President and CEO of Civista Bancshares, and I would like to thank you for joining us for our third quarter 2023 earnings call. I am joined today by Rich Dutton, SVP of the company and Chief Operating Officer of the bank; Chuck Parcher, SVP of the company and Chief Lending Officer of the bank; and other members of our executive team.

This morning we reported net income for the third quarter of $10.4 million, or $0.66 per diluted share, which represents a 6.5% decrease from the third quarter in 2022, and net income of $33.3 million, or $2.12 per diluted share, for the nine months ended September 30, 2023, which represents a 22.1% increase over our first nine months of 2022's performance.

Our strong third quarter and year-to-date performance were set up by continued growth in our loan and lease portfolios, which grew at an annualized rate of 18% for the quarter and 10.9% year-to-date. This was organic growth, and I believe is indicative of the strength of our markets and our organization. While we do not anticipate continuing to grow at this pace, we do anticipate continued growth at a single-digit pace for the balance of the year and into 2024.

This growth and the higher rate environment led to higher net interest income for the linked quarter and year-to-date, which translated into record net earnings, which were up 22% over the same period in the prior year.

In the face of funding pressures, our margin compressed, albeit at a slower pace than the previous quarter, coming in at 3.69% for the quarter and 3.88% year-to-date. Our yield on earning assets increased by 3 basis points during the quarter to 5.34% and was 5.29% year-to-date. However, the cost of funding our balance sheet increased by 21 basis points during the quarter to 1.72% and was 1.47% year-to-date.

During the quarter, we continued our measured approach to increasing rates paid on some of our higher-tiered domain deposit accounts and select CDs. This led to an increase in our cost of deposits, excluding brokered, by 18 basis points to 0.67% during the quarter. All in, our funding costs increased by 21 basis points from our linked quarter to 1.72%.

During the quarter, we experienced what has become our typical decline in total deposits, which were down $147 million for the linked quarter. I say typical because the decline was due to the seasonality of the deposits related to our tax business, which were down $187 million for the linked quarter.

As we noted in our earnings release, we made the decision during the quarter to step away from our income tax refund business for 2024. Since the first quarter of 2021, when we mistakenly received $5.6 billion in stimulus payments from the U.S. government, we began receiving an increased volume of complaints from taxpayers looking for their stimulus payments. Since then, the amount of information required by our regulators to close out each complaint has increased. While our business partner TPG handled the brunt of the research related to these requests, it has become apparent that our regulators' view of the program is changing, and we felt it better to step away before it became something that might inhibit future M&A activity. We will look to our new leasing division, other revenue opportunities and tighter expense controls to help us replace this lost revenue next year and into the future.

Yesterday, we announced the quarterly dividend of $0.16 per share. This is consistent with our prior quarter dividend and represents a 24.2% dividend payout ratio based on our year-to-date earnings. Our efficiency ratio for the quarter was 66.5%, compared to 67.9% for the linked quarter and 65.5% year-to-date. However, if we were to back out the depreciation expense

related to our operating leases from our new leasing company, our efficiency ratio would have been 62.6% for the quarter and 61.7% year-to-date. Our return on average assets for the quarter was consistent with our linked quarter at 1.12% and our return on average equity was 11.83% for the quarter, compared to 11.58% for the linked quarter. Year-to-date, our return on assets was 1.24% and our return on equity was 12.88%.

During the quarter, non-interest income declined $1 million, or 11.2%, in comparison to the linked quarter and increased $2.4 million, or 41.7%, in comparison to the prior year third quarter. The primary drivers of the decrease from our linked quarter were declines in lease residuals, fees from our income tax refund processing program and other non-interest income. Consistent with prior years, income from our tax program is earned during the first and second quarters. The primary driver for the increase over the prior year's quarter was $1.9 million in lease revenue and residuals generated by our leasing division. Our leasing division and that revenue stream were not a part of Civista until the beginning of the fourth quarter in 2022.

