Event Name: Home Bancorp, Inc., First Quarter 2024 Earnings Call
Event Date: Thursday, April 18, 2024, 11:30 AM Eastern Time

Officers and Speakers
David Kirkley; Chief Financial Officer
John Bordelon; Chairman, President and Chief Executive Officer

Analysts
Graham Dick; Piper Sandler
Brett Rabatin; Hovde Group
Joe Yanchunis; Raymond James

Presentation

Operator: Good morning, ladies and gentlemen, and welcome to the Home Bancorp's First Quarter 2024 Earnings Conference Call.

[Operator Instructions]

Please note this event is being recorded.

I would now like to turn the conference over to Home Bancorp's Chairman, President and CEO, John Bordelon, and Chief Financial Officer, David Kirkley. Mr. Kirkley, please go ahead.

David Kirkley: Thank you, Joelle. Good morning, and welcome to Home Bank's first quarter 2024 earnings call. Our earnings release and investor presentation are available on our website. I'd ask that everyone please refer to the disclaimer regarding forward-looking statements in the investor presentation and our SEC filings.

Now I'll hand it over to John to make a few comments about the first quarter. John?

John Bordelon: Thanks, David. Good morning, and thank you for joining Home Bancorp's earnings call today. We appreciate your interest in Home Bancorp as we discuss our strong quarterly results and describe our approach to creating long-term shareholder value.

Home Bank delivered a solid first quarter performance with healthy loan and deposit growth and continued expense discipline. We are quite proud of our accomplishments in the first quarter, as net income was $9.2 million, or $1.14 per share, which generated a return on assets of 1.11%.

Loans increased $40.1 million over the quarter, or about 6% annualized, which is in line with our expectations for 2024. Houston was again a big contributor to our loan growth as we relocated an acquired branch and opened an LPO to house the commercial team we brought on board in the fourth quarter. We will be relocating an additional branch next week in Houston as we continue to invest in our markets and seek ways to drive additional activity.

First quarter deposits increased $52 million, following a $73-million increase in the fourth quarter. Deposits have increased by 6.4% since March 31 of last year, which we feel very good about considering everything that's happened in the banking industry in the last 12 months. Our loan-to-deposit ratio came down slightly to 96.3, which is still a little above the upper end of our target range.

As we indicated last quarter, we saw some additional pressure on the net interest margin, which decreased to 3.64% in the first quarter. While the last couple of weeks has made predicting rates challenging, we continue to expect them to stabilize around this level in the next two quarters.

With that, I'll turn it back over to David, our chief financial officer.

David Kirkley: Thanks, John. Net interest income totaled $28.9 million in Q1, a slight decline of $381,000 from the previous quarter, as deposit costs continued to put pressure on NIM.

The pace of deposit migration is certainly slowing, but we are still seeing customers move funds out of savings, checking and non-interest-bearing deposits into higher-yielding CDs and money market accounts. The 26-basis-point increase in yield of interest-bearing deposits during the first quarter was less than the 40-basis-point increase in the fourth quarter and 54-basis-point increase in the third quarter, so it does appear that the pace of increase is slowing. As deposit migration slows and the spread between new CD origination rates and the rate of the existing CD portfolio narrows, we should continue to see smaller increase in deposit costs.

Page 11 and 12 of our investor presentation provides some additional detail on credit.

Non-performing loans increased by $11.5 million in the first quarter to $20.3 million, primarily due to two relationships totaling $9.6 million. The first relationship has loans totaling $4.6 million and is secured by a portfolio of residential investment properties with an LTV in the 65% range, and we expect minimal, if any, losses. The other relationship is about $5 million and was included in the 90 days past due and still accruing bucket, which is not a category we utilize very often. It's a small multifamily construction project that was waiting for its certificate of occupancy, which was just received yesterday. We expect the sale of two units totaling $970,000 to close tomorrow and a couple more units to close this month.