Year-to-date, non-interest income increased $9.3 million, or 49.1%, in comparison to the prior year. The primary drivers of this increase were $6.2 million in lease revenue and residual fees from the addition of our leasing division in 2022. These fees are primarily made up of operating lease payments and gains on the sale of equipment at the end of the lease term. Also included in other non-interest income was the $1.5-million bonus we received for entering into a new debit brand agreement during the first quarter and $707,000 in interim rent payments generated by our leasing division that we did not have in the prior year.

Wealth management revenues for the quarter were consistent with the linked quarter and declined slightly year-to-date compared to the prior year. While we anticipate that market uncertainty will continue for some time, we continue to view the expansion of these services across our footprint as an opportunity to diversify and grow non-interest income.

Non-interest expense for the quarter of $26.8 million represents a 4.2% decline from our linked quarter, as we experienced improvement in nearly every line item of non-interest expense. Year-to-date, non-interest expense increased $19.1 million, or 30.2%, over the prior year. Much of this increase is attributable to growth from our acquisitions of Comunibanc and VFG in the third and fourth quarters of 2022.

Our compensation expense increased $7.5 million, or 20.4%, over the prior year. The bulk of the increase is due to $6.1 million in additional salary, commissions and benefits attributable to new employees from last year's acquisitions. The balance of this increase is attributable to normal benefit and merit increases.

While we do have seven additional branch offices as a result of our Comunibanc acquisition, the $7.2-million increase in occupancy and equipment expense was primarily due to an increase in depreciation expense on the equipment related to our new leasing division. Equipment under an operating lease is owned and depreciated by Civista until the end of the lease term. Depreciation related to operating leases was $6.1 million year-to-date. The increase in other non-interest expense was primarily due to a $595,000 provision for credit losses on unfunded loan commitments; that was a new expense category resulting from our adoption of CECL in January.

Like many in the industry, we experienced an increase of $353,000 in bad check losses year-to-date. We also experienced $608,000 of increases in a number of other expense categories related to our new leasing division.

Turning to the balance sheet. Year-to-date, our total loans have grown by $208.2 million, which includes $32.9 million of loans and leases originated by our leasing division. This represents an annualized growth rate of 10.9%. A number of banks in our markets have curtailed their lending efforts, which we view as an opportunity; opportunity for new and expanded lending, opportunity to increase our spreads on those loans and opportunity to require new and increased compensating deposit balances.

While we experienced increases in nearly every loan category, our most significant increases were in non-owner-occupied CRE, residential real estate loans and lease financing receivables. The loans we are originating are virtually all adjustable-rate loans and our leases all have maturities of five years or less. Loans secured by office buildings make up 5.5% of our total loan portfolio. These loans are not secured by high-risk office buildings; rather, they are predominantly secured by single- or two-story offices located outside of central business districts. Along with year-to-date loan production, our undrawn construction lines were $239.5 million at September 30. We anticipate loan growth to moderate to a low-single-digit rate for the balance of 2023 and into 2024.

On the funding side, total deposits increased $175.8 million or 6.7% since the beginning of the year. However, if we were to back out non-core tax program and brokered deposits, our deposit balances declined 1% year-to-date. When compared to what we are seeing across the industry, we believe this illustrates the strong relationships we have with our commercial and retail customers. Our deposit base is what we would term as fairly granular, with an average deposit account excluding CDs of approximately $26,000.

Non-interest-bearing demand accounts continue to be a focus. Excluding tax-related and brokered deposits, non-interest-bearing deposits made up 30.2% of the remaining total deposits at September 30.

With respect to FDIC-insured deposits, excluding Civista's own deposit accounts and those related to the tax program, 14.5%, or $404.5 million, of our deposits were in excess of the FDIC limits at September 30. Our cash and unpledged securities at September 30 were $430 million, which more than covered these uninsured deposits.

Other than $361.1 million of public funds with various municipalities across our footprint, we had no concentration in deposits at September 30. At September 30, our loan-to-deposit ratio, excluding deposits related to our tax refund processing program, was 101%.