Our allowance for loan loss ratio was 1.2%, down 2 basis points from the prior quarter. The decline in this ratio was due to the migration of CD loans into permanent loans and CECL. There were no changes in our qualitative factors during this quarter and we feel confident in our reserve levels.

Slide 16 has some detail on our historic NIM and its components. As John mentioned, NIM declined by 5 basis points in the first quarter but appears close to stabilizing.

Slide 17 has our current and historic deposit beta statistics and shows that our cost of total deposits in Q1 was 1.82%, with a cycle-to-date beta of 32%. At 1.95%, our cost of funding earning assets was 35% of the upper limit of the Fed funds target range of 5.5%.

Loan growth picked up in the first quarter to $40.1 million with an average origination rate of

8.23% during the quarter. Our loan pipeline remains strong, and we continue to expect 4% to 6% growth in 2024, but recognize that Fed activity could impact both growth and yields.

Slide 18 of the presentation has some additional details on non-interest income and expenses. Non-interest income was stable in the first quarter at $3.5 million. Non-interest expense increased slightly to $20.9 million but still came in below our forecast due to lower-than-expected compensation expenses and several T&E projects being pushed further into 2024. Annual salary increases took effect April 1, and we expect core non-interest expenses to be around $22 million to $22.5 million in the second and third quarters.

Slide 19 summarizes the impact our capital management strategy has had on Home Bank over the last few years. We've grown adjusted tangible book value by 55% since 2018, increased our dividend by 67% since 2016 and repurchased 13% of our shares, all while maintaining robust capital ratios. This positions us to be successful in any economic environment and take advantage of opportunities as they arise.

With that, operator, please open the line for Q&A.

Questions & Answers

Operator: [Operator Instructions]

Your first question comes from Graham Dick with Piper Sandler.

Graham Dick: I just wanted to start on -- call out those two credits in the press release that moved to non-accrual this quarter. It doesn't sound like you guys are expecting much loss there, but I just wanted to know a little more color around industry, type of credit, and what sort of gives you confidence that you might be able to move these out of the bank without having to really charge anything off?

John Bordelon: Well, the first credit that David described is a situation where there are five partners, and one of the partners has kind of turned against the other four. There are, I think, 15 properties -- I'm not exactly sure how many properties -- in a very, very strong location, next to Tulane University, and they're all leased and such, but they stopped paying us for some dispute that they're having internally.

We have sent a 30-day letter. We have started foreclosure proceedings. The four individuals on one side are trying to find a way to not lose the $2.2 million of equity that they have in the project. As far as our concern, is that if they don't update this and bring it current, we'll probably, third quarter, end of third quarter or so, have a sheriff's sale, at which time I think we'll have no trouble selling it. So it's really about a dispute. It's not -- the properties aren't bad. They're all in very good shape. They're all leased. It's just a problem with the partners.

The second project really was a situation where, cost overruns and such, the borrower ran out of funds for the most part. The project is finished; it has its ability to sell. We have two sales tomorrow for $970,000; that will bring all the interest current and also reduce principal by about

$750,000. There are two additional sales that will happen before the end of the month, so we feel as though that one will take care of itself now that they've gotten their certificate of occupancy and can start selling the properties.

So I would anticipate one of those being off of classified by next quarter, the large one being off. The other one's just going to take until they decide to work together or until a sheriff's sale. But no losses on either one.

Graham Dick: Okay, that sounds good. All right, and I just wanted to kind of turn to the NIM. I think last quarter you guys had hoped that, obviously, there would be maybe a little downside this quarter, but then stabilize into 2Q and sort of drift higher from there. How do you feel about the way that outlook might be evolving given what you're seeing on the rate outlook in the Fed right now if you were to only get one, two, maybe no rate cuts this year?

David Kirkley: Yes, I think Q2 is probably going to be a much more stable NIM for Home Bank. Our deposit costs are kind of starting to peak out, where I mentioned earlier on the call that the way -- the spread between our CD portfolio and the rate at which we're putting on CDs right now is narrowing very quickly, so you're not going to see that rapid rise in deposit costs that we have been experiencing.