As I mentioned, we are having success requesting additional deposits and compensating balances from our commercial customers, and we will continue to be disciplined in how we price our deposits, and we will take advantage of brokered funding when we think it makes sense. We believe our low-cost-deposit franchise is one of Civista's most valuable characteristics, contributing significantly to our strong net interest margin and overall profitability.

At September 30, all of our $595.5 million in securities were classified as available for sale and we had $93.1 million of unrealized losses associated with them, which puts pressure on our tangible common equity. At quarter end, our tangible common equity ratio had declined to 5.5% as compared to 5.83% at December 31, 2022. Despite this decline, our Tier 1 capital ratio at September 30 was 8.79%, which is well above what is deemed well capitalized for regulatory purposes.

Civista's strong earnings continue to create capital and our overall goal remains to maintain adequate capital to support organic growth and potential acquisition. We continue to believe our stock is of value, and as such, we've resumed our repurchase program during the third quarter. During the quarter, we repurchased 84,230 shares of common stock for $1.5 million, for an average price of $17.77 per share. This represents all of our repurchase activity year-to-date. We have an authorization of approximately $12 million remaining in our current repurchase program.

While our capital levels remain strong, we recognize our tangible common equity ratio screens low and will balance our repurchases and the payment of dividends with building capital to support growth.

Despite uncertainties associated with the economy and the expense pressures our borrowers face, our credit quality remains strong and our credit metrics remain stable. We did make a $630,000 provision during the quarter, which was primarily attributable to loan and lease growth. Our ratio of allowance for loan losses to loans improved from 1.12% at December 31, 2022, to 1.28% at September 30, reflecting growth and our adoption of CECL during the first quarter. In addition, our allowance for loan losses to non-performing loans increased from 261.45% at December 31, 2022, to 308.52% at September 30.

In summary, although we experienced margin compression, we continued to generate strong earnings and our margin remains strong. While we experienced exceptional organic loan growth during the quarter, we anticipate a slowdown in loan growth as we finish out the year. While we continue to examine and stress our portfolios, we have seen no material deterioration in our credit quality. Our focus continues to be on creating shareholder value, which is evidenced by the year-over-year increase in our earnings per share and hopefully will eventually be rewarded.

Thank you for your attention this afternoon, and now we'll be happy to address any questions that you may have.

Questions & Answers

Operator: [Operator Instructions]

The first question comes from Nick Cucharale with Hovde.

Nick Cucharale: Just wanted to clarify the loan growth outlook. Are you suggesting that early indications are for a slowdown in loan growth for 2024 to a low-single-digit pace? Did I hear that correctly?

Charles Parcher: Yes, I'd say to low to mid-single digits. I mean, I would say, ball park, 5% maybe, Nick, from my perspective. Somewhere in that range, I would think. We're seeing, obviously, loan growth's been great and our pipelines are really strong right now, but we just -- we're starting to see some slowness from the economy.

Dennis Shaffer: And Nick, I think some of it will be us being a little bit more selective. We have to push our interest rates -- we've got to get our spread, because our loan-to-deposit ratio is so high, so we have to push our spread, and those spreads are widening for us, so we anticipate that higher rate environment will slow lending activity as well.

Nick Cucharale: Yes, makes sense. Just to pivot over to expenses, was there anything irregular in the results that drove the outperformance relative to the guidance? And any sense of where that may shake out in the fourth quarter?

Richard Dutton: I don't know if I'd use the term irregular, but yes, I think in the fourth quarter, what we did, we had a -- I think it was -- we're self-insured for health insurance, and it's hard for us not to do what the actuaries tell us to do until we get close to the end of the year, and our employees tend to be a little more healthy, I guess, than what the actuaries thought they were going to be. So we backed out -- that was the big, I guess, decline in the compensation number in the fourth quarter, was that we've kind of reduced the accrual, Nick, on health insurance.

I think I told you guys $28 million would be our run rate last quarter; it looks like you guys heard me. I don't know what to tell you; a good rate from the fourth quarter is probably $27.5 million. I don't know that I would want to go into next year, as there's a couple things moving around, but I think that was a good number for the fourth quarter, and it won't be a whole lot different than that. And again, we do raises, merit raises, the first part of April, so they're not really impacting the first quarter, and we've gotten some pretty favorable pricing on our health insurance, the re-insurance piece of it that we use to kind of base our expense on. In fact, we had no increase during that renewal, which I thought was kind of phenomenal. But anyway, those are the big things, Nick.

Nick Cucharale: Yes, that's great color. Historically, the fourth quarter is an especially strong period for the leasing business; is your expectation that you see a material pickup in sales and lease revenue during the fourth quarter relative to the September period, and if so, can you help us quantify that impact?

Dennis Shaffer: Well, we do anticipate it to increase. We were just on a call with them yesterday, Chuck. It looked like they're going to double what they did in September, so --

Charles Parcher: Yes, I think we probably need to get back with you, Nick, on quantification number, but we do expect higher production and outputs in the leasing division in the fourth quarter.

Nick Cucharale: Appreciate that. And then lastly, do you expect to take any charge given your announcement that you're going to be exiting the tax business?

Richard Dutton: No, no charge. I mean, I think it'll just be that the revenue that we incurred or earned, I guess, in each of the first two quarters for the last number of years, that just goes to zero.

Nick Cucharale: Yes, [indiscernible] income statement impact, then. Okay.

Dennis Shaffer: Yes, yes. And we'll look to replace that income. I think we've got -- we've -- well, we think we have opportunity through our leasing division as well as current revenue -- we've identified two revenue opportunities within our existing products and services, and I think we'll have -- we're -- we'll have tighter expense controls as we move into next year, so we're still working through the budget, so we really can't quantify any numbers there, but we're looking to kind of make it a neutral -- as neutral of an impact as possible.

Operator: The next question comes from Terry McEvoy with Stephens.

Terry McEvoy: Dennis, I think your comments on the income tax refund business in the press release were pretty clear, as is the $2.4 million of fees. What amount of deposits do you still have on the balance sheet connected to this program? And when do you expect them to completely run off? And that run-off -- I noticed the uptick in FHLB or short-term debt; will that level kind of be consistent or potentially grow from here?

Dennis Shaffer: Yes, we'll maintain some of those deposits as just a certain percentage that sticks around, that we'll have to achieve over the next five years or so. But Rich, do you have the balances there?

Richard Dutton: Yes, at September 30, Terry, we had $73.4 million on our balance sheet, and I think at the beginning of the year, that number was -- I want to say $40 million. I may not be exactly right, but it's close. And that's that number that Dennis said that, for whatever reason -- I mean, it's a small percentage of folks that ask for us to give them their refund via check, and then I don't know if they died or lost the check or whatever, but those checks, a percentage of them just don't ever get cashed, and those will remain on our balance sheet, again, for what is typically five years. Each state's a little different, but I think for the most part, that will run out or spin down over the next five years.

Terry McEvoy: And where were the peak in balances this year? Where did they peak out? Any guess or any feel there?

Richard Dutton: Oh, yes, I mean -- I think the average -- you've got me flipping through my notes here.

Dennis Shaffer: We had about $174 million in reduction, I think, in tax deposits for the quarter, so --

Richard Dutton: So the year-to-date average, Terry, was $169 million through the first three quarters. It peaks, as you would think, in the middle of the second quarter, right after March-ish kind of thing. That's when most of it comes through.

Dennis Shaffer: But that money, Terry, was moving in and out much quicker the last two years than it had the previous, say, five years, for whatever reason. We really didn't know. But our funding as we move forward is going to have to rely on more brokered and FHLB borrowings and things like that, and we'd hope to offset that funding by pushing our loan yields higher.