We've also looked at kind of the migration from customers, retail customers specifically, that have been moving funds out of checking accounts into money markets and CDs over the past couple quarters, and that pace has slowed significantly. So it's almost as if the people that were looking for rates or -- have found them, and that outflow into higher-yielding deposit products is slowing, and the pace at which CDs are pricing higher has slowed significantly.

On the flip side, we are seeing some success in our loan portfolio. As I mentioned, weighted average rate of originations was 8.23%, so that's starting to offset the increase in liability costs as well. So we feel good about a slight decline to stability in NIM in Q2.

Graham Dick: Okay. And then as you just sort of look ahead, do you think that there's a chance that, as these deposit costs continue to top off and new loan yields come on at higher rates, given no change to Fed funds rate, do you think the NIM could still tick higher, I guess, in the back half of the year? Is that a possibility?

David Kirkley: I think the pace would be slower, but yes, I think it's a possibility that it could tick higher, for sure.

Graham Dick: Okay. Okay, great. And then I guess just one more from me is on loan growth. It came in with -- inside your guidance of mid-single digit, but still a good start to the year. Do you expect the Houston team to continue to do the heavy lifting there, for the rest of the year? And if so, what are you sort of seeing in your legacy markets that are maybe holding back growth there a little bit?

John Bordelon: I think all the markets will flow as the year goes on somewhat, especially if rates stay where they are. The treasury going up, I think, yesterday, to 4.6% or whatever, but -- so there is a slowdown, but we have a lot that's in the pipeline right now, some C&D that's starting to build out a little bit, so I think you'll -- at the end of the day, I don't know that we'll finish fourth quarter, if rates are where they are today, with the type of quarter that we had in the first. I think you'll see a diminishing growth rate. Now, [indiscernible] changes, Fed does reduce rates two or three times, that could change a lot.

Operator: Your next question comes from Brett Rabatin with Hovde Group.

Brett Rabatin: Wanted to go back to credit, and if I look at Slide 11, the total substandard -- and granted, your criticized assets are still at very, very low levels, but I saw that the substandard bucket moved up about $7 million, linked quarter. I was just curious what you were seeing in terms of migration in or out of the substandard bucket in particular, and then just any industries or things that you're seeing incrementally where maybe there's pressure either on revenue or just overall sales.

John Bordelon: I think the general thought for Home Bank that 2024 will continue as '23 did in reducing classified assets. These two one-offs that we discussed momentarily are really not because of the economy as much as it is just mismanagement a little bit in the project. So I don't anticipate that continuing throughout '24. I would anticipate those classifieds coming down as they did toward the end of the year. So we're not seeing any sign that there's a wave of bad assets coming our way.

David Kirkley: Outside of the two credits that we mentioned, there was a little bit of a migration in from a mix between some residential properties, some small CREs, some very small C&I, as well as some outflows that basically were the exact same thing, some residential, some small CRE and some various payoffs. So they kind of -- they're washing each other out right now.

Brett Rabatin: Okay. And then from a capital perspective, your ratios are building a little bit; you bought back a little bit of stock; any thoughts on the level of buyback activity from here? And then are you going to keep, maybe, some powder dry for potential M&A, or do you kind of feel like M&A is less likely with higher marks, given where the 10-year has moved?

David Kirkley: We're going to be picking up -- picking back up our buybacks a little bit more in Q2. We did start a little bit in earlier part of Q1, but it's kind of a balancing act of, one, keeping the powder dry, and two, buying back at the levels that our stock is trading at today.