We think we can do that just because there's been a number of banks that have gone to the sidelines, you know? The big banks generally fear recession, so they kind of go to the sidelines, and then there's a number of other banks that I think are in the same situation. The balance sheets are pretty levered up and they've chosen to stop lending. And we're not going to stop lending, but our lending will probably slow just because we've got to push rates, those spreads, higher in order to do some of those deals, but we view it really as an opportunity to pick up core deposits and other deposit relationships because if we're going to do the loans and no one else is lending, we're going to require much more of those deposits or all of those deposits.

Terry McEvoy: Makes complete sense. The bad check loss, is that just a one-off situation? Is that just what you're seeing across the bank, which I think is consistent with the industry, or -- and do you think that level continues from here on the expense side?

Richard Dutton: We wish it was one, and there are no big ones, but there were -- just a phenomenon that I think we're all, in the industry, trying to figure out. If we could get everybody to switch over to positive pay, that would be a huge help for us, and our [indiscernible] management folks, I'll tell you what, they've been selling the heck out of it. But apparently they're just not selling them fast enough.

Dennis Shaffer: Well, they're -- we're trying to -- we have a big campaign, an awareness campaign, that we're doing on social media. We're doing it through our digital sign-on, our online banking, just to make our customers aware, but fraud is really prevalent. We are working, along with a number of other banks, with our banking associations here in Ohio and our regulators -- I was at a regulatory meeting three weeks ago, and this was a topic of discussion. But we've just got to raise the level of awareness for all of our customers, because the fraud piece of it has really picked up throughout our industry.

Terry McEvoy: Yes. And maybe one last one. The decision to exit the income tax refund business, as you mentioned, the release might get in the way of future bank M&A, so it sounds like that was part of the decision, on top of the number of complaints. So the level, maybe, Dennis, of conversations you're having with potential partners -- clearly there's some interest rate marks and financial obstacles to get over, but what's your outlook for bank M&A for Civista?

Dennis Shaffer: Well, I think -- you know, I think it's tough right now just, as you mentioned, just to do any type of M&A given where stock prices are and loan marks and marks on security portfolios and things like that. So it's just tough to make that math work. We are continuing to

have dialogue, and we're meeting with potential partners, so those discussions are ongoing. I just think it makes it -- whether you're a buyer or a seller, the math is really hard to do right now. We have looked at a couple of smaller deals that were announced earlier in the year; we just couldn't make those, you know, the math work. And I don't see that easing up in the near term, but we have to continue with the discussions, because the minute you stop, you kind of lose that -- a little bit of that -- maybe that relationship and stuff, so I just think you have to continue those discussions and -- because certain banks are going to be under more pressure than we are, and they're going to want to partner up, and we want to make sure we're top of mind. So we'll continue to have meaningful discussions with people that we view as good partners.

Operator: [Operator Instructions]

The next question comes from Tim Switzer with KBW.

Tim Switzer: I'm on for Mike Perito. First off, do you have what the purchase accounting impact was to the margin this quarter? I think last quarter it was around 8 basis points and had some, like, prepayments. I'm wondering if that settled down at all.

Richard Dutton: It's almost identical. We computed it at 7 basis points this quarter, Tim.

Tim Switzer: Okay. Is that, like, kind of a good run rate going forward or should it move back down once prepayments moderate?

Richard Dutton: I would use that until we tell you different. How about that? So if you're wrong, you'll only be wrong for a quarter.

Tim Switzer: Sounds good. And could you guys talk about your expectations for the NIM going forward? I would expect a little bit of moderation on the compression, still, next quarter or two, but like, when do you think you could really trough here?

Richard Dutton: Well, I think one thing I'd like to say to kind of set the table is I think as we've increased our funding and a little more reliance -- not reliance, but we've not reduced the deposits that we have. I mean, they were only down, like Dennis said, 1%. But we've got more overnight borrowing and we've got more brokered, short-term brokered CDs. Our balance sheet has gotten more neutral than it was. We used to talk about being asset-sensitive; it's really a pretty low balance. When we ran our model at the end of Q3 and looked out, rates up, it's really flat for the first, at least, 100 basis points movement. I'd be surprised if you think rates going to go up more than 100 basis points. And breaks down, for each quarter point down, our model shows our NIM compressing at something less than 5 basis points for every quarter point move. So again, are we at the trough? I guess the model says we are. I guess the other thing I would say is, if our margin for the quarter was 3 --

Dennis Shaffer: 3.88% or 3.69%.

Richard Dutton: Well, 3.69%, and our margin year-to-date was 3.88%, I mean, that would indicate that maybe there's still some room for it to kind of compress a little bit, but not -- nothing like we've experienced, I don't believe, in the first -- or the last two quarters.

Dennis Shaffer: Yes, we may see similar impact in the fourth quarter just because of that reliance on the brokered and stuff. But we really don't -- as we get through that, we think it's tough. I'm surprised, as I talk to other banks, we haven't given up all the margin. If you look back at the end of '21, our margin was 3.47%. So I think we haven't given all that margin back up, so we may -- I think we were -- we -- our deposit beta didn't move as quick the first two quarters as it did in the last quarter and -- I'm sorry, the fourth quarter of '22 and the first quarter of '23, our deposit beta didn't move like other banks did. It did, then, start moving much more rapidly in the second and third quarter, and we'll probably have further compression here into the fourth quarter.

Tim Switzer: Okay, okay. So at least another quarter or two of compression and possibly the rate should stabilize.

Dennis Shaffer: Right.

Tim Switzer: Okay, yes, that makes sense. And the last question I had was, you guys stepped back and started to do repurchases again; you made the comment that you like the value of your stock here. Any insight you can give us on if you'll continue to do that and use the rest of your authorization over the rest of the year and into '24?

Dennis Shaffer: Well, I think as I mentioned in the comments, we just recognize that that tangible common equity ratio is -- it just screens low, into the ratios lower this quarter than it was the previous quarter, so I think it makes repurchasing your stock a little bit tougher, but we'll continue to be mindful of that and try to balance the repurchases and the payment of dividends with building capital and supportive growth. We -- I don't anticipate repurchase activity to really --

Richard Dutton: At the levels it has been for the last couple of years.

Dennis Shaffer: Yes, yes. So I think it would be tough to burn through that authorization.

Richard Dutton: Tim, I want to make one clarification. Dennis said he thought it was a value. He did not say he liked where our stock price was.

Dennis Shaffer: That's right.

Operator: The next question comes from Manuel Navas with D.A. Davidson.

Manuel Navas: Just wanted to follow up on the NIM a little bit. Are you seeing similar compression to the third quarter and the fourth quarter or first quarter, or is that compression going to become a little less as you pursue other deposit opportunities? Can you just kind of clarify that a little bit, that progression?

Richard Dutton: Well, I think the compression was a whole lot more from one to two than it was from two to three, and I think what we're seeing is probably that 17 basis points of compression that we saw in -- or over the course of Q3 is probably a good barometer of what we might anticipate.

Dennis Shaffer: [Indiscernible] -- fourth quarter, in the fourth quarter.

Richard Dutton: Right.

Manuel Navas: And then, perhaps a little bit less compression into next year [indiscernible]?

Richard Dutton: Correct, [indiscernible]. Correct.

Manuel Navas: And this is -- and then at the point -- if we have no more hikes, and we're staying at 5.50% for the final -- for into '24, is there a point in '24 where you could start to see the NIM inflect, or would it just stay stable after it's done compressing?

Richard Dutton: I think it would be more of a stable kind of a scenario, Manuel. I think we're, you know, 100% wound up, ish, so that makes it -- not a whole lot of levers to pull, and we're -- everything that -- every bit of growth that we have incrementally, we've got to go out and fund it, and that makes it hard to expand for sure.

Dennis Shaffer: And our modeling kind of shows it. Rates up, rates down, it's pretty neutral.