Brett Rabatin: Okay. And any comments [indiscernible] --

John Bordelon: One other point in that regard, we had kind of pulled off of the buybacks. We were engaged in a potential purchase of some branch locations from another bank, and that was very much in line to be announced yesterday, and unfortunately, another bank came in and -- what we felt was a little bit on the high side, price-wise. But anyway, the seller basically reneged on us three days before closing and took another bank. So that was one of the reasons that we stopped the buybacks about 60 days ago, for the most part.

Brett Rabatin: Okay. That's helpful. And then just lastly, any comments on -- I think, if I have this right, you still want to migrate the loan-to-deposit ratio a little lower, so just, how do you fund the loan growth from here? Is it CDs? It's good to see the DDA was kind of stable this quarter. Any thoughts on how you fund growth?

John Bordelon: Well, I think our focus completely is on C&I customers, and with that comes the deposit relationship. We're trying to get away, right now, from non-owner-occupied CRE, just from the standpoint that it doesn't bring the deposits. So bringing in the whole customer is extremely important to us, and that's going to help us maintain the DDA level that we have acquired and/or attained up till this year. So even though some of those balances moved when rates started going up into CDs, we still are ahead of where we were pre-pandemic as a percent of total deposits in DDAs and savings accounts. So we're going to continue to drive the C&I portfolio much more so than anything else, and that will help with that deposit mix. We'd love to get that down to, you know, 92%, 93%, something like that.

Operator: [Operator Instructions]

Your next question comes from Joseph Yanchunis with Raymond James.

Joe Yanchunis: I was hoping to start with kind of -- I'd say it sounds like the cost of interest-bearing deposits may have peaked, kind of based on what you had said earlier. So if we assume the forward curve, do you have a sense for how deposit betas will behave when the Fed starts cutting rates?

David Kirkley: So I don't want to use the word "peak" because I still think that it's going to continue to drift up a little bit, but just at a much slower pace. So there is still some low-hanging fruit out there, so there's still going to be some upward migration in deposit costs, but it's slowing -- it's coming down pretty -- the pace of increase is slowing.

As far as the deposit betas, when rates start ticking down, I think a lot of banks are going to be, one, anxious to lower rates, but a lot of loan-to-deposit ratios are not where people want to -- banks want to be, and customers are getting used to 5-handles on their CDs, which will force those customers to be a little bit -- shop a lot more. So I think the -- a 25- or 50-basis-point rate cut is going to -- the beta is going to eventually going to work its way out to a normalized beta, but I think it might take a little bit longer to play out as customers continue to fight for higher rates.

Joe Yanchunis: Got it. I appreciate that. And the Houston market continues to generate strong loan growth, so with 18% of loans being in Texas, do you have a medium-term target for how large you'd like to grow that portfolio?

John Bordelon: No, we do not. We think it's a tremendous market, and the people that we have there, including the new group that we've pulled out in the fourth quarter, are doing a great job of staying in the arena that we want to play in. So I know a lot of banks complain about going to Texas and you have to play big to get anything; we're not seeing that. The talent that we have there is keeping it in the type of portfolio, type of loans that we're searching for, and doing a very good job, and doing it at a high volume, so we're very excited about what's going on there.

And unfortunately, we didn't get the M&A deal that we wanted to help us expand in the Houston market, but I'm sure there will be other opportunities in that market to come.

Joe Yanchunis: Okay. And then last one from me here. So we've heard from a lot of banks this earnings call that their outlooks call for an acceleration in loan growth throughout 2024, but kind of based on your reiterated outlook, it seems like, for it to reach the high end of your guide, that loan growth would remain stable. Do you have a sense for why there's a disconnect there?

John Bordelon: No, I really don't. I think if -- we probably wouldn't be so optimistic without our Houston franchise. Things are slowing a little bit more in Louisiana than they are in Texas. But I do believe every market is slowing to some degree, but Texas is keeping us propped up. So that's the only explanation I can find.

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

John Bordelon: Once again, thank you all for joining us today. We look forward to speaking to many of you in the coming days and weeks. Thank you for your interest in Home Bancorp. Hope you have a wonderful day.

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