Richard Dutton: Right.

Charles Parcher: [Indiscernible] that part right now, Manuel, is that we are slowly seeing -- as Dennis mentioned earlier -- we're slowly seeing our loan rates increase month over month from a production perspective, and obviously, all the ones that roll right now are rolling at a significantly higher price.

Manuel Navas: Okay. Is -- can you talk a little bit about kind of the -- where you're focusing on for deposit gathering? Because I'm sure that's kind of a wild card for you, that you could have less wholesale funding if all the focus initiatives that you have out there on the deposit side will act to form.

Dennis Shaffer: Yes, a couple things here. One, the commercial deposits that we mentioned, we're really pushing hard to say, look, with certain banks not lending, we're saying, if we're going to do your deal, we've got to have all these deposits. So we need those compensating balances [indiscernible] --

Richard Dutton: And we're having success with it.

Dennis Shaffer: Yes, and we're having pretty good success with that. We're having pretty good success with that, so that's one focus. We have streamlined our small business, the way we

process small business loans, and that is set to kick off here in the fourth quarter, and we think that will make it easier for our people to kind of process -- go after those loans and process those loans. We'll also look to just check out a micro loan through our retail division, which we don't have, because a lot of those small business loans are self-funding. So -- but those are two areas where we're really focusing on, and then we continue to work on our digital app to get -- we're not fully maximizing its capabilities yet, but we'll continue to work on that to add differentiating services that may drive people to that app, and we can open accounts through that app, and things like that, so those are a couple of things that we're working on to try to gather additional deposits.

Manuel Navas: Okay, that's great. Just shifting over, equipment leasing growth seemed to be a little bit less this quarter. Just -- is that still coming on at 9% yields, and are the expectations pretty much unchanged for the year?

Dennis Shaffer: The yields are higher. The yields are -- the yields for at least September were 10%. And as Chuck indicated on the commercial side, even deals that are going on in October have made an increase since the September 30 rates, so yes, volume was a little bit less than we had anticipated for that third quarter, but pipelines are really good, so we do anticipate that volume in the leasing groups to be up quite a bit in the fourth quarter.

Charles Parcher: Probably just a little bit less -- probably just a touch less, Manuel, than what we guided for the full year, but we think we'll close the gap here in the fourth quarter.

Manuel Navas: And you can always choose to sell more of that if you have any balance sheet constraints.

Dennis Shaffer: Right. That's exactly right. We are getting paid less on it for the people purchasing it, so we try to weigh that, but yes, we may end up having to do that. Right now, we modeled it going in at keeping 50% and selling 50%; that's kind of what made the earn-back numbers work -- we felt made it work, and so far we've been sticking to that, but we may have to shift course depending on liquidity needs.

Operator: The next question comes from Daniel Cardenas with Janney.

Daniel Cardenas: You had mentioned on the call that that $2.4-million revenue hole was going to be plugged through increasing your leasing and some revenue opportunities within your current products and services and some expense controls. I guess, if you had to assign percentages, how would that work out, and how quickly do you think you can fill that hole?

Dennis Shaffer: Well, we hope to gain a chunk of it through the leasing group, because as they became -- they were an unregulated, privately held company, and so we had additional expenses in there, consultants that we've had to hire, we had to have some of them -- this included accountants and IT people and different things. That should be behind us for the most part, so we hope to pick up some there. We hope to build a little bit more cadence now. I can tell you, the activity the last four or five months has been much better than the first four or five months of the year, Dan, so if we just continue now to do what we're doing, we're going to make up those first

four or five months where we weren't really extremely profitable in that -- with that group. Just because we were -- they were kind of sidetracked toward other things, and we had additional expenses, and the rates were moving up, and just that getting that everybody on board, so we do think we'll be able to make up a good chunk of that with the leasing group.

Then there's some expenses that go away on that side. We've identified some expenses on our side. Things like overtime and things like that that we can think we can control a little bit more. So we've identified some expense things, and then just through normal products and services that we have. Chuck has led a revenue-enhancement project team that -- and they've come up -- we had people from all over the bank and they've come up with some dollars there as well. So I would say maybe half of it's going to come from the leasing side and then the other half from revenue enhancements and from expense saves. And that's my best guess right now. Again, we're working through the budget, so -- but that's our best guess right now.

Daniel Cardenas: Right, right. And do you think that this is -- that the timing on this can be done in 2024, or do you think that's going to take until '25 before you kind of hit full stride there?

Dennis Shaffer: No, we think we can get that -- we want to -- so some of things involve sending disclosures and things like that. Those are really set to go out in December, so we hope to be hitting the ground running in January with a lot of this.

Daniel Cardenas: Wonderful. Good, good. And then just jumping over to the balance sheet quickly, can you give me some color as to how much of your securities portfolio is scheduled to mature here in the fourth quarter? And how would those proceeds be put to work, on the lending side? Or do those get put back into the securities portfolio?

Richard Dutton: A little bit of both. I'm trying to get to the page. So we're scheduled for, what, almost $30 million that will mature in the next quarter, in the fourth quarter, and probably two-thirds or -- yes, two-thirds of that is at our investment subsidiary. Those proceeds, when they mature, probably stay in the investment portfolio. We've got another third of that that's in the bank and when those -- and they have been maturing over the course of the year -- as those mature, those are used to fund loans and/or pay off borrowings.

Dennis Shaffer: And Rich and I were just talking about some of that, Dan, too, even at the investment sub. There are certain tax implications. We're going to run the math and see what those tax implications are, because it may be better for us just to utilize those funds to fund some of this loan growth and stuff, or pay down borrowings, or stuff like that. So we're running -- we're working on that as well. We just don't have an answer for you there. But Rich is right; so far, our -- we've said, hey, let's just reinvest those because of the tax implications, but we'll be running the math on that.

Daniel Cardenas: Got it. Okay. Good, good. And then on your -- I mean, credit quality looks good. How are watch list trends directionally -- what were they looking like here into Q3, and what areas are you guys kind of watching a little closer today than you were, say, two or three quarters ago?

Charles Parcher: Yes, Dan, this is Chuck. I mean, knock on wood, our metrics continue to be really stable, and we really feel really good about the portfolio. Obviously, kind of like everybody else, we're really watching office. We don't really have any, per se, any concentration in any downtown office; most of our office is in suburban office, that one-, two-, three-story building in suburbia. So we're not really seeing a lot of strain there yet, but we're watching it closely.

What we're really seeing a lot of, really nice growth, is the multifamily piece across our major metropolitan areas in Ohio. They can't build units fast enough in Columbus, et cetera, so we feel good about that piece of it. All in all, I would tell you that we don't have a lot of concern right now, so like everybody else, we'll watch that a little closer.

Richard Dutton: Yes, and the watch list has been fairly -- the migration there, it's been pretty neutral because we've added a couple, but then a couple have either paid off or upgraded, so it's been -- from a number of loans from a dollar standpoint, it's pretty neutral.

Daniel Cardenas: Okay, good. And a last question from me. What -- how should we be thinking about your tax rate here on a go-forward basis?

Richard Dutton: The effective tax rate for the -- I guess year-to-date was 15.4% and for the quarter was -- it's 15.2%, so I'd say 15% would be what I'd put in my model.

Operator: This concludes our question-and-answer session. I would like to turn the conference back over to Dennis Shaffer for any closing remarks.

Dennis Shaffer: Well, thank you. In closing, I just want to thank everyone for joining, and those that participated in today's call. The interest rate environment continues to be a challenge; however, our earnings do remain strong, our margin remains solid, and I remain optimistic that our disciplined approach to pricing and our solid core deposit franchise will continue to produce superior results, and I look forward to talking to you in a few months to share our year-end results. So thank you for your time today.

Operator: The conference has now concluded. Thank you for attending today's presentation. You may now disconnect